

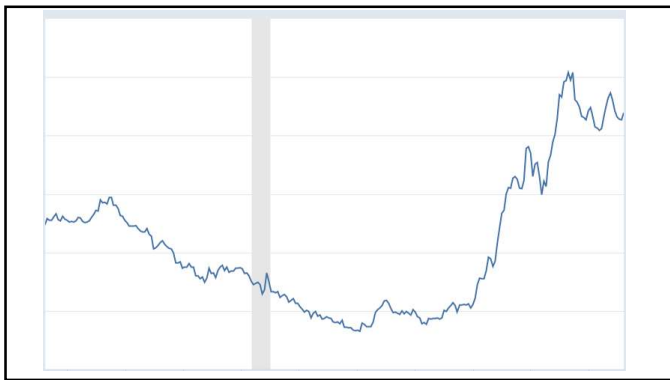
Seller Financing Scenarios

MLTA Spring 2023 Education Seminar

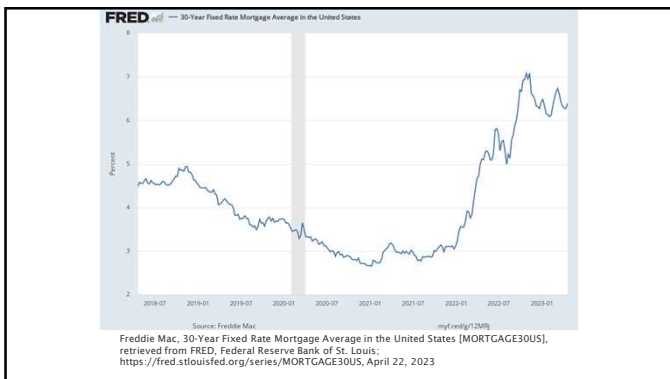
Presented By: Adam Stricker, Sr. Underwriter
May 18, 2023



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Free and Clear Properties

Seller Carry-Back Mortgage

- Buyer = Mortgagor, Seller = Mortgagee
- Insuring Transactions Involving Seller Carry Mortgages
 - Exception for Mortgage on Owner's Policy
- Before Issuing Loan Policy
 - Properly drafted documents (Mortgage, Promissory Note, etc.)
 - Who will draft documents? Legal advice?
 - Extended Coverage and/or Endorsements?

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Free and Clear Properties

Seller Carry-Back Mortgage, Continued

- Pros of a Seller Carry-Back Mortgage
 - Sale without conventional financing or down payment
 - Financial benefits to Seller/Mortgagee
 - Future Judgment Liens will be subordinate

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Free and Clear Properties

Seller Carry-Back Mortgage, Continued

- Cons of a Seller Carry-Back Mortgage
 - Loan Servicing (i.e., collecting payments, dealing with taxes and insurance)
 - Judicial Foreclosure
 - Mortgagee must directly release upon payoff

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Free and Clear Properties

Seller Carry-Back Deed of Trust/Trust Indenture

- Buyer = Grantor, Seller = Beneficiary, Trustee = ?
- Trustee must be:
 - Attorney licensed to practice law in Montana
 - Bank, Trust Company or S&L authorized to do business in Montana under the laws of Montana or the U.S.
 - Title Insurer, Title Insurance Producer or Title Agency authorized to do business in Montana under the laws of Montana
- Property encumbered must be 40 acres or less

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Free and Clear Properties

Seller Carry-Back Deed of Trust/Trust Indenture, Continued

- Pros and Cons are similar to a Mortgage
 - Non-judicial power of sale
 - Trustee can reconvey when directed by Beneficiary
 - Beneficiary may appoint Successor Trustee
 - Title Companies can directly release (M.C.A. § 71-1-308)

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Free and Clear Properties

Conventional Financing with Seller Carry-Back

- Majority of purchase price is funded with conventional financing and remaining balanced is carried by Seller via a junior Mortgage/DOT
- If insuring Seller Mortgage/DOT, add Exception for 1st Loan
- Require express subordination of Seller Mortgage/DOT via recorded Subordination Agreement. Do not rely on recording order alone!

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Free and Clear Properties

Dodd-Frank and CFPB Rules

- Under Rules adopted in 2014, anyone arranging a consumer credit transaction secured by a dwelling must be a registered and licensed mortgage originator
- Three Property Exclusion (per year)
 - Seller (individual or entity) must have owned the property
 - Seller did not construct or act as contractor
 - Loan must be full amortizing (i.e., no balloon payments)
 - Fixed Rate or ARM with fixed rate for first five years
 - Good Faith determination that consumer has ability to repay

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Free and Clear Properties

Dodd-Frank and CFPB Rules, Continued

- One Property Exclusion (per year)
 - Seller must be individual, trust or estate
 - Seller did not construct or act as contractor
 - Repayment schedule cannot include negative amortization
 - Fixed Rate or ARM with fixed rate for first five years
- TRID Disclosure Rules do not apply to “creditors” who make five or fewer loans per calendar year
- Montana law does not appear to require TRID disclosures for seller financed transactions (M.C.A. § 32-9-103 and 148)

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Free and Clear Properties

Contract for Deed Transactions

- Buyer receives equitable title and Seller retains legal title
- Insuring a Contract Buyer
 - Easiest is “Indirect Method”
 - Schedule A shows Fee Title vested in Seller
 - Buyer is named as Insured
 - Record Notice of Purchaser’s Interest
 - Exception for Terms and Conditions of unrecorded Contract for Deed as evidenced by recorded Notice of Purchaser’s Interest

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Free and Clear Properties

Contract for Deed Transactions, Continued

- Pros of a Contract for Deed
 - Sale without conventional loan underwriting or down payment
 - Allows for sale of unusual property or property that would not otherwise qualify for a conventional loan
 - Buyer may use and occupy the property while making payments

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Free and Clear Properties

Contract for Deed Transactions, Continued

- Cons of a Contract for Deed
 - Encumbered properties may be subject to due on sale clause
 - Long-Term Escrow Issues
 - Default and Forfeiture
 - Judgment Liens against Buyer and Seller are *problematic*

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Existing Encumbrances

Lender Approved Assumptions

- Buy-Sell will indicate an Assumption
- Require Assumption Statement which discloses current loan balance and all fees associated with the assumption
- Require recording of Assumption/Modification Agreement
- Exception in Owner's Policy for existing Mortgage
 - Assumption Agreement as a Note

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Existing Encumbrances

Lender Approved Assumptions, Continued

- Continuing coverage for the Lender
 - ALTA 11 or CLTA 110.4/110.5/110.6 to insure Modification
 - Date Down endorsement to bring Policy Date forward
 - CLTA 111.4 to insure Mortgage Impairment after Conveyance (New as of 8/4/22)
- Also consider brand new Loan Policy insuring original Mortgage and Assumption in Schedule A
 - Simultaneous rate may be less expensive than endorsements

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Existing Encumbrances

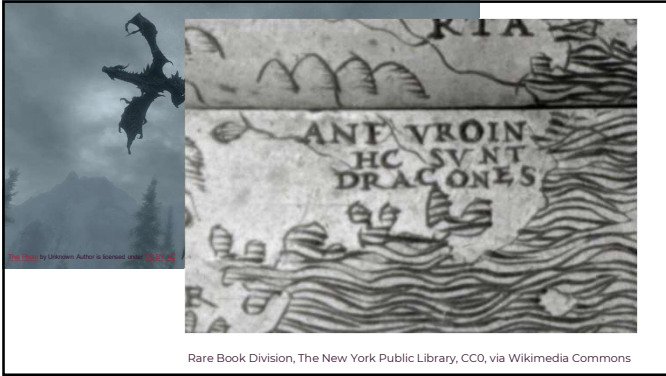
Lender Approved Assumptions, Continued

- Pros and Cons for Lender Approved Assumptions
 - Less rigorous qualification process for Buyer
 - Possible below market interest rate even if lender requires increase
 - Seller may remain personally liable on existing indebtedness
 - May affect Seller's future eligibility for loan benefits

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Existing Encumbrances
Silent Assumptions

- Buy-Sell may or may not indicate the Silent Assumption, but purchase price may be a clue
- Due on Sale Clause
- Recommendation: Disclaimer/Indemnity from Buyer and Seller and Status Letter or Payoff Statement. Legal advice?
- Exception in Owner's Policy for existing Mortgage/DOT

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Existing Encumbrances
All-Inclusive Mortgage/DOT aka "Wrap"

- Hybrid of Seller Carry-Back and Silent Assumption
 - Existing Mortgage/DOT is left in place and Seller carries back a 2nd position security instrument which "wraps" the existing 1st
 - Any Loan Policy for the Wrap DOT must contain an Exception for the 1st. Owner's Policy should contain an Exception for both
 - Same Due on Sale, Disclaimer/Indemnity and Legal advice concerns as a Silent Assumption

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Existing Encumbrances

All-Inclusive Mortgage/DOT aka "Wrap", Continued

- Recent Claim Scenario
 - Purchase Money DOT in 2002
 - 2nd Position DOT in 2003 with home as extra collateral for a business loan
 - 2nd Position Lender forecloses in 2006 and takes title subject to existing 1st DOT

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Existing Encumbrances

All-Inclusive Mortgage/DOT aka "Wrap", Continued

- Recent Claim Scenario, Continued
 - In 2009, 2nd position lender sells to LLC. Sale is financed via Seller Carry-Back DOT which wraps existing 1st DOT from 2002. Wrap DOT is expressly identified as such on its face and sale and loan are insured by Title Company #1
 - In 2019, Members of the LLC convey to themselves, individually, and refinance. Loan transaction is insured by Title Company #2

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Existing Encumbrances

All-Inclusive Mortgage/DOT aka "Wrap", Continued

- Recent Claim Scenario, Continued
 - In 2021, individual owners refinance again. Title Company #3 identifies 1st position DOT from 2002, but decides to insure over without underwriting approval
 - 1st position DOT goes into foreclosure in December of 2022

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Existing Encumbrances

All-Inclusive Mortgage/DOT aka "Wrap", Continued

- Recent Claim Scenario, Continued
 - 2009 Owner's Policy contains a Schedule B Exception for the 2002 DOT
 - However, Title Company #3 must defend its 2021 insured DOT
 - Moral of the Story: Read the documents!

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Existing Encumbrances

"Subject to" Sales

- Different variations of a Silent Assumption transaction
- Due on Sale Clause and Legal advice concerns
- Exception in Owner's Policy for existing Mortgage/DOT
- Disclaimer/Indemnity recommended and consider requiring other written disclosures from the parties

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Existing Encumbrances

"Subject to" Sales, Continued

- Simplest version is a Silent Assumption without any additional funds paid on top
 - Buyer takes over payments on existing Mortgage/DOT while preparing to fix and flip
- If Seller has defaulted on their loan the "purchase price" may consist of the Buyer paying the amount needed to bring the loan current

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Existing Encumbrances

“Subject to” Sales, Continued

- In other variations, the Buyer will target Sellers that are not in default, but want to dispose of the property quickly
 - Divorces, Military, Incarcerated, etc.
 - Little to no consideration paid and Seller gives Buyer authorization to communicate with existing Lender
 - Buyer attempts to fix and flip property before it goes to foreclosure sale
 - Require full disclosure that Buyer will not make payments

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Existing Encumbrances

“Subject to” Sales, Continued

- In scenarios where purchase price is cost to bring loan current the Buyer may lease the property back to Seller subject to existing Mortgage/DOT
 - If Seller defaults on lease, Buyer evicts and sells
 - Prohibited in other states, but no apparent restriction in Montana

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Bonus Materials (Time Permitting)

“Wholesale” aka Assignment of Contract

- Buyer goes under contract with Seller at a below-market price with little to no earnest money
- Buyer markets property for sale to third-parties at higher price
- Original contract is assigned to third-party buyer and Buyer is paid an “Assignment Fee” equivalent to the difference in price
- Recommendation: Full Disclosure, in writing, to Seller and Assignment Fee shown as line item on Settlement Statement

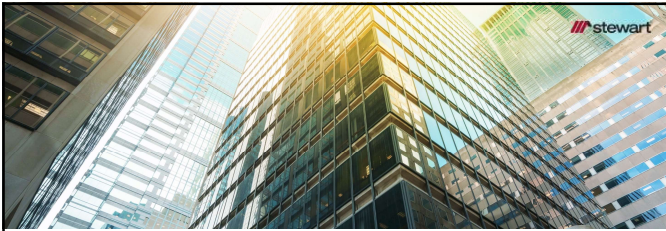
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Bonus Materials (Time Permitting)

Double Sale aka "ABC Closing"

- Seller ("A") goes under contract with Buyer ("B") at below-market price with little to no earnest money
- Buyer ("B") goes under contract with third-party buyer ("C") at higher price
- AB Sale and BC Sale close simultaneously or same day and B uses Buyer C's funds to pay Seller A while retaining difference

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Questions?



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