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Dodd-Frank Act: government overreach into private real estate

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As of Jan. 21, the Dodd-Frank Wall Street Reform and Consumer Protection Act began regulating all residential real estate transactions in the U.S. This new law will have a negative effect on Florida's real estate economy and will alter what has traditionally been an accepted procedure — private seller financing.

Private seller financing, sometimes referred to as "purchase money financing" or "carry back financing" is where a private seller transfers title to property and accepts a mortgage for a substantial part of the sale price rather than receiving all cash on the sale.

Private seller financing historically has been beneficial for buyers and sellers and Florida's economy. For example, a couple who invested in a residential property and paid off the underlying mortgage decides it would be a better return for their retirement if they sell the property and carry back a purchase money mortgage.

By receiving payments from the buyer over the next few years, the seller would not receive all cash and the immediate tax impact and would have a higher return on their money than if they invest in treasuries or certificates of deposits offered by banks. Buyers who cannot qualify for an institutional mortgage can nonetheless acquire title using seller financing.

Most home mortgages are amortized over 30 years, allowing for reasonable monthly payments. In a private seller financing scenario, a 30-year amortization is generally used with a balloon payment after three, five or 10 years, as the private seller does not want to carry financing for 30 years.

Even though Florida law provides adequate notification to a purchaser of a balloon mortgage and requires a notification to parties accepting financing with balloon mortgages, Dodd-Frank overrides Florida law and eliminates the ability of private sellers to utilize a balloon mortgage.

Additionally, Dodd-Frank eliminates the ability of a small homebuilder to construct a home and sell that home to a third-party purchaser without the use of institutional financing. Dodd-Frank drives the private market to institutional financing, benefitting banks at the expense of the private seller.

Some of Dodd-Frank's restrictions on private seller financing of residential property are:

• The seller cannot have constructed the home.

• The seller must determine the buyer has reasonable ability to repay the loan.

• The loan must have a fixed interest rate for a minimum of five years.

• The loan must meet criteria identified by the Federal Reserve Board.

The small homebuilder has no ability to sell its homes using purchase money financing and the couple who wanted to sell their property as a retirement investment cannot do so unless they want to hold the mortgage loan for an impractical period of time.

Dodd-Frank was touted as regulating “Wall Street,” but actually benefits institutional lenders at the expense of “Main Street” by making it illegal, or at least completely impractical, for private sellers to get a decent return on their investment.