Regulations Bring Change to Hard Money Deals

Although the new standards may be arduous, lenders still should thrive in the post-TRID world

By Yanni Raz

The new integrated-disclosure rule known as TRID is excellent for consumers but also laborious for lenders. It will consequently have some short-term negative impact on lenders, including some hard money lenders — although in the longer term, it promises to offer benefits as well.

Any hard money lender who makes five or more loans a year may need to include details of construction-only and bridge loans in the new disclosure documents. The determination of whether a hard money loan is subject to TRID — also known as the Truth in Lending Act (TILA) and Real Estate Settlement Procedures Act Integrated Disclosure rule — will depend on the facts of the deal, but generally the new rules will apply to any mortgage loan in which the proceeds are used by the borrower primarily for personal, family or household purposes.

What the new TRID regulations mean is that affected real estate deals will be a great deal more transparent for the client, and somewhat more work for the investor or lender.

Yanni Raz is CEO of HML Investments and has been a hard money lender for more than 10 years. Raz was a real estate broker for five years before he partnered with a group of investors from California and began assisting real estate investors in financing commercial and residential projects. He writes about real estate financing for magazines, blogs and other online news outlets. Reach Raz at yanni@hmlinvestments.com or (818) 308-4443. Visit lioncrestfunding.com, hmlinvestments.com and facebook.com/Hard.money.lenders.CA.

In a pre-TRID world, hard money lenders simply required a note and a deed of trust. Other documentation requirements varied but generally included a personal guarantee from the borrower, personal financial statements — such as past tax returns and proof of income — and assurance that the borrower had the funds to rejuvenate and maintain the property. The burden of proof rested largely on the borrower.

Under TRID, which took effect this past October, lenders have to engender trust by showing their calculations to clients.

New documents

As part of the new guidelines, a lender making a residential real estate loan must submit to the client two new forms. They are the Loan Estimate and the Closing Disclosure — which is a statement of final loan terms and closing costs. The client has to receive these forms within a certain timeframe, and the loan can only be finalized once the client understands and is satisfied with the lender's numbers and decisions.

The upfront Loan Estimate form uses simple language to summarize the Good Faith Estimate and TILA-disclosure requirements for the client and explains the loan's key features, costs and risks.

The Closing Disclosure form, provided near the end of the mortgage process, summarizes the final TILA and loan-settlement statements. Again, this form uses language that is easy to understand and provides the borrower with a detailed accounting of the entire transaction — including projected monthly payments, fees and other costs.

The lender is responsible for preparing the Closing Disclosure form — although a qualified settlement agent may handle that task in some cases. The form also contains additional new disclosures required by the Dodd-Frank Wall Street Reform and Consumer Protection Act as well as a detailed accounting of the settlement transaction.

The 2,000-page TRID-instruction manual also outlines other regulatory requirements and includes instructions informing the lender how to format and word the Loan Estimate and Closing Disclosure documents.

New deadlines

TRID requires that borrowers be provided with the Loan Estimate form at least three business days after applying for a loan — which means at least three business days after borrowers provide the lender with details such as their name, income, Social Security number, property address and the mortgage amount sought.

Borrowers must receive the Closing Disclosure at least three business days before loan consummation. Any significant changes to the loan terms — such as an interest-rate increase of more than 0.125 percent for fixed-rate loans or 0.25 percent for adjustable-rate loans; a prepayment penalty; or changes in the loan product — will cause the three-day interim period to start again.

In short, lenders should prepare their borrowers for at least a 14-day wait before a mortgage can legally go to closing — and sometimes longer if either the borrower or the lender finds it necessary to delay the closing. Finally, until borrowers have received and reviewed both TRID forms and agreed to proceed, the only fee lenders can impose is a reasonable charge for obtaining a consumer's credit report.

Continued >>

<< Continued

Lender preparation

Hard money lenders making loans that may be affected by TRID should review policies and procedures, in addition to changing the way they track and modify disclosures. Pre-application estimates, compliance tests and reporting requirements will be affected by the rule.

Hard money lenders also are advised to prepare clients for the changes. Lenders and clients may experience confusion and delay with documents and procedures, and some lenders may find they have to hire additional personnel to fulfill the requirements.

Lenders must keep the new TRID timelines in mind when drawing up contracts — to coordinate closings carefully and to avoid last-minute changes. Lenders also should encourage their clients to thoroughly review the documents and to disclose all concerns. Initially, affected hard money loans and purchases may take longer to close. Lenders should explain the situation to their clients.

Big picture

Some in the mortgage industry have lambasted TRID, declaring that it will escalate loan-processing costs across the industry by billions of dollars. They contend the new rules will result in delayed closings, frustrated clients and general confusion as industry players adjust to the changes.

It is true that mortgage originators, including some hard money lenders, may have to cope with longer timelines and delayed closing dates because of TRID. In the long run, however, the reality may not be so bad. Lenders may initially find themselves with more work and a somewhat larger technical hurdle to conquer, but TRID also could wind up benefiting loan originators, including hard money lenders, as much as it benefits the borrower.

Unfortunately, hard money lending is not well understood outside the industry, including by many borrowers on the residential side, and that can make it intimidating. The new loan-documentation requirements, however, could lead to stronger customer-lender relationships as a result of the lender explaining the new forms, being upfront with the borrower about consumer-protection guidelines and clarifying the myriad loan details.

TRID also could help to transform the loan experience for the borrower from a paperwork nightmare, with piles of opaque documents to review and sign, into a more manageable exercise. TRID simplifies loan documentation, clarifies loan terms and fees, and avoids unpleasant surprises at the end.

In the big picture, therefore, TRID may well be a blessing in disguise for hard money lenders. ■