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Navigating the complexities of seller financing in Maine - by Jessica Estes

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Today's interest rates, underwriting standards, and financing timelines can often be an obstacle in closing a real estate transaction.

Once the buyer and seller agree on the price and terms for the real estate sale, the broker usually introduces the buyer to commercial lenders to help with financing. This process can be challenging for buyers unfamiliar with such transactions.

The buyer may be unable to secure satisfactory financing due to any number of the following factors:

- The property will not appraise.
- The buyer does not have sufficient credit established.
- Current interest rates are too high (they have more than doubled in a year!).
- The buyer needs to close before the bank's timeline to complete the loan process.

As brokers, we are there to assist the buyer in overcoming these obstacles and bringing the transaction to a close. When traditional lending is either not desirable or not possible, seller financing can play a pivotal role.

What is seller financing?

It is when the seller holds the mortgage on a property they are conveying to a buyer. This can take many forms, but for this article, we will assume there is a straightforward arrangement.

Sellers are often willing to "hold paper" in a transaction. Often it enables them to defer their capital gain taxes on the sale, allows them to take the property back in the event of buyer default, and the transaction can close significantly faster than with traditional financing.

The buyer may also not have to put as much equity into the front end of the deal, saving cash for property repairs or upgrades if necessary.

What are the risks?

For the buyer:

- If the seller has a mortgage and defaults on payments, the property can be foreclosed on.
- Traditional financing will force the buyer to take numerous steps to ensure the property is worthy of the mortgage including an environmental assessment and appraisal. The buyer can be exposed if this is not done for a seller-financed deal.

- The interest rate may be higher than a standard commercial mortgage, other terms of the loan could vary from commercial lending norms as well on the creditworthiness of the buyer, the state of the property, and the seller's preferences.

For the seller:

- The buyer may default and may also leave the property in disrepair.
- Capital gains are deferred, not eliminated, and tax liability may be higher at the time of the gains being realized.
- Foreclosing can be an expensive and time-consuming process.

If you are considering seller financing, make sure you have an experienced commercial real estate attorney who can write up and or review the documents. This is a complex transaction element that requires experience and capability to protect you and your assets.

As always, make sure you have a real estate broker working on your behalf who understands how to navigate these transactions.

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