



When Must a Lender Send a

BALLOON PAYMENT

Notice?



Cathy K. Robinson, Esq.
Wright, Finlay & Zak, LLP



T. Robert Finlay, Esq.
Wright, Finlay & Zak, LLP

Loan servicers know which loans require a balloon payment notice; but many private lenders servicing their own loans have no idea whether a balloon payment notice is required and, if it is, when it must be sent. This article is intended to help these private investors identify when a balloon payment notice is required.

What Loans Require a Balloon Payment Notice?

If the answer was as easy as – any loan with a balloon payment at the end of its term, this article would be very short. But there is more to it than that.

California has two mutually exclusive statutes that govern when a balloon payment is required – Civil Code §§ 2924i and 2966. Fortunately, both sections define a “balloon payment” the same: “a final payment as originally scheduled which is more than twice the amount of any of the immediately preceding six regularly scheduled payments or which contains a call provision” that is actually exercised. After the initial definition, the statutes diverge.

Section 2924i applies to residential loans for a period of longer than one year, secured by a deed of trust on real property containing one to four residential units, of which at least one is occupied by the borrower (or was intended to be owner occupied) at the time of loan origination. It specifically excludes open-ended¹ and construction loans.

Meanwhile, § 2966 applies to seller carryback loans used to purchase a dwelling for not more than four families, involving an “arranger of credit” (typically a real estate broker).

When Must the Balloon Notice Be Sent to the Borrower?

If a loan qualifies as a balloon payment loan, both statutes require that the lender provides a notice of final payment to the borrower at least 90 days, but no more than 150, before the final payment is due. The notice must include:

“(1) A statement of the name and address of the person to whom the final payment is required to be paid.

- (2) The date on or before which the final payment is required to be paid.
- (3) The amount of the final payment, or if the exact amount is unknown, a good faith estimate of the amount thereof, including unpaid principal, interest and any other charges, such amount to be determined assuming timely payment in full of all scheduled installments coming due between the date the notice is prepared and the date when the final payment is due.
- (4) If the borrower has a contractual right to refinance the final payment, a statement to that effect.”²

Unique Scenarios to Consider

In most instances, whether a loan requires a balloon payment notice is pretty straightforward; however, there are a few unique scenarios to consider:

- **Extended Bridge Loans.** By definition, bridge loans must mature in less than a year and, as a result, do not require a

continued on page 12

balloon payment notice. Extending a bridge loan past one year should not destroy the bridge nature of the loan or the corresponding protections. However, given that the term of the loan now exceeds one-year, sending a balloon payment notice, while arguably not required, may be prudent.

- **Extended Maturity Date on Balloon Payment Loans.** As discussed in another recent article, accepting a post-maturity payment generally does not extend the maturity of the loan. However, if the lender intentionally extends the maturity date, a new balloon notice is required.³

- **Commercial Loans Modified to Add Residential Property.** If the lender modifies a loan originally secured by commercial property or residential property over four units and then later, modifies the loan to add additional owner-occupied residential property under four units, a balloon notice should not be required. The determination of whether the loan is owner-occupied is made at the time of origination.

- **Modified Fully Amortized Loans.** Again, the determination of whether a loan qualifies as a balloon payment loan is made at the time the loan originates. Therefore, if the loan fully amortizes over the life of the loan, a balloon notice is not required because there is not a balloon payment due. Even if the lender later advances additional funds or adds a delinquency to the “back-end” of the loan, creating a balloon payment at term, a balloon payment notice should not be required. Of course, the lender is welcome to send one as a courtesy.

What Happens If the Lender Fails to Timely Send the Balloon Payment Notice?

Good news! *Failure to send the notice timely does not invalidate the loan but will extend the loan terms via operation of law to a date at least 90 days after the notice date, thus delaying collection on the loan.* However, a willful violation of the statute can result in an award of actual damages and attorney’s fees.

Conclusion

Below is a comparison of the two statutes:

Feature	§ 2924i	§§ 2956–2966
Lender type	Institutional lender	Seller/vendor (carryback financing)
Transaction type	Any residential mortgage loan	Purchase money transactions only
Arranger of credit	Not required	Required
Instruments covered	Deed of trust or mortgage	Mortgage, deed of trust, real property sales contract, lease with option to purchase
Property type	1-4 unit residential, owner-occupied	Dwelling for not more than four families
Construction loans	Excluded	Not addressed
Open-end credit	Excluded	Not specifically addressed
Applicable since	January 1, 1984	July 1, 1983
Notice timing	90–150 days before due	90–150 days before due



Disclaimer: The above information is intended for information purposes alone and is not intended as legal advice. Please consult with counsel before taking any steps in reliance on any of the information contained herein.

Endnotes

- 1 As defined by Regulation Z.
- 2 Civil Code §§ 2924i and 2966.
- 3 If the due date is extended before the balloon payment notice was otherwise required, the notice requirement shall only apply to the new due date. Civil Code §§ 2924i and 2966.

Cathy K. Robinson, Esq. is a Partner at Wright, Finlay and Zak. She can be reached at crobinson@wrightlegal.net.

T. Robert Finlay, Esq. is CMA’s legal counsel and a Founding Partner of Wright, Finlay and Zak. He can be reached at rfinlay@wrightlegal.net.