

Mortgage Wraps: Prepaid Interest

In a mortgage wrap transaction, the new mortgage will be handled the same way as a conventional mortgage. Per the amortization table, the first payment will be owed 30 days after closing since mortgages are paid in arrears vs. in advance like rentals.

If you close in the middle of the month, you can handle the interest in either of two ways. Let's use the example of closing on the 10th of any given month. One of the following options will need to occur:

1. If the payment is to be the 1st of the very next month, the buyer will be owed the ten days of interest from the 1st to the 10th of the closing month since the seller was the owner of the property. Thus, the seller owes a credit for interest on the HUD to the buyer for this period. The buyer's first full payment will be the 1st of the very next month after closing.
2. If the buyer is to skip the first month payment and the initial payment is to be the 1st of the second month following closing, the buyer will owe interest for the remaining days of the closing month. Thus, the seller will be paid "prepaid interest" on the HUD for the 10th to the end of the month. The buyer's 1st full month mortgage payment will be the 1st on the second month following the closing.

In a subject to/assumption transaction, it is handled the same way unless it is a distressed seller situation. If the investor is to bring the mortgage current and pay the seller a certain amount, the investor will be paying the very next mortgage payment after closing and the prepaid interest exercise detailed above is not followed.

If you would like to learn more about Wraps and Sub Tos, reach out to schedule a time to meet with us.

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