

Court Holds a California Finance Lender May Sell Loans to Purchasers That are Neither Licensed Finance Lenders Nor Institutional Investors

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On June 12, a Court of Appeal for California issued a decision in *Montgomery v. GCFS, Inc.*, 237 Cal. App. 4th 724, 188 Cal. Rptr. 3d 446 (2015), which clarifies the scope of the licensing requirements imposed by the California Finance Lenders Law, Cal. Fin. Code §§ 22000 *et seq.*

A provision of the California Finance Lenders Law, Cal. Fin. Code § 22340(a), provides that a licensed finance lender may sell promissory notes evidencing loans that it made, or that it purchased from another finance lender, to an institutional investor. That provision further allows the licensee to make agreements with the institutional investor for the collection of payments or the performance of services in connection with those notes. For purposes of this provision, an “institutional investor” is defined to include a licensed finance lender and a narrow list of other investors. See Cal. Fin. Code § 22340(b). This provision has been viewed by some as prohibiting finance lenders from selling loans to purchasers that are not licensed as finance lenders or do not otherwise meet the definition of “institutional investor.” In addition, the provision has been construed as requiring a purchaser that does not otherwise meet the definition of “institutional investor” to obtain a finance lender license to purchase loans from a licensee.

In *Montgomery*, when a licensed finance lender sold an account to an unlicensed purchaser and the purchaser sued for payment on the debt, the consumer filed a cross-complaint alleging that the sale of her debt to entities that were neither licensed as finance lenders nor as institutional investors violated the California Finance Lenders Law and rendered the debt void. The trial court found the sale did not violate the California Finance Lenders Law.

The Court of Appeal affirmed, holding that Cal. Fin. Code § 22340(a) does not prohibit a finance lender from selling loans to an entity that is not licensed as a finance lender and does not otherwise meet the definition of an institutional investor.

Note, however, the Court explored the legislative history of Cal. Fin. Code § 22340(a) and found that its purpose was to authorize finance lenders to sell loans to institutional investors while acting under the authority of that license. When engaged in this activity, a finance lender could take advantage of the exemption from real estate broker licensing contained in Cal. Bus. & Prof. Code § 10133.1(6) and would not need to obtain a real estate broker license.

Based on the *Montgomery* decision, a licensed finance lender may sell loans to an entity that is not licensed as a finance lender and does not meet the definition of an institutional investor. In addition, a purchaser that does not meet the definition of an institutional investor may purchase loans from a finance lender without obtaining a finance lender license. However, when a transaction involves a real estate secured loan, the sale and purchase may not be within the authority granted by the California Finance Lenders Law and further inquiry should be conducted to determine whether the finance lender and purchaser need to be licensed as real estate brokers.

If you have further questions on this issue, please contact [Jeffrey Barringer](#) or another member of our [Consumer Financial Services team](#).

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