



## THE RETURN OF SELLER FINANCING: CONTRACTS FOR DEED AS AN OPTION IN TODAY'S STRUGGLING REAL ESTATE MARKET

A contract for deed may be a helpful tool for both sellers and purchasers in a tough real estate market. A contract for deed is also known as a "land contract" or "installment land contract." In a contract for deed, the seller, rather than a lending institution, finances the purchase of the property. The purchaser takes immediate possession of the property and agrees to pay the purchase price of the property over time, generally in monthly installments. The seller retains legal title to the property throughout the term of the contract until the last payment is made and the contract is fulfilled. When the total purchase price has been paid to the seller, the purchaser is entitled to the type of conveyance identified in the contract. Generally, this will require the conveyance of a warranty deed to the purchaser.

### **Contracts for Deed - From A Purchaser's Perspective**

A contract for deed is attractive to purchasers who may not otherwise qualify for a loan or be in a financial position to purchase the property. A contract for deed is beneficial to a purchaser, because (i) it generally requires a smaller down payment than institutional mortgage financing; (ii) in the event of a default in payments, the purchaser must only bring payments current (within the time period provided by state law) to preserve rights in the property (assuming there is no acceleration clause in the contract, as discussed below); (iii) it is faster and easier to qualify for financing since the seller decides whether the purchaser is approved; and (iv) it is less costly than traditional mortgages since many closing costs, origination fees, application costs, and mortgage registration taxes are not applicable.

While a contract for deed has many benefits for a purchaser, it does not come without risk. The seller keeps legal title to the property until the contract price is paid in full, which means the purchaser does not become the owner of the property until he or she completes his obligations and receives title from the seller. If the purchaser defaults on the contract and fails to cure such default, the purchaser in almost all cases loses all of the money that has been paid on the contract and never obtains the property. It is extremely important for a purchaser to understand each and every obligation under the contract for deed prior to executing the document.

### **Contracts for Deed - From A Seller's Perspective**

A contract for deed is attractive to a seller because it is relatively simple to understand and allows the seller to control payment and interest terms. A seller facing large taxable capital gains on the sale of a property may wish to create an installment sale scenario where they can spread any taxable gains over many years.

A contract for deed also gives the seller more flexibility than a mortgage because the contract for deed affords the seller a quick method of canceling the transaction in the event of a default. In general, if the purchaser defaults on an installment, the seller can cancel the contract, retake the land, and, almost always, retain all the payments made and benefit from any improvements that the purchaser has made to the property. The seller may take this action without a foreclosure by advertisement or judicial foreclosure, which are required if the property is secured by a mortgage. A seller alternatively may elect to sue the purchaser for breach of contract, if the amount owing on the contract for deed exceeds the value of the property.

While a contract for deed has many benefits for a seller, it also involves some risk. The seller continues to own the property during the term of the contract for deed and retains exposure to some forms of liability that may attach to the property. If the seller chooses to retake the property after a default, he or she may have to take legal action to evict the purchaser. If the seller instead chooses to sue the purchaser for the unpaid

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installments, separate lawsuits will be required for each installment unless the contract for deed included an acceleration clause that provides for all principal payments to become due upon a single default. The standard form contract often used by non-lawyers in Minnesota does not include such a clause.

### ***Contractual Rights and Remedies***

The standard form contract for deed provides that the time of performance by the purchaser is an essential part of the contract. Thus, in most cases, the failure of the purchaser to comply with the terms of a contract for deed on the date specified in the contract constitutes a default. Once a monetary or non-monetary default has occurred, the seller has the right to terminate the contract for deed.

Minnesota Statute § 559.21 clearly sets forth the steps that must be taken to terminate a contract for deed. Once a default exists and the seller has decided to terminate the contract for deed, a notice of termination must be served upon the purchaser. The notice must set forth the following information:

1. The conditions under which default exists.
2. The period of time within which the purchaser may reinstate.
3. A statement that the purchaser must either (i) make payments in the amount owed, plus costs of service, attorneys' fees incurred, and other amounts due under the cancellation statute; or (ii) secure a court order suspending termination of the contract for deed.
4. The name, address, and telephone number of the seller or an attorney authorized by the seller to accept payments.
5. Certain specific language required by Minn. Stat. § 559.21 that notifies the purchaser of the consequences of a failure to comply with the notice.

For contracts for deed executed on or after August 1, 1985, the notice must state that the purchaser is further required to pay two percent (2%) of the amount in default at the time of service of the notice, not including balloon payment, taxes, assessments, mortgages, or prior contracts assumed by the purchaser. For the seller to recover attorneys' fees under a contract for deed executed on or after August 1, 1985, some default must have occurred for at least 30 days prior to the date of service of the notice upon the purchaser.

The right of the purchaser to reinstate a contract for deed is absolute, if the purchaser pays all sums required by the notice. If the purchaser fails to comply with the notice, the contract will automatically terminate. Upon termination, the Seller is almost always able to retain all sums that have been paid on the contract. The purchaser will lose the possession and use of the property, forfeit the right to assert any claims or defenses against the seller, and be subject to eviction from the property. Once the termination has been completed, however, the seller can no longer maintain any action for a monetary deficiency judgment against the purchaser.

A real estate attorney can help either a seller or purchaser understand the benefits, the risks, and the process of entering into a contract for deed.