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THE REAL ESTATE INSTALLMENT SALE CONTRACT: ITS DRAFTING, USE, ENFORCEMENT, AND CONSEQUENCES

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I. INTRODUCTION

A seller of real estate will often choose the real estate installment sale contract[1] to measure and define his contract obligation to his vendee and his rights and remedies if the vendee does not meet his end of the bargain. Such a contract is normally used when the buyer can make only a small down payment and there is substantial risk of nonperformance. The vendor uses the contract and retains title until a substantial part or all of the purchase price has been paid. The contract is usually drawn with the objective that, upon the vendee's default, the vendor should be able to reacquire all of his precontract rights to the property with a minimum of legal formality. Since the vendee's original equity under the contract may be minimal, he does not usually have much bargaining power in the negotiation of the agreement or its drafting. The contract itself usually limits the vendee's rights to possession of the property pending default and the right to a conveyance of the required title when and if he fully performs the contract.

Any other rights the defaulting vendee may have under such a contract are usually those which the law gives him outside the terms of the contract itself. A vendee unable to perform his contract obligations usually has few resources to assist him in claiming and enforcing any rights he may actually have. His bargaining power often consists merely of his possession of the property and the possibility that, without some formal surrender of his rights, the existence of the unperformed contract may appear to be a cloud on the seller's title that will hamper future disposition of the property.

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1. As used in this article, such a contract is distinguished from the ordinary executory contract for the sale of land or binder or earnest money agreement.

Missouri property law is not unlike that of Arkansas, and the author, as a member of the bar of both states, finds relevant Missouri writings on the general area covered by this article. In the *Journal of the Missouri Bar*, Professor Grant S. Nelson of the University of Missouri School of Law, Columbia, points out that the installment sale contract is a desirable instrument from the standpoint of the vendor, subject, however, to two very important qualifications: "If the contract is enforceable as written and if the title will not be clouded."[2] Professor Nelson concludes that it would be prudent for lawyers in that state to avoid installment sale contracts, particularly since, unlike Arkansas, there is a workable and relatively uncomplicated nonjudicial deed of trust proceeding available for foreclosure.[3]

While this writer does not entirely agree with Professor Nelson's conclusions, the purpose of this article is to consider whether the use of the installment land sale contract in Arkansas is always as desirable as it may appear, to suggest provisions which should be contained in such a contract, and to review the possible rights and remedies of the vendor and vendee under the contract. In this review, the inconsistent attitudes of courts in dealing with these agreements must be taken into account, and particular attention must be paid to the rights of the vendee upon default.

II. THE CONTRACT[4]

An installment sale contract is usually drafted by the vendor's attorney, and the vendee or his attorney may have little input into its content.

All persons owning an interest in the property should join in and be bound by the contract. The spouses of individual owners should join in the execution of the contract so that they will be bound to convey their homestead rights and any dower or curtesy

2. Nelson, *The Use of Installment Land Contracts in Missouri: Courting Clouds on Titles*, 33 J. MO. BAR 161 (1977). The article also refers to the following Missouri writings in this area: Parrish, *Forfeiture Provisions in Missouri Installment Land Contracts*, 29 MO. L. REV. 222 (1964); Comment, *Installment Contracts for the Sale of Land in Missouri*, 24 MO. L. REV. 240 (1959); Smith, *Contract for Deed—Caveat!*, 21 J. MO. BAR 492 (1965).

3. His opinion is that to continue the present Missouri practice of relying upon nonjudicial termination of the vendee's rights under an installment sale contract is to court increasing title problems.

4. In Fendler, *Drafting Instruments for Purchase and Conveyancing of Land*, 13 ARK. L. REV. 26 (1958), the author discusses the contents of the ordinary executory contract for the sale of land. Some of his thoughts are repeated here insofar as they are pertinent to installment sales.

rights involved, either choate or inchoate.[5] The vendee's spouse is not a necessary party to the contract unless his or her personal net worth lends something to the financial responsibility of the vendee or unless the property is to be purchased as an estate by the entirety.

When the property contracted to be sold is subject to an existing mortgage lien, there are various choices available to the parties. The parties may choose to say nothing about the mortgage lien. In this case, when the vendee completes his payments and is entitled to a warranty deed conveying the property free from all liens and encumbrances, it is the legal responsibility of the vendor to discharge this lien. If the vendor does this, all is well. However, the vendor may be unable to discharge the mortgage indebtedness at the time the required deed is to be executed and delivered. The existing mortgage may limit or preclude payment in advance of maturity, or the vendor may simply not have enough money with which to pay the amount required to procure release of the existing lien.

To avoid this unhappy situation, a number of alternatives should be considered when the sale contract is drafted. The mortgagee can be consulted, can be made a party to the contract, and can agree not to make any additional advancements under the existing security instrument, and the contract can set forth the terms upon which the lien of the mortgage is to be released as to the property covered by the contract.

The contract can require the vendee to make the vendor's mortgage loan payments directly to the mortgagee and to be given credit for such payments as part of his purchase money obligation. The contract should specify how the vendor is to be notified as such payments are made. If the purchase money obligation under the contract will not discharge the existing mortgage according to its scheduled maturity and if the mortgage contains no valid due-on-sale provision, the contract can provide for a conveyance of the property to the vendee when the existing mortgage indebtedness is no greater than the amount due under the contract, with the vendee at that time to receive his deed under the contract and to assume the remaining mortgage obligation. While this will not release the vendor from his personal liability with respect to the mortgage indebtedness, the vendor should be protected from loss with respect to the

5. ARK. STAT. ANN. § 61-208 (Cum. Supp. 1981), would preserve the statutory rights of both spouses in the property unless each joins in the final conveyance to the vendee. Hence, one spouse should be contractually obligated to join the other when the property is conveyed.

assumed indebtedness if the vendee has achieved a sufficient equity in the property purchased.

Another plan is for the payments under the contract to be made to an escrow agent who will make the mortgage payments to the holder of the existing mortgage, with any remainder to be turned over to the vendor. While this provision will not take care of the obligation of the mortgagor to insure or to pay taxes, those are usually obligations which are assumed by the vendee under the contract and may be taken care of by requiring additional payments for this purpose to the escrow agent or evidence that the vendee has paid taxes or insurance with his own funds.

Unless the vendor-mortgagor is of unquestionable solvency,[6] the existing mortgage should be taken into account, and counsel for the vendee can appropriately insist on provisions which will protect his client's interest when the client becomes entitled to conveyance of the property under the contract.

The property description should be that which is contemplated for use when the purchase price is paid in full. It should take into account any excepted mineral interests, easements of record, the accepted boundary lines, and easements with respect to any visible improvements. By setting forth the exceptions or easements following the description it will not be necessary to refer to these in detail in other contract provisions.

The contract should carefully spell out the obligations of the parties with respect to taxes and how the vendor is to be informed that the taxes have been paid. If the mortgage requires tax and insurance payments to be paid into escrow, this should be included in the contract.[7]

The improvements are often a substantial part of the property involved. The extent to which they should be insured[8] and the iden-

6. The vendee will not always be dealing with his original vendor when the contract is finally performed. The original vendor may die, and while his heirs may take the property subject to the vendee's contract rights, their responsibility may be less than that of the party with whom the vendee originally dealt.

7. In the absence of an agreement to the contrary, the vendee has the obligation to pay taxes coming due on or after the contract date, although they may be based upon a lien created in a year when he had no interest in the property. Subsequent taxes should also be paid by the vendee. *See* Booth v. Mason, 241 Ark. 144, 406 S.W.2d 715 (1966); ARK. STAT. ANN. § 50-401 (1971).

8. In many contract situations the continuance of the improvements in at least their contract date status is regarded as essential to the protection of the vendor's security interest in the property sold. The vendor may require insurance coverage against loss or damage at least to the extent of the balance due under the contract. If the insurance coverage is re-

tity of the party who is to bear the risk of damage by fire or similar hazard (1) between the date of the contract and delivery of possession and (2) thereafter, until the execution and delivery of the final conveyance of the property are subjects which may appropriately be included in the contract.

The writer has assumed that once possession is delivered to the vendee, the risk of loss by fire and similar casualty is that of the vendee. This is probably so, but Arkansas law is not so clear as to eliminate the need for specific provisions in the installment sale contract. While not many controversies have arisen in Arkansas in this area, most can be avoided by appropriate contract provisions and adherence to them.

Between the date of the contract and the delivery of possession, the risk of loss should be that of the vendor, but this responsibility may be limited to the amount of the vendor's existing insurance, the obligation to continue it until delivery of possession, and a requirement that he apply any insurance proceeds collected to the restoration of the insured improvements.[9]

Between the date of the delivery of possession and the final conveyance, the risk of loss should be that of the vendee, and the contract may require him to carry insurance, with the vendee being a payee of the insurance proceeds as his interest may appear and with either the policy or a certificate of insurance being furnished to the vendor, including a mortgage clause or loss payable clause in his favor.[10]

The vendor frequently contracts to furnish an abstract reflecting a certain type of title when the vendee completes the payment of the purchase price as provided by the contract. From the vendor's standpoint, it appears desirable to postpone the abstract or other title expense until the vendor has actually received the purchase price

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quired to be the insurable value of the improvements, there is a greater likelihood that the insurance proceeds will be sufficient to repair the damage. Otherwise, the damage may not be restored, and the vendor may be compelled to accept payment of his debt through insurance proceeds at a time when, for tax reasons, he would prefer not to do so.

9. The author has on occasion provided that the insurance need not exceed the balance due under the contract. This assumes that the insurance company will issue coverage for the smaller amount and pay the entire proceeds of the loss to the contract vendor. Neither assumption may be correct. If continued existence of the improvements is not really essential to the vendor's protection, the better practice might be to leave out the requirement of insurance altogether.

10. Without a contract provision to that effect, the vendor is liable for waste committed by him or for which he may be responsible. He is deemed to have a trust relationship to his vendee while in possession. *See* Newman v. Mountain Park Land Co., 85 Ark. 208, 107 S.W. 391 (1908); 77 AM. JUR. 2D *Vendor and Purchaser* §§ 363-367 (1975).

contemplated by the contract. This is not always the better choice. If there is to be any dispute about the sufficiency of the title as submitted, it should occur at the time of the execution of the contract of sale rather than later, when substantial equities may have intervened.

The vendor, or those who may have succeeded to his interest in the contract, will be required to convey the property to the vendee by an appropriate deed upon completion of the vendee's contract obligations. When the deed is not executed as of the contract date it should limit the warranty obligations of the vendor by excluding matters referred to or excepted in the description of the property and matters arising from and after the contract date by the act, neglect, or default of the vendee or those succeeding to his interest.

When the vendor is advanced in years or the contract is of long duration, deposit of the deed in escrow is desirable.

The vendor often wants a clause in the contract prohibiting the assignment of the vendee's interest without his consent.[11] An unqualified prohibition against assignment is usually invalid, but such a provision is usually appropriate to protect the vendor although, to protect the vendee, the language could appropriately provide that such consent shall not be unreasonably withheld if the vendor has advance notice of it.[12]

The contract should provide that any assignment must be in writing with a copy delivered to the vendor, so that the vendor will know, when he has received final payment, that the assignee of the contract has, in fact, been granted all the rights of the original vendee. The language prohibiting or restricting assignment should extend not only to absolute assignments but also to assignments by way of pledge, mortgage, or other device and may include a provision defining the vendor's rights in the event of an execution sale

11. *E.g.*, Sproull v. Miles, 82 Ark. 455, 102 S.W. 204 (1907); Annot., 138 A.L.R. 205, 211 (1941) (stating that the majority of the cases take the view that even if the assignment of the contract is made in violation or disregard of a provision prohibiting the vendee from assigning it, this does not preclude the assignee from maintaining a suit to compel specific performance if his assignor could have done so in the absence of the assignment); *see* Weis v. Meyer, 1 S.W. 679 (Ark. 1886); American Land Co. v. Grady, 33 Ark. 550 (1878); 77 AM. JUR. 2D *Vendor and Purchaser* §§ 399-402 (1975).

12. *Cf.* Warmack v. Merchant's Nat'l Bank, 272 Ark. 166, 612 S.W.2d 733 (1981) (landlord cannot unreasonably withhold consent to a sublease); Tucker v. Pulaski Fed. Sav. & Loan Ass'n, 252 Ark. 849, 481 S.W.2d 725 (1972) (there must be legitimate grounds for the mortgagee to withhold consent to the conveyance of mortgaged property). The vendor, however, is entitled to *know* of any proposed assignment. This right, the author believes, would be held enforceable even though the vendor might be required to consent to the assignment (without release of the original vendor) if he were made aware of it.

against the vendee's interest. Particularly in connection with the matter of assignment of or levy upon the vendee's interest, the contract should contain a provision concerning what remedies the vendor may be given in the event of a prohibited assignment. These remedies may consist of forfeiture of the vendee's rights, rescission of the contract by the vendor, or a right of acceleration with regard to all remaining payments due under the contract.[13] The forfeiture clause may not always be enforceable, however, and rescission would require the vendor to repay the consideration paid by the vendee plus interest but less the rental value of the property prior to rescission. Therefore, the acceleration of the remaining payments would appear to be the most feasible remedy which the courts would enforce in the event of an impermissible assignment or involuntary appropriation of the vendee's rights under the contract.

The author regards it desirable from the standpoint of both vendor and vendee for the contract to contain a provision whereby the vendor executes a warranty deed, furnishes the required abstract, and takes a purchase money mortgage or deed of trust to secure the balance due after the vendee has paid a specified part of the contract price. This is advantageous to the vendee, who then has legal title to the property, and may more readily sell or mortgage it subject to the rights of the vendor as the first lienholder. It may also benefit the vendor because he may more easily borrow against his note and deed of trust than against an unperformed contract. The unperformed contract would, of course, obligate an assignee of the vendor's interest to furnish the required conveyance of title upon payment, which may not be possible unless the vendor has deposited with his secured creditor or an escrow agent the warranty deed required by the contract.

The author regards it as advantageous for the vendor to require a promissory note to evidence the installment obligations of the vendee under the contract,[14] with this note to contain the permissible provisions for attorneys' fees in the event of default.

The contract should provide that any prior indulgence with regard to accepting late payments or delayed performance under the contract shall not be treated as a precedent with respect to any subsequent default on the part of the vendee.[15] It may state that time is

13. There may be serious questions about whether an acceleration can be based only on the fact of the assignment without a showing of prejudice to the vendor or some other violation. *See* Tucker v. Pulaski Fed. Sav. & Loan Ass'n, 252 Ark. 849, 481 S.W.2d 725 (1972).

14. *See* 77 AM. JUR. 2D *Vendor and Purchaser* §§ 477-478 (1975).

15. Recent Decisions, 18 ARK. L. REV. 175 (1964) discusses the eagerness of the courts

of the essence with regard to the performance of all obligations of both parties under the contract. If the vendee has paid for the property as provided by the contract, there is no logical reason why the vendor should not perform his obligations promptly by executing the required deed. With regard to payments, the vendor is entitled to expect and receive prompt payment and prompt performance of the vendee's other obligations. The "time is of the essence" provisions in the contract merely accentuate the intent of the parties that both parties should perform their respective obligations promptly and reflect the hope that the courts will enforce those contractual covenants.

In some cases, the vendor may deposit with an escrow agent the executed warranty deed, dated as of the date of the contract, to be delivered upon full payment of the purchase price. The escrow agent normally will not want to assume any responsibility for the enforcement of the contract. When such an escrow agent is used, the contract or the separate escrow agreement should provide that within a prescribed number of days after the due date of an unpaid installment the vendor may, without notice to the vendee, pick up the instruments deposited in escrow, and the escrow agent shall then be under no further responsibility with respect to the escrow. In the absence of such a provision, the escrow agent may be involved in an election of remedies procedure which is not within the scope of its duties or willingness to act.

The contract will normally provide for the options available to the vendor in the event of default. The author suggests the following:

> Should the vendee default with respect to any of the payments of principal or interest as herein provided, or otherwise violate or be in default with respect to the vendee's obligations hereunder, the vendor may, at vendor's option, cancel and terminate this contract, in which event the vendor shall be entitled to immediate possession of said premises and retain all sums heretofore paid as rent for the use and possession of said premises prior to default and as liquidated damages for the vendee's breach of the contract, with the vendor to return to the vendee any promissory note given in connection with this contract, with any unpaid balance marked "cancelled" by reason of the termination of the contract, or the vendor may declare the entire indebtedness due and

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to avoid the consequences of forfeiture clauses in contracts. The suggested provision is intended to make it less likely that the vendor will be decreed to have waived something he did not intend to waive. What the courts will do with such a provision is another matter.

payable at once, sue therefor in accordance with the terms under the note and foreclose this contract of sale as to the equitable interest of the vendee hereunder.

The author suggests a separability clause declaring that if any portion of the contract regarding the rights of the vendor be held void or unenforceable, the vendor may nevertheless enforce the remaining provisions.

It is to the advantage of the vendor that there be no acknowledgment of the instrument, which will preclude it from being recorded. If recorded, the contract may create a cloud on the record title although the vendee may have long since departed and returned possession of the premises to his vendor. As long as the vendee is in possession of the premises, that possession is constructive notice of his rights or that such rights may exist. In the usual vendor-vendee situation under a long-term installment contract, there appears to be no great need for the contract to be recorded if the premises are sold to and are actually occupied by the vendee.

Recording is certainly not desirable when the vendor expects to effectively enforce the summary remedies which his contract calls for upon default by his vendee. Some forms actually prohibit the vendee from recording his contract until all of his payments have been made and all of his obligations have been performed.[16] The writer dislikes such a provision and doubts that the courts would enforce it if the instrument were otherwise entitled to record. It seems unduly harsh to impair a vendee's rights if he has actually acquired a substantial equity in the property and may have temporarily vacated it, thus depriving him of the benefits accruing from any constructive knowledge by a third party of his equity. However, the same result may follow if the original contract simply is not acknowledged, even though it contains no specific provision with regard to the contract's being recorded.

The contract provisions may vary according to the specific problems involved. When farm property is involved, the author believes it desirable that the maturity of all payments be fixed whereby a debt will not come due after a crop has been planted, so that there will be no problems with respect to growing crops or unplanted ground. Many of the problems with respect to tenancies from year to year and a tenant holder under an oral lease of farm lands[17] can

16. 16 AM. JUR. 2D *Legal Forms* § 219.655 (1973), contains such a form.

17. Prior to 1981, a farm tenant holding under an oral one-year agreement was not entitled to notice of the landlord's decision not to extend the lease for another year. This

be alleviated if the maturity of each installment is fixed early enough in the calendar year so that the vendor retaking possession can give notice to the vendee's tenant of his intention to terminate any existing tenancy prior to the June 30th deadline otherwise applicable. While the rights of the vendor under the contract may be superior to those of the tenant, the selection of an appropriate due date for payments may avoid undue and extended unsatisfactory relationships between the vendor and the vendee's tenants.[18]

The use of a good office form or a good form book will be helpful to the draftsman of the installment sale contract. The draftsman must, however, be aware that many of the fact situations presented do not come within the confines of a form contract. The factual situation should be carefully analyzed before the language of a previous contract is routinely used, and the contract should be adapted to the facts and apparent equities of the particular case.

The vendor should be alerted to the fact that not all of the language in his favor which has been inserted in the contract may be enforceable in the courts. This is particularly true if the vendor does not, after the contract's execution, insist upon strict observance by the vendee of all the vendee's contractual obligations. Without such a warning, the draftsman may find himself subject to criticism by his client—and possibly to a malpractice claim—when the vendor finds out that not all of the remedies specified in the contract are actually available to him and that, at least in Arkansas, there are uncharted areas concerning what the vendor can or cannot do in the event of his vendee's default.

III. RIGHTS AND REMEDIES UNDER THE CONTRACT

A. *The Rights*

Arkansas courts have generally held that both the rights of the vendor[19] and those of the vendee[20] are assignable and that this is a

rule was modified by ARK. STAT. ANN. § 50-531 (Cum. Supp. 1981) which requires, in the case of oral agreements, the same notice not to renew or extend as was previously applicable to tenancies from year to year.

18. *See* Wallin v. Donnahoe, 175 Ark. 791, 300 S.W. 428 (1927). If the unpaid vendor exercises his summary remedies involving his vendee prior to June 30th of any year, he may nevertheless find it desirable to recognize the tenant's rights for the remainder of the calendar year, particularly when a crop has already been started. He can avoid the effect of a possible year-to-year tenancy claim or an oral tenancy for the next year if the summary remedies can be enforced prior to June 30th and notice of an intention not to rent beyond the current year is given before June 30th.

19. Lancaster v. Robinson, 221 Ark. 767, 256 S.W.2d 330 (1953).

20. Corcorren v. Sharum, 141 Ark. 572, 217 S.W. 803 (1920).

statutory right.[21] The status of the vendor of real estate has been described as that of a constructive trustee for the purchaser, with the vendor holding the naked legal title which he or his heirs must convey to the purchaser upon payment of the purchase price.[22]

If the vendor's spouse has not joined in the contract and refuses to release dower or curtesy rights to the vendee, the vendee, in seeking specific performance of the contract, has the right to have the purchase price abated by the value of the dower or curtesy rights, but with the abatement to be restored as a part of the purchase price if the vendor is alive seven years after his deed to the vendee is recorded.[23]

If a vendee dies while in possession of the land under a contract of purchase and has paid a portion of the purchase money, his or her spouse is entitled to dower or curtesy therein,[24] but dower and curtesy rights are subordinate to the lien or claim of the vendor for his unpaid purchase price.[25]

If the property in question has been occupied by the deceased vendee as a homestead, the widow or widower and minor children would also take homestead rights therein, but subject to the superior equities of the vendor with respect to his unpaid purchase price.[26]

If, as the earlier cases state, the vendee acquires an equitable estate in the lands by reason of his contract of purchase, he should be able to mortgage his interest therein and create a valid lien in favor of his mortgagee to the extent of his equitable interest. In *Harris v. McCann*,[27] decided in 1959, the Arkansas Supreme Court held that when the contract purchaser had possession of the property and had paid part of the purchase price, he had an equitable interest which he had a right to mortgage.[28]

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21. *Id.*; ARK. STAT. ANN. § 68-801 (1979).

22. McKim v. McLiney, 250 Ark. 423, 465 S.W.2d 911 (1971).

23. Box v. Dudeck, 265 Ark. 165, 578 S.W.2d 567 (1979). A spouse's inchoate right of dower or curtesy is barred under ARK. STAT. ANN. § 61-226 (Cum. Supp. 1981) when the conveyance by the husband or wife has been made and recorded for a period of seven years or more. The court's opinion avoids the issue whether the values determined by the court were precise with respect to the present value of the wife's right of inchoate dower, pointing out that it was the affirmative duty of the appellants to show that the value determined by the court was erroneous, which the appellant had failed to do.

24. Spaulding v. Haley, 101 Ark. 296, 142 S.W. 172 (1911); ARK. STAT. ANN. §§ 61-201, -206, -207 (Cum. Supp. 1981).

25. Corcorren v. Sharum, 141 Ark. 572, 217 S.W. 803 (1920).

26. Spaulding v. Haley, 101 Ark. 296, 142 S.W. 172 (1911).

27. 229 Ark. 972, 319 S.W.2d 832 (1959).

28. 55 AM. JUR. 2D *Mortgages* § 111 (1971) (the courts regard as mortgagable interests both the interest of the vendor of land, while the contract for sale remains executory and no

A 1979 decision of the Supreme Court of Arkansas, *Arkansas Supply, Inc. v. Young*,[29] appears to be inconsistent both with this decision of twenty years earlier and the general law on the question of whether the interest of the contract purchaser is mortgagable. Wright, the contract purchaser, had contracted to buy land for a total purchase price of $15,000, of which only $150 was paid to the vendor. Wright procured credit from Arkansas Supply, made improvements on the premises, and gave Arkansas Supply a mortgage on his interest in the contract. Upon the failure of the vendee to pay the required purchase obligation, the vendor gave notice to the vendee of his intention to cancel the contract. The vendor retrieved the deed to the vendee which had been deposited with a bank in escrow pending payment of the full purchase price. Without any recognition of the rights of Arkansas Supply as a mortgagee of the interest of the vendee, Young paid Wright $3,000 for the relinquishment of his interest in the contract and paid the vendor $15,707 for a deed to the property.

The Arkansas Supreme Court summarily disposed of the claim of Arkansas Supply as the mortgagee of Wright. The court held that Wright, the mortgagor, acquired no interest in the property until the conditions of the escrow agreement and the contract of sale had been met. Consequently, his mortgagee took no interest even though the escrow papers had not been picked up from the bank at the time the Arkansas Supply mortgage was given and recorded.[30]

The *Arkansas Supply* decision is simply inconsistent both with the statutory law of this state and the earlier cases. It should operate as a warning to any creditor of a vendee who seeks to take security by a mortgage of the vendee's interest in a partially performed contract of sale. In advising a vendor of such a vendee about his rights under the unperformed contract, the author of this article would, however, be reluctant to advise such a vendor that he can terminate the interest of a defaulting vendee without recognition of a recorded mortgage covering the vendee's interest under the contract.

If the interest of the vendee under an incomplete contract of sale is not subject to mortgage by the voluntary act of the vendee, the question arises whether it is subject to execution issued at the

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deed has passed, and the interest of the vendee under a contract to purchase). *See also* A. HUGHES, ARKANSAS MORTGAGES §§ 159-160 (1930) (equitable titles may be mortgaged).

29. 265 Ark. 281, 580 S.W.2d 174 (1979). The author has reviewed the briefs in this case and in some instances has made references to facts stated in the briefs which do not appear to be in dispute but which are not covered in the opinion.

30. *Id.* at 284A, 580 S.W.2d at 175.

instance of his judgment creditor. Despite the holding in the *Arkansas Supply* case and its apparent implications, the author believes that the present statutory law[31] compels the conclusion that either the interest of the vendee or his vendor can be reached by execution, attachment or similar process.

A number of earlier cases state that once a vendor has entered into a valid contract of sale, his interest in the property is no longer subject to execution or similar process, particularly at law.[32] The rule of these earlier cases was modified in 1953 by a statute which made such an interest subject to seizure under execution, garnishment, attachment, or other process.[33] It would appear that this statute makes both the interest of the vendor and that of the vendee under a contract of sale subject to execution, attachment, and similar process, but with the sale to convey subject to the equities, rights, and interest of other parties who might have a prior or superior interest in the property. Both by case law and statute the interest of a vendee in a land contract is subject to levy or execution.[34]

Following the execution of an executory land sale contract, is the interest of either the vendor or that of the vendee subject to a judgment lien? Concerning the interest of the contract vendor, there is now no question but that the rights of the contract vendee are superior to those of the judgment lien creditor whose judgment is obtained after the execution of the land sale contract.[35]

Concerning the interest of a contract vendee, the present statute[36] makes judgments a lien on the "real estate" owned by the defendant in the county where the judgment is entered and in the

31. ARK. STAT. ANN. §§ 30-201, -219 (1979).

32. Snow Bros. Hardware Co. v. Ellis, 180 Ark. 238, 21 S.W.2d 162 (1929); Howes v. King, 127 Ark. 511, 192 S.W. 883 (1917); Strauss v. White, 66 Ark. 167, 51 S.W. 64 (1899); *cf.* Hill v. Heard, 104 Ark. 23, 26, 148 S.W. 254, 255 (1912) (citing with approval 1 C. POMEROY, EQUITY JURISPRUDENCE § 367 (2d ed. 1905) regarding the interest of a contract vendee: "He may convey or incumber it, may devise it by will; on his death, intestate, it descends to his heirs, and not to his administrator.")

33. ARK. STAT. ANN. § 30-219 (1979).

34. Evins v. Sandefur-Julian Co., 81 Ark. 70, 98 S.W. 677 (1906); ARK. STAT. ANN. §§ 30-201, -219 (1979).

35. Pulaski Federal Sav. & Loan Ass'n v. Carrigan, 243 Ark. 317, 419 S.W.2d 813 (1967). While the court's opinion speaks only of the priorities between the rights of the judgment lien creditor and those of the contract vendee, the chancellor had held that the judgment lien did not constitute a lien against the property covered by the contract, and that decision was affirmed on appeal. *Accord*, State Bank v. Sanders, 114 Ark. 440, 170 S.W. 86 (1914); Shinn v. Taylor, 28 Ark. 523 (1873). *But see* 46 AM. JUR. 2D *Judgments* § 256 (1969) (the interest of a vendor in lands contracted to be sold is bound by the lien of a judgment recovered against him while the contract is unexecuted, to the extent that it is unexecuted).

36. ARK. STAT. ANN. § 29-130 (1979).

counties where it may be filed. An early case held that the equitable estate of a defendant in realty was bound by such a judgment lien.[37] This case, the author believes, is strong authority for the proposition that the judgment lien of a creditor extends to the equitable interest of the contract vendee in real estate.

From the standpoint of consistency, since Arkansas law does not make a judgment lien applicable to an interest in personalty, and, under the doctrine of equitable conversion, the interest of the contract vendor is treated as personalty after the execution of the contract of sale,[38] it would appear that the Arkansas courts should hold that the lien of the judgment against the contract vendor does not extend even to the vendor's remaining interest in the property sold, since that interest is treated as personalty. When the vendor has terminated[39] the interest of the vendee's contract, it would appear that the vendor again owns realty and the judgment lien would then attach.

Usually there is not much likelihood that the vendor will be called upon to repay to his defaulting vendee any sums paid by the

37. Cohn v. Hoffman, 50 Ark. 108, 6 S.W. 511 (1887). For the rules governing the application of the judgment lien to the interest of the contract vendee, see Annot., 1 A.L.R.2D 727, 742 (1948) and 46 AM. JUR. 2D *Judgments* §§ 237-244 (1969).

38. Pulaski Fed. Sav. & Loan Ass'n v. Carrigan, 243 Ark. 317, 419 S.W.2d 813 (1967). The author agrees with the result achieved by the majority in the *Carrigan* case, but not with the reasoning. Judgment liens exist only by reason of statute and, until an execution has been issued, a judgment is not a lien against personalty. In the *Carrigan* case, a contract of sale was executed on December 9, 1965, which, under many decisions of the Arkansas courts, had the effect of converting the interest of the sellers from realty into personalty. The judgment against the sellers was not obtained until March 23, 1966. Execution against the interest of the vendors in their contract was not issued until sometime after May 5, 1966, by which date a deed from the vendor (the judgment debtor) had already been delivered to the Carrigans. By the time execution was levied, there was nothing to be levied upon, either legal or equitable, with respect to the contracted property since the transaction had already been closed and the full consideration paid.

The dissent observed that the bond for title, once in common use in conveyancing when lands were sold upon credit, has fallen into disuse. The dissent pointed out that the bond for title contains a provision whereby the vendor bargains and sells the real estate to the purchaser while the vendor in a contract of sale "agrees to sell." If there ever was any distinction between the two phrases, they have long since ceased to exist in actual practice. 243 Ark. at 321-25, 419 S.W.2d at 816-18 (Fogleman, J., dissenting). In the law firm with which the author practices, forms are used for contracts of sale which recite that the vendor "contracts and sells" and the vendee "contracts and buys" the lands. Since the instrument is designated a contract of sale, the parties to it regard it as such and act accordingly. Substitution of the word "to" for the word "and" should not reduce or enhance the vendor's forfeiture rights, since the courts look at the substance and not the form of a transaction.

39. Bates v. Simmons, 259 Ark. 657, 536 S.W.2d 292 (1976) is a recission case, but the principles involved are similar to those in which the termination of a valid contract is involved.

vendee prior to default. The retention of such sums may be justified either on the basis of rental for the use and possession of the contracted property prior to default, or as liquidated damages, for the breach of the vendee's contract to purchase the property and to pay for it according to schedule.[40] In the absence of exceptional equities in favor of the defaulting vendee, the vendor will probably be allowed to keep any money paid by the vendee prior to default, particularly when the contract expressly provides for the retention of such payments.

B. *The Remedies Available*

The remedies available should be considered in the light of the relationships created.

Many cases have declared that the relation of vendor and purchaser is essentially that of a mortgagor and mortgagee and that the vendor has an equitable lien on the land upon the failure of the vendee to pay the purchase price.[41] In *Weaver v. Gilbert*,[42] decided in 1949, the court pointed out that a long line of Arkansas cases had held that the effect of the contract was to create a mortgage in favor of the vendor in the same manner as if the vendor had conveyed the land by an absolute deed to the vendee and taken a mortgage back to secure the purchase price. This concept strongly suggests that the appropriate remedy should be foreclosure of the vendee's rights in equity.

What, however, if the unpaid vendor merely retakes possession of the property? Is this a cancellation of the contract and termination of the vendee's rights? Early cases suggest that when the possession of the land is given under an executory contract for its purchase and the purchase money is due and unpaid, the vendor may recover possession of the land *for the purpose of applying the rents and profits to the payment of his debt*.[43] Cancellation of the debt resulting from the contract does not extinguish the vendee's equitable title under the contract unless done with the consent of the

40. Suter v. Mason, 147 Ark. 505, 227 S.W. 782 (1921), held that an initial payment of $3,000.00 could validly be collected as liquidated damages for the failure of the buyer to perform since the amount was not unreasonable nor void as a penalty, in view of the magnitude of the transaction and the risk of monetary depression. See Annot., 6 A.L.R.2D 1401 (1949).

41. Hogue v. Hogue, 247 Ark. 914, 448 S.W.2d 627 (1969); Brooks v. Smith, 215 Ark. 421, 220 S.W.2d 801 (1949).

42. 214 Ark. 800, 218 S.W.2d 353 (1949).

43. Cleveland v. Aldridge, 94 Ark. 51, 125 S.W. 1016 (1910); Smith v. Robinson, 13 Ark. 533 (1853).

vendee, and a subsequent sale of the land by the vendor to a third person does not pass complete title, but merely subrogates the new purchaser to the rights of the original vendor as mortgagee.[44]

If, following default by the vendee, the vendor seeks to retake possession of the contracted property by legal proceedings, the suit should indicate that he does not thereby undertake the status of the mortgagee in possession but sues as the absolute owner following a valid forfeiture of the vendee's interest or an accepted cancellation of the vendee's debt for the unpaid purchase price.[45]

The rule of the earlier cases making the original vendor a mortgagee in possession and giving him no reacquired title which he can convey in fee simple will not apply, of course, when there has been a valid forfeiture of the vendee's contract interest which is binding upon not only the original vendee but also the vendee's judgment creditors and the mortgagees with respect to the contracted property.

Contracts drawn to protect the vendor usually provide for a forfeiture at the option of the vendor in the event of default of the vendee. Many contracts contain such a provision. In *White v. Page*[46] Justice McFadden points out that an executory contract with a forfeiture clause is valid and that the forfeiture can be exercised pursuant to the contract without proceedings in law or equity. There are many cases which support this conclusion.[47]

The author, however, is unable to accept the reasoning in *White v. Page* which makes forfeiture clauses valid if they are contained in a contract of sale but ineffective and requiring foreclosure if they are contained in a contract which is deemed to be a title bond.

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44. Robertson v. Read, 52 Ark. 381, 14 S.W. 387 (1889).

45. See *supra* text accompanying note 42. The same suit can, the author believes, seek a determination through declaratory judgment that the judgment creditors and mortgagees of the vendee, if there are any, have no interest in the property. Without such a full determination, the author thinks that there will still be the possibility that the vendor has acquired something less than a fee simple title even though he may have recovered possession following default. If the interest of the vendee is viewed merely as a contingent interest or an expectancy which has not been realized, the judgment creditors and the mortgagees of the defaulting vendee may have nothing against which to enforce their judgment lien or their mortgage upon what has, in many cases, been recognized as the equitable estate of the contract vendee.

46. 216 Ark. 632, 226 S.W.2d 973 (1950).

47. *E.g.*, Wade v. Texarkana Building & Loan Ass'n, 150 Ark. 99, 233 S.W. 937 (1921); Three States Lumber Co. v. Bowen, 95 Ark. 529, 129 S.W. 799 (1910); Friar v. Baldridge, 91 Ark. 133, 120 S.W. 989 (1909); Souter v. Witt, 87 Ark. 593, 113 S.W. 800 (1908); Ish v. McRae, 48 Ark. 413, 3 S.W. 440 (1887).

As early as 1884[48] the Arkansas Supreme Court said,

> A title bond, although it has become a common mode of making a equitable conveyance [sic], is in fact but an executory contract in writing for the sale of real estate, to be afterwards consummated by a further action when the conditions may be complied with . . . .[49]

And further:

> In every respect a title bond is but an agreement to convey, from which a court of equity creates an equitable estate in the vendee, holding the vendor as his trustee for the land and the purchaser as the vendor's trustee for the money . . . .[50]

The cases cited in *White v. Page* which are treated as bond for title cases[51] are not substantially different from those cited in the same opinion which are treated as contract of sale cases,[52] in which a forfeiture may be enforced unless waived by action of the parties.[53]

If the vendee defaults and the land is worth more than the unpaid contract obligations, the vendor will usually want to avail himself of the forfeiture provisions in his contract by summary action. The safest procedure, from the vendor's standpoint, would be to procure a written release by way of quitclaim deed or similar instrument evidencing the fact that neither the vendee, his judgment lien creditors, his mortgagees, nor his assigns claim any interest in the contracted property. Such an instrument cannot always be obtained. Without such a written release, and absent judicial foreclosure or appropriate declaratory judgment procedure, the vendor undertaking to resell the property may find that he has something less than a marketable title acceptable to a new vendee.

If the vendor merely wants to get his money out of the property, his most complete remedy would be by foreclosure in equity. There, the vendor would get the first lien on the proceeds of the sale, and the claim to any equitable interest on the part of the vendee, his judgment creditors, or his assignees could be disposed of if they were made parties to the suit. The objection to the procedure is that

48. Atkinson v. Hudson, 44 Ark. 192 (1884).

49. *Id.* at 196.

50. *Id.* at 197.

51. 216 Ark. 632, 636, 226 S.W.2d 973, 975 (1950).

52. *Id.* at 637, 226 S.W.2d at 975.

53. This subject is discussed in Recent Decisions, 18 ARK. L. REV. 175 (1964); Recent Decisions, 21 ARK. L. REV. 139 (1967); and Note, 24 ARK. L. REV. 578 (1971).

it costs money, and the vendor may be more interested in reacquiring his property than in procuring the payment for it according to the original contract. This may be true even when the use of a note will permit him to recover some, if not all, of his attorneys' fees incurred in connection with a foreclosure.

The vendor's choice is between a remedy which may be inexpensive and apparently effective but which may leave some clouds on the title, and a more expensive one which may leave the vendor with a marketable title.

C. *Effects of Bankruptcy*

The bankruptcy of either the vendor or the vendee may bring into play different rights and remedies from those otherwise available to the parties. If the vendee becomes a bankrupt and the trustee in bankruptcy (or the debtor in possession) should determine, with court approval, that the vendee has no equity in the property worth protecting, the executory obligations of the vendee can be cancelled and the property returned to the vendor free from any obligation to make further payments and free from any claim of the vendee.

If the bankruptcy court determines the equity of the contract vendee to be of value either to him or the bankrupt's estate, the trustee (including the debtor in possession) can accept the remaining obligations of the sale contract. If this is done, the trustee or the debtor in possession is required to cure any existing default or furnish adequate assurance that such default will be cured promptly and compensate or provide assurance that parties other than the debtor will be compensated for any actual loss resulting from such default. Also, the vendor is entitled to adequate assurance of future performance by the vendee under the contract. One option not available to the vendor in the event of the bankruptcy of his vendee is that he may not accelerate the indebtedness due from the bankrupt vendee merely by reason of the bankruptcy.[54] Just what these requirements mean in actual practice will depend largely upon the attitude of the bankruptcy judge regarding the protection to be afforded the vendor upon his vendee's bankruptcy.

A purchaser in possession is entitled to retain his possession for as long as he performs his obligations under the contract, notwith-

54. See 11 U.S.C. § 365(b)(2) (Supp. IV 1980), which precludes such an acceleration even though the contract may provide for it.

standing the bankruptcy of the vendor.[55] If the vendor becomes a bankrupt, the obligations owed to him by the vendee are a bankruptcy asset which can be disposed of with the approval of the bankruptcy judge,[56] and this disposition can be made free of any rights of dower or curtesy, vested or contingent, which might otherwise exist in favor of the bankrupt's spouse. The trustee can also assign the debtor's interest in the contract and thus relieve the bankrupt or the estate from any liability for defaults occurring after the assignment.[57]

If the vendor is permitted to retain his rights under the contract, either as a part of his exemption or as an asset which the bankruptcy court sees fit to return to him, it appears that the dower or curtesy rights of the spouse remain and must be relinquished in the final conveyance pursuant to the contract.

IV. CONCLUSION

The Arkansas court has not been consistent in dealing with either the nature of these contracts, the statutes which cover them or the rights of the contracting parties or those claiming under them. Its reasoning in supporting or rejecting a sometimes harsh and often inequitable result is not new to the Arkansas court or to these times. An ancient but respected authority often found similar problems in other jurisdictions in the contest between the literal language of the contract and an equitable result.[58] The Arkansas court has sometimes avoided a forfeiture by finding waivers to exist on rather insubstantial grounds and certainly contrary to the intention of the unpaid vendor.[59]

Since the remedies of an unpaid vendor are not covered by statute, but entirely by equitable principles, the author believes that the best rule would be one suggested by the Oregon Supreme Court in 1922, in which the following language was used:

> This case, therefore, presents a controversy not affected by statute, but is one that is controlled entirely by equitable principles. Under those principles as recognized and adopted by the decisions of the courts of this and other states where a contract for the sale of realty is executory on both sides and the vendee has failed

55. 11 U.S.C. § 365(i)(1) & (2) (Supp. IV 1980).
56. *Id.* at § 363.
57. *Id.* at § 365(k).
58. 1 C. POMEROY, EQUITY JURISPRUDENCE § 455 (2d ed. 1905).
59. Berry v. Crawford, 237 Ark. 380, 373 S.W.2d 129 (1963); Recent Decisions, 18 ARK. L. REV. 175 (1964).

> to make the payments required under the contract, the vendor, in case such relief is not inequitable, is entitled to a decree fixing a reasonable time in which the vendee will be required to pay the purchase price, and upon his failure to pay such price within the time limited, the vendee, without judicial sale, will be barred and foreclosed of his equitable estate in said property, whereupon the contract will be canceled and the vendee's rights thereunder will be terminated. If, however, the vendee has paid a considerable portion of the purchase price, or if the property has largely enhanced in value, or if, for any other reason, it would be inequitable to grant a strict foreclosure, it is within the inherent powers of a court of chancery, independent of statute, to decree that the property be sold by judicial sale, and that the proceeds of such sale, after the purchase price and the expenses of such sale have been paid, be paid over to the vendee or to those entitled thereto.[60]

Such a procedure would have the disadvantage of requiring the parties to go into court to establish their rights under a partially performed contract. It would eliminate the question whether there has been a waiver of the forfeiture provisions of a contract and whether the contract is, in legal effect, a bond for title or merely an executory contract of sale. It would eliminate the need for and the expense of a foreclosure sale if the vendee had, in fact, no equity in the property to be sold either for himself or for the benefit of his judgment creditors or his mortgagees.

It would have the advantage of recognizing that a vendee's equity in the property is measured not by what he has paid to the vendor but by what the value of the property may be at the time of his default.

While, as a practicing lawyer, the writer recognizes that the results will not always be uniform even in cases having similar facts, the Oregon procedure would probably be preferable to the present situation in which the defaulting vendee and those claiming under him may either lose their rights because the contract was skillfully drawn to protect the vendor or because the defaulting vendee did not recognize the rights which he had upon default, or, if he did recognize them, found himself unable to finance the defense of whatever rights he had.

The present law with respect to installment sale contracts of realty could be clarified by more consistent court decisions. The cases

60. Sheehan v. McKinstry, 105 Or. 473, 484-85, 210 P. 167, 171 (1922).

should recognize on a consistent basis that the making of the contract changes the vendor's interest in real estate from realty into personalty and that the vendee's interest, however slight, is an interest in realty and should be treated as such. Next, changes of ownership in or with respect to the vendee's interest should be fully recognized whether accruing by way of voluntary assignment or as the result of execution, attachment, or other process against a creditor's interest. The validity of forfeiture provisions in the contract should depend upon whether the vendee or the vendee's assigns have any interest worth protecting, and not upon the form of the agreement.

The idea that a contract of sale should be treated merely as a bond for title should be recognized as inadequate. Although the contract may create a bond for title on the part of the vendor once the vendee's obligations have been met, the bond for title is a part of the contract of sale and not something different and apart from it as used in installment sales. If equity really abhors forfeitures, as it professes to do, it should refuse to enforce them, even when they are contracted for, unless there is really nothing to forfeit. Installment sale contracts with respect to real estate should be recognized by the courts, the parties who use them, and the lawyers who draw them as something more than a panacea for all of the vendor's headaches when the vendee does not pay. Inflation is apt to take care of the vendor who gets his property back, even if the vendee does not.