

## LAND CONTRACT SALES

### I. Overview

A land contract is an agreement for the sale of real estate where the buyer (sometimes called the vendee) makes an initial down payment to the seller (sometimes called the vendor) and pays the remainder of the purchase price, plus interest, in installments over a period of time, usually several years. The interest rate charged under a land contract cannot lawfully exceed 11% per year.

Generally, the buyer takes possession of the property when the land contract is signed. However, the buyer does not acquire full ownership – or *legal title* – to the property until buyer makes the last payment under the land contract and the purchase price is paid in full. In the meantime, the buyer has *equitable title* to the property. This means the buyer has *some* interest in the property short of full ownership. Once the buyer pays the full purchase price, the seller delivers the deed to the buyer and conveys full title to the property. Ideally, when the land contract is signed the deed will be held in escrow with a title company who then records the deed when the land contract is paid in full.

A land contract may be an attractive option for buyers who do not have sufficient funds for a large down payment, or who cannot qualify for a loan with a financial institution. In essence, the seller in a land contract transaction loans the purchase price (other than the down payment) to the buyer who in turn makes regular payments directly to the seller. Therefore, a land contract transaction generally does not involve banks, mortgages, or promissory notes. Sellers and buyers should beware, however, that a sale by land contract of property that is already mortgaged may result in a default of that mortgage.

From a seller's perspective, a land contract is advantageous because the seller retains legal title to the property until the full purchase price is paid. In addition, the seller has the option of foreclosing or forfeiting in the event the buyer defaults on the land contract. Sellers should be aware that even though the land contract may require that the buyer pay the real estate taxes on the property, if the buyer fails to do so, the taxes remain due and can become a lien on the property that may ultimately be foreclosed upon if not paid. Similarly, if the buyer is to keep the property insured, the seller will want to obtain such insurance if the buyer fails to do so.

### II. Buyer Default

When a buyer fails to make payments or otherwise breaches the contract, a seller should look to the land contract in order to determine the parties' rights and obligations. Generally, in the event of a default by the buyer, a land contract will give the seller the option of pursuing specific performance (suing to enforce the provision breached) or of regaining possession of the property, which can be accomplished by one of two means:

1. seeking forfeiture of the land contract; or
2. foreclosing on and selling the land contract property.

Generally, a seller must use the court system in order to regain possession of the property and evict a land contract buyer who has failed to meet the requirements of the land contract. The method used for regaining possession of the property must be set forth in the land contract itself.

### III. Land Contract Forfeiture

A seller may regain possession of land contract property through forfeiture if (i) the land contract expressly provides for forfeiture and termination of the land contract, and (ii) the buyer has either failed to make payment of money required to be paid or has materially breached the land contract (e.g., failed to pay taxes, keep the property insured, etc.).

Procedure to regain possession of the property through forfeiture:

1. Seller must provide the buyer with a written notice of forfeiture describing the default (for example, if the default is nonpayment, the notice must specify the unpaid amount and the dates on which the payments were due). MCL 600.5728.
2. The buyer has at least 15 days (or more if stated in the land contract) to correct the default by paying the money due or complying with the provisions of the land contract allegedly breached. If the buyer fails to do so, or to reach an agreement otherwise with the seller, the seller may take legal action. MCL 600.5728.
3. The seller must file a summons and complaint, together with a copy of the land contract, the notice of forfeiture, and proof of service with the appropriate court – generally the district court in the municipality where the property is located. The plaintiff (usually the seller) must obtain personal service upon all defendants (usually the buyers) or as otherwise allowed by the Michigan Court Rules (MCR 2.105. MCR 4.202(F)).
4. The court will deliver or mail to the buyer the summons and complaint, which will provide the date and time on which the court will hold a hearing (usually called a summary proceeding).
5. If the seller is successful at the hearing, the judge will enter a judgment in favor of the seller. However, even if the seller prevails, the buyer does not have to vacate the property right away. Instead, the buyer will have either, 90 days if less than 50% of the purchase price has been paid, or 180 days if more than 50% of the purchase price has been paid following the entry of judgment in which to pay the missed payments and court costs and/or to correct any other breach of the land contract. MCL 600.5744(3). If the buyer does so, he or she can remain in possession of the property. In fact, the buyer has an absolute right to remain in possession if it pays the full judgment amount during the applicable time period. This right is called the “equitable right of redemption.”
6. After a judgment of possession has been entered, if the buyer fails to timely pay the full amount or correct the breach the seller should ask the court to issue its final order (called a “writ of restitution”), after which the buyer no longer has the right to pay the judgment amount in order to remain on the property; that is, the buyer loses the equitable right of redemption once the writ of restitution has been entered. After the writ of restitution has been entered by the court, the seller then hires the court officer to evict the buyer from the property, just as a tenant would be evicted from rental property. Even if the buyer has voluntarily moved out, obtaining a court ordered writ of restitution may be necessary to eliminate any concern that the buyer’s right as an owner of the property has been extinguished. For example, sellers who attempt to re-sell the property may be required by the new buyer’s lender (if not sold on land contract), or the title insurance company, to record the writ of restitution in the applicable register of deeds in order to prove that buyer’s interest has been extinguished.

*Advantages of Forfeiture:*

1. A seller is usually able to regain possession much quicker than in a foreclosure proceeding.
2. The buyer's time period for redeeming the property may be shorter than in a foreclosure.

#### *Disadvantages of Forfeiture:*

1. A buyer may prevent the loss of the property by merely paying the past due payments included in the judgment of possession. The buyer is not required to make any of the payments that come due during the 90 or 180-day redemption period. Therefore, a seller may need to restart the forfeiture process more than once or turn to foreclosure as a means to resolve issues with a nonpaying buyer.
2. Unlike foreclosure, when a seller has regained possession of the property via forfeiture, the buyer typically has no further liability under the land contract. In other words, the seller's sole remedy is repossessing the property – the seller generally cannot proceed against the buyer to recover amounts due under the contract.

#### **IV. Land Contract Foreclosure**

A seller may prefer to regain possession of land contract property through foreclosure if (i) the land contract expressly provides for foreclosure and contains an acceleration provision, and (ii) the buyer has breached the land contract. The procedure for foreclosing on a land contract is in essence the same as foreclosing on a real estate mortgage. The legal process begins when the seller files a complaint in the circuit court and obtains a court order for the sale of the property.

#### *Advantages of Foreclosure:*

1. A buyer may be required to pay the entire balance due under the land contract to prevent foreclosure. This is called "acceleration" of the entire balance due in case of a default and most land contracts contain such a provision.
2. Even if the property is returned to the seller the buyer may remain personally liable to the seller for the portion of the balance due under the land contract which was not satisfied by the sale of the property (the "deficiency amount").

#### *Disadvantages of Foreclosure:*

1. A foreclosure sale cannot take place until 3 months after filing a complaint with the court.
2. The buyer will have 6 months after a foreclosure sale to pay the principal and interest due, with costs, and "redeem" or buy back the property.

#### **V. Seller Default**

Generally, upon a buyer's fulfillment of the land contract, the seller must give the buyer the required deed conveying the property free of liens created by the seller (e.g., the seller's mortgage). A seller who fails to provide the required deed may be in breach of the contract. If the seller is unwilling or unable to give the required deed, the buyer may have various options, including legal action for:

1. Specific performance (where a court orders the seller to 'perform' under the contract and give buyer the required deed);
2. Quiet title (where a court determines which party has title to the property to the exclusion of everyone else);
3. Cancellation of the land contract (where the buyer seeks a return of the money paid under the contract and the property is returned to the seller);
4. Money damages.

Above all, both the buyer and the seller may be able to avoid problems if they talk to each other at the time questions or concerns first arise regarding the land contract.

*This pamphlet should not be used in place of legal assistance. Before signing a land contract and in the event of a land contract dispute, seek legal advice.*

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