

**Professional Training for Farm Succession Advisors in New England  
The Falls Center  
21 Front Street  
Manchester, NH 03102**

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Other Land Access Tools**

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**Using a Land Contract for the Transfer of Farmland**

A land contract is a long term executory contract for the sale of land. The buyer agrees to make regular principal and interest payments, usually annually, to the seller. The seller of the land agrees to transfer title to the buyer once all payments have been made. The buyer takes possession when the contract is first entered. Land contracts are called by lots of different names: land contract, installment land contract, contract for deed, etc.

A land contract can provide an exiting farmer with a seemingly simple means of transferring farmland to a family or non-family member. Payments provided in installments can ease the tax consequences for the recognition of gain on the sale. A new farmer unable to obtain commercial credit can obtain possession of land without a significant down payment. An exiting farmer can also retain a life estate in the homestead on the farm.

There are risks, however. Default, waste, a decline in land values, and bankruptcy of the buyer are all risks to the seller. The buyer, too, risks forfeiting possession and all payments made if a payment is missed.

**I. Risk of Default, Risk of Forfeiture**

Land contract buyers are often ineligible for commercial or FSA lending and a land contract can offer an alternative, seller financed route to land ownership. Because the seller is taking on the significant risk of default, a land contract almost always will provide that if the buyer defaults on a payment, he forfeits possession of the property and all the payments made to date. This “forfeiture clause” is sometimes considered a form of liquidated damages. As a measure of liquidated damages, it can become unreasonable where the buyer has made most of the contract payments and made significant improvements to the farm prior to default.

Treatment and enforcement of a forfeiture clause vary a great deal by jurisdiction. Some states will enforce a forfeiture clause but require that the seller provide a brief right to cure and a

right of redemption upon full payment of the contract. (For example this is the approach taken by statute in Maine.) Some courts have adopted a restitution theory requiring a seller to return any payments to the extent that they exceed the seller's actual damages. Some of these states will use a rental value theory of damages, others will look at the fair market value of the land at the time of default in relation to the contract price. (For example, market value is used to determine reasonable damages in land contract cases in New Hampshire). Also see *Freedman v. Rector* 230 P 2d 629 (Cal. 1951).

The Restatement of Property §3.4(a) (1997) takes the position that a land contract should be regarded as a mortgage with the seller's remedy being foreclosure. If the property sells foreclosure for more than the contract price, the buyer gets the excess. If the property sells at foreclosure for less than the contract price the seller has a right to the deficiency. In this way, the seller gets the benefit of his bargain. Several states have adopted this approach. See *Skendzel v. Marshal* 301 N.E 2d 641 (Ind. 1973) and *Kubany v. Woods*, 622 So. 2d 22 (Fla. Dist. Ct. App. 1993)

The treatment of forfeiture provisions in New England jurisdictions are as varied as the rest of the country. And in several jurisdictions, there is little to no guidance on whether a forfeiture clause will be enforced.

#### **Maine:**

Maine has adopted a Land Contract statute for any contract for the sale of real estate requiring at least 5 or more installment payments exclusive of a down payment. 33 M.R.S. §481.2

The statute includes a detailed list of required land contract provisions including the following:

*K. A statement which explains that the contract is not a mortgage and that the purchaser does not obtain title to the property until the purchase price is paid in full.*

*L. A statement of the rights of the buyer established by Title 14, §6111 to cure a default by the buyer.*

14 M.R.S. §6111.1, however, only provides a right to cure in the case of "residential property located in the state when the mortgagor is occupying all or a portion of the property as the mortgagor's primary residence and the mortgage secures a loan for personal, family or household use..."

33 M.R.S. §6203-F the state's foreclosure statute also provides a right to cure, right of redemption and an opportunity to extend the right of redemption for up to one year for a foreclosure upon a bond for deed or for contracts for the sale of real estate. This provision, however, also only applies to residential real estate.

In *Thurston v. Galvin*, 2014 ME 76, 94 A 3d 16(2014), the court considered whether a seller under a land contract in default was entitled to a writ of possession or if instead the property was to be sold at the expiration of the redemption period as dictated by the mortgage foreclosure statutes. The court said:

*In land installment contracts generally, and certainly in this one, the purchaser's contractual rights are limited to possession of the premises until she has made the final payment.[5] The vendor retains legal title to the property. See Thompson v. Skowhegan Sav. Bank, 433 A.2d 434, 436 (Me. 1981) (stating that "the vendor of land under an installment sale contract retains legal title to the land"). Accordingly, because Galvin's sole rights are possessory rights, those are the only rights affected by the section 6203-F foreclosure process. Ending Galvin's right to possess the property, but then compelling the Thurstons to submit the property to a public sale would implicate the vendors' rights in the property, rather than the purchaser's rights. The plain meaning of section 6203-F precludes such an interpretation. Here, the only applicable provisions of 14 M.R.S. § § 6321-6325 are those that apply to Galvin's right to possess to the property, i.e., those provisions that concern Galvin's rights of redemption. As to those, there is no dispute.*

*We recognize that a growing number of courts have held that a land installment contract should be treated as a mortgage, at least in those cases where the purchaser's payments have been more than nominal, so as to afford a purchaser rights beyond redemption. See Restatement (Third) of Property: Mortgages § 3.4 cmt. b(3) & reporters' note (1997) (compiling cases); Grant S. Nelson, *The Contract for Deed As A Mortgage: The Case for the Restatement Approach*, 1998 BYU L. Rev. 1111, 1115-16 & n.58. We note, however, that the contract between Galvin and the Thurstons contains no language suggesting that Galvin should be permitted to recoup any of the payments made before breaching the contract. In addition, our treatment of a land installment contract as a mortgage would render meaningless the words "the rights of the purchaser in the contract" in section 6203-F. This we cannot do. See *Blue Yonder, LLC v. State Tax Assessor*, 2011 ME 49, ¶ 13, 17 A.3d 667 ("[W]e must not interpret the statutes in a manner that would render some of the language superfluous and meaningless."). To alter the statutory protections enjoyed by a purchaser of land through a land installment contract "is the province of the Legislature, not of this Court." *Mason v. Town of Readfield*, 1998 ME 201, ¶ 8, 715 A.2d 179. *Thurston* at 21.*

## **Vermont**

The only case in Vermont to mention Land Contracts stands for the proposition that a breach of a land contract does not create the relationship of a landlord / tenant or render the buyer subject to the summary ejectment procedures available under landlord tenant law. The court does make the statement that land contracts are "regarded in equity as analogous to equitable mortgages." *Strengowski v. Gomes* 128 Vt. 555, 268 A. 2d 749 (1970)

Dicta in full: *Contracts of this character, contemplating the purchaser's use and occupancy of the premises, are regarded in equity as analogous to equitable mortgages. The right of*

*forfeiture or defeasance for a breach of the covenants contained in the contract was only in aid of the security. Van Dyke and Drew v. Cole, 81 Vt. 379, 396, 397, 70 A. 593. Strenowski at 750.*

## **New Hampshire**

In *Newcomb v. Ray*, 99 N.H. 463(1955) the court ordered restitution to a defaulting buyer under a land contract reasoning as follows:

*In the hands of the defendants, the part payments made by the plaintiffs represent a net benefit to the defendants to the extent that, when added to the net amount actually received by the defendants from the sale of the property, they exceed the net amount which the defendants would have received from the property if the plaintiffs had completed the purchase of it. Omitting consideration of the legal expenses of \$84.10, an item chargeable to the defendants in any event upon the sale of the property, the net amount which the defendants would have received if the plaintiffs had completed their purchase would have been \$29,700, the purchase price of \$33,000 less the real estate commission of \$3,300. On the same basis, the net amount actually received from the sale of the property was \$24,700, the sale price of \$26,000 less the real estate commission of \$1,300. The net amount of \$24,700 actually received by the defendants from the sale plus the net amount of \$6,700 received by them from the plaintiffs totals \$31,400. The net benefit to the defendants is the difference between this total and the \$29,700 which they would have received had the plaintiffs performed the contract. The plaintiffs are entitled to that part of \$1,700 which is 'in excess of the harm' caused to the defendants by the plaintiffs' breach of the contract. (emphasis supplied)*

Similarly, in *Randall v. Riel*, 123 N.H. 757 (1983) the court remanded a forfeiture case saying:

*At the hearing on remand, reasonable damages should be determined as the difference between the market value of the property and the contract price, plus such other special damages as may have resulted from the plaintiff's breach of the contract for deed. Cf. *Bower v. Davis & Symonds Lumber Co.*, 119 N.H. 605, 609, 406 A.2d 119, 122 (1979) (\$10,000 liquidated damages provision was reasonable because property was sold in an arms-length transaction after breach for \$90,000, which was less than \$100,000 contract price).*

## **Massachusetts**

In *Cameron v. Gunstock Acres, Inc.*, 370 Mass 378 (1976) the court notes:

*A purchaser under an instalment land contract resembles a mortgagor in some respects. *Barrell v. Britton*, 244 Mass. 273, 278--279, 138 N.E. 579 (1923). But the plaintiff does not tell us what rights he claims under the law of New Hampshire, which would seem to control any mortgage analogy. Cf. *Churchill v. Bigelow*, 333 Mass. 196, 198, 129 N.E.2d 903 (1955).*

## **Rhode Island**

There is no case law or statutory provisions on land contracts in Rhode Island.

## **Connecticut**

La Fleur v. Pohronezny, WWMCV064003658S the Superior Court of Connecticut upheld a forfeiture provision in a bond for deed, characterizing it as a valid liquidated damages clause, saying:

*"Enforcement of liquidated damages clause is subject to well established legal criteria. First, Connecticut recognizes the right of parties to agree to liquidated damages in the form of forfeiture of a deposit or a portion thereof for breach of an agreement to purchase real estate." Willert v. Russo, Superior Court, judicial district Danbury, Docket No. CV 07 5002983 (May 4, 2009, Sommer, J.). Second, a liquidated damage clause in a contract will be upheld if the following requisite conditions are met: "(1) The damage which was to be expected as a result of a breach of the contract was uncertain in amount or difficult to prove; (2) there was an intent on the part of the parties to liquidate damages in advance; and (3) the amount stipulated was reasonable in the sense that it was not greatly disproportionate to the amount of the damage which, as the parties looked forward, seemed to be the presumable loss which would be sustained by the contractee in the event of a breach of the contract." (Citation omitted; Internal quotation marks omitted.) Bellemare v. Wachovia Mortgage Corp., 284 Conn. 193, 203, 931 A.2d 916(2007). "The party seeking to repudiate a clause that fixes a sum as damages has the burden of showing that the agreed upon sum is so exorbitant as to be in the nature of a penalty." Syncsort, Inc. v. Indata Services, 14 Conn.App. 481, 485, 541 A.2d 543, cert. denied, 209 Conn. 804, 548 A.2d 443 (1988).*

And later:

*The court finds based on the evidence before it that the damage to the plaintiff is uncertain and difficult to prove. Additionally as evidenced by the presence of the liquidated damages clause in the bond for deed, it is clear that the parties intended to liquidate damages. Finally the forfeiture of the defendants' interests in the property and the sums paid prior to the breach is reasonable and not disproportionate to what the presumptive amount of damages would have been in the event of breach. Accordingly the court orders that any interest the defendants have in the property and all moneys paid under the bond for deed be forfeited.*

## **II. FSA Land Contract Guarantee Program**

Land contracts involve risks for both buyers and sellers. Default, waste, a decline in land values, and bankruptcy of the buyer are all risks to the seller. The buyer, too, risks forfeiting possession and all payments made if a payment is missed.

A new Land Contract Guarantee Program included in the 2014 farm bill could help mitigate some of the risks of land contracts, at least for sellers. How a buyer will fare in the event of

default even with an FSA guarantee is still very much a function of each state's treatment of land contracts.

FSA defines a land contract as follows: An installment contract executed between a buyer and a seller for the sale of real property, in which complete fee title ownership of the property is not transferred until all payments under the contract have been made. 7 C.F.R. §761.2(b)

A. FSA offers two types of land contract guarantees.

1. Prompt payment guarantee will guarantee payment of an amount not to exceed three amortized annual payments, plus real estate taxes and insurance for the period covered by the annual installment.
2. The standard guarantee program will guarantee an amount equal to 90% of the outstanding principal under the land contract. Outstanding principal is calculated as the outstanding balance less the liquidated or appraised value of the real estate.

B. **Eligibility**

1. Buyer must be a beginning (BF) or socially disadvantaged farmer or rancher (SDFR.) 7 C.F.R. §763.5(b)(1)

A beginning farmer will not have operated a farm for more than 10 years. If an entity, all members must meet this definition. The BF must materially and substantially participate in the operation. Must not own farmland or owns farm property which does not exceed 30 percent of the average farm acreage of the farms in the county where the property is located determined from the most recent Census of Agriculture. The BF must demonstrate that available resources of the BF and spouse are insufficient to enable the BF to enter or continue farming on a viable scale. 7 C.F.R. §761.2(b)

A socially disadvantaged farmer or rancher is a member of a group whose members have been subject to racial, ethnic or gender prejudice because of their identity as members of a group without regard to their individual qualities. These groups consist of American Indians or Alaskan Natives, Asians, Black or African Americans, Native Hawaiians or other Pacific Islanders, Hispanics, and women. For an entity, the majority interest must be held by SDFR individuals. For married couples, the SDFR individual must have at least a 50% ownership interest in the farm business and make most of the management decisions, contribute a significant amount of labor and generally be recognized as the operator of the farm. 7 C.F.R. §761.2(b)

2. Buyer must be the owner and operator of a "family farm" after the contract is completed. 7 C.F.R. §763.5(b)(2)

A family farm is defined as a business that produced agricultural commodities for sale in sufficient quantities so that it is recognized as a farm rather than a rural residence; where the majority of day-to-day physical labor and operational and management decisions are made by the borrower and persons related to the borrower by blood or marriage or in the case of an entity, the members responsible for operating the farm. The farm may use reasonable amounts of temporary labor for seasonal peak workload periods. 7 C.F.R. §761.2(b)

### 3. Farming Experience

Buyer must have participated in the business operations of the farm for at least 3 years out of the last 10. One year of postsecondary agriculture courses may count toward the 3-year requirement. 7 C.F.R. §763.5(b)(3)

### 4. Citizenship Status

The buyer and in the case of an entity, all members must be citizens of the United States or be a qualified alien under the applicable Federal immigration laws. A qualified alien includes anyone who is lawfully admitted for permanent residence under the Immigration and Nationality Act. 8 U.S.C §1641 and 7 C.F.R. §763.5(b)(7)

### 5. Credit History

The buyer must have an acceptable credit history demonstrating satisfactory debt repayment. A history of failure to pay will demonstrate an unacceptable credit history but not isolated instances of late payments or a lack of a credit history.

## C. Limitations

The purchase price of the farm may not exceed the lesser of \$500,000 or the current fair market value of the property. Existing land contracts are not eligible for the program. A guarantee may not be used to establish or support non-eligible enterprises. 7 C.F.R. §763.6

## D. Feasibility

The buyers proposed operation must be feasible. Projected income, expenses and production estimates must be based on the buyer's last three production cycles. For those farming less than 3 years, a combination of actual history and other reliable sources may be used. When a feasible plan depends on income from sources other than farming, the income must be dependable and likely to continue. 7 C.F.R. §763.10

## E. Contract Terms and Modifications

The buyer must provide a minimum down payment of five percent of the purchase price of the farm. The interest rate must be a fixed rate not to exceed the Agency's direct farm ownership

loan interest rate in effect at the time the guarantee is approved plus three percent. The loan must be amortized for a minimum of 20 years with equal annual installments during the term of the guarantee. Balloon payments, are prohibited during the 10 year terms of the guarantee. 7 C.F.R. §763.12

The seller and the buyer may modify the contract to lower the interest rate and the corresponding annual installments without Agency approval. With written approval from the Agency the buyer and seller may defer installments, lease or sublease, transfer and assumption and assignment provided the modification is justified by a feasible plan with reasonable projections for the upcoming operating cycle.

#### **F. Prompt Payment Guarantee**

##### **a. Loss limits, guarantee period and conditions**

1. The maximum loss amount is limited to three amortized annual installments or an amount equal to three annual installments plus taxes and insurance incurred during the period covered by the installments. 7 C.F.R §763.11(a)
2. The guarantee period shall not exceed 10 years from the effective date of the contract. 7 C.F.R §763.11(b)
3. The seller must select an escrow agent who will receive the land contract payments; notify the Agency and the seller if the buyer defaults; make a demand upon the Agency to pay the missed payment; and perform other servicing duties. 7 C.F.R. §763.18

##### **b. Default**

1. The escrow agent must make a written demand to the buyer for the payment of the defaulted amount within 30 days of the missed payment, taxes, or insurance and send a copy of the demand letter to the Agency and to the seller. 7 C.F.R §763.20(a)(1)
2. The escrow agent must make a written demand of the Agency within 90 days from the original payment, taxes or insurance due date, for the missed payment in the event the buyer has not made the payment. 7 C.F.R §763.20(a)(2)
3. Any amount paid by the Agency as a result of an approved loss claim is immediately due and payable by the buyer. If the debt is not restructured into a payment plan the Agency may use all remedies available to collect the debt. The debt may be rescheduled for repayment consistent with the buyer's ability to pay, not to exceed 7 years. 7 C.F.R. §763.21

The Agency will cover only 3 missed payments. During this period the buyer will retain in possession of the land. If the buyer defaults the fourth time, the seller's rights will be dictated by the contract between the two parties and how that particular state treats land contracts. If the contract and state law favor forfeiture provisions, the buyer will have to vacate the

property and will lose any payments made. Or state law (or the contract) could require some measure of restitution to the buyer.

## **G. Standard Guarantee Plan**

### **a. Guarantee period and conditions**

1. The guarantee period shall not exceed 10 years from the effective date of the contract. 7 C.F.R §763.11(b)
2. The guarantee will cover an amount not to exceed 90 percent of the outstanding principal balance. 7 C.F.R §763.11(a)(2)
3. The seller must use a third-party servicing agent approved by the Agency who will receive installment payments and send them to the seller; provide evidence to the Agency that property taxes are paid; perform an annual physical inspection of the farm; Obtain a balance sheet and income statement and cash flow on an annual basis; notify the Agency if the buyer defaults; and service the delinquent accounts. 7 C.F.R. §763.18(b)

### **b. Default**

1. If the buyer fails to pay an annual installment then the seller has the option of either liquidating the property or having the loss amount established by the Agency by an appraisal of the real estate. 7 C.F.R. §763.20(b)
2. The servicing agent must make a written demand to the buyer within 30 days of the missed payment. If the payment is not made within 60 days of the demand letter the servicing agent must immediately inform the Agency whether seller will utilize the liquidation method or the appraisal method to establish the loss amount. 7 C.F.R. §763.20(b)(1)

**Liquidation Method:** The servicing agent will submit a liquidation plan to the Agency and complete liquidation within 12 months of the missed payment unless prevented by bankruptcy, redemption rights, or other legal action. Credit an amount equal to the sales price received in liquidation to the principal balance of the land contract. 7 C.F.R. §763.20(b)(2)(i)

**Appraisal Method:** The Agency will complete an appraisal on the real estate and the loss claim will be based on the difference between the appraised value at the time of the loss and the unpaid principal balance of the land contract. The Agency will retain a lien on the property in the amount of the loss claim. If the property sells

within 5 years from the date of the loss payment the seller must repay the Agency the difference, up to the amount of the loss claim. 7 C.F.R. §763.20(b)(2)(ii)

3. Any amount paid by the Agency as a result of an approved loss claim is immediately due and payable by the buyer. If the debt is not restructured into a payment plan the Agency may use all remedies available to collect the debt. The debt may be rescheduled for repayment consistent with the buyer's ability to pay, not to exceed 7 years. 7 C.F.R. §763.21

Whichever route the seller chooses, appraisal or liquidation, FSA will ensure that the seller gets the benefit of his bargain. The buyer's rights upon default will be dictated by the terms of the contract between the parties and that state's laws on forfeiture. If forfeiture is favored, the buyer could lose all payments made under the contract. If state law provides an opportunity for some form of restitution of payments made, the buyer could exercise those rights.

### **III. Risk of Bankruptcy**

A land contracts may extend for 10 or even 20 years. A lot can happen in that time span, including the seller or the buyer filing bankruptcy.

Debtors in Bankruptcy are allowed to "assume, assign or reject" executory contracts. If the seller is the debtor, however, the code provides certain protections to buyers under a land contract. If the buyer is in possession, the buyer has the option of terminating the contract or remaining in possession and continue to make the payments. The Bankruptcy trustee will receive payments and deliver title to the buyer when all the payments have been made. 11 U.S.C. §365.

If the buyer is the debtor there is less clarity with respect to whether the land contract will be treated as an executory contract or as a mortgage. If the latter, the seller will have a security interest in the land up to the value of the land. If the seller is undersecured, the balance of claim is treated as an unsecured debt and a large portion of it may be subject to discharge.

If the land contract is treated as an executory contract the buyer must assume, reject or assign the contract without modifying its terms or discharging any of the debt. Bankruptcy Courts will look to state law in deciding whether to characterize a land contract as a mortgage or an executory contract.

#### **IV. Elements of a Land Contract / Checklist**

(Adapted from Maine's land contract statute at 33 M.R.S §482 and "Financing Farmland with an Effective Land Contract: A Toolbox" by Farm Commons.)

##### **Land Contract Elements**

1. The full names and post-office addresses of all the parties to the contract.
2. The date the contract is signed by each party.
3. A legal description of the property conveyed.
4. The sale price of the property conveyed.
5. Any charges or fees for services included in the contract separate from the sale price.
6. The amount of the buyer's down payment.
7. The principal balance owed by the buyer. Which is the sum of the sales price of the property conveyed and the amount of any charges or fees for services included in the contract separate from the sales price.
8. The amount and due date of each installment payment and the total number of installment payments.
9. The interest rate on the unpaid balance and the method of determining the interest rate.
10. Will the land contract include an acceleration clause? Will the land contract include a forfeiture provision?
11. Will the land contract provide a right to cure?
12. A statement indicating the seller has good and marketable title.
13. A promise that the seller will deliver a warranty or other type of deed upon completion of the contract.
14. Will either or both buyer and seller have a right to mortgage or assign their interest in the contract?
15. A provision that, if the seller defaults on any mortgage on the property, the buyer may pay on the mortgage and receive credit on the land installment contract.
16. A requirement that the buyer shall be responsible for the payment of taxes, assessments and other charges against the property from the date of the contract, unless agreed to the contrary.
17. A provision that the buyer has the right to accelerate or prepay any installment payments without penalty, unless agreed to the contrary.
18. A provision that states which party will be responsible for the payment of insurance and which party will be responsible for damages to the property.
19. A promise on the part of the buyer to not commit waste, damage or destruction of the property.
20. A provision that states what happens if the land is condemned or the government takes the land.
21. How and whether the land contract can be amended.
22. A force majeure provision.
23. A statement that the land contract will be recorded.