

**FARM LEGAL SERIES**

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## Termination of Contracts for Deed

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### INTRODUCTION

If a farm debtor is unable to perform under a contract for deed, the rights of the parties are determined by state law. In general, if the farmer defaults on his or her contract for deed, the seller will have the right to terminate the contract and take the land back. Minnesota law is very specific with respect to the process of terminating a contract for deed. Specific time periods are provided by the statutes and must be followed to the letter by the creditor who is attempting to terminate a contract for deed. Failure to follow each step of the termination process properly may result in an invalid termination.

### DEFAULT

A typical contract for deed includes several terms that require the purchaser to do more than merely make the necessary periodic payments. For example, the purchaser is required to maintain insurance on the premises, pay all real estate taxes and maintain the premises for the benefit of both the purchaser and the seller. In addition, contracts for deed may include provisions prohibiting the sale of all or any portion of the premises without the prior written consent of the seller. Such provisions are known as due on sale clauses. If the purchaser fails to abide by any of the terms in the contract, the purchaser is in default.

The standard form contract for deed in use in Minnesota provides that the time of performance by the purchaser of the terms of a contract is an essential part of the contract. Thus, in most cases, the failure of the purchaser to comply with the terms of a contract for deed on the date specified by the contract constitutes a default.

### CREDITOR'S OPTIONS UPON DEFAULT

Once a default has occurred, the creditor has several available options besides simply terminating the contract for deed.

#### **Deed in Lieu of Termination**

The creditor can negotiate an arrangement with the debtor whereby the debtor gives the property back to the creditor in satisfaction of the underlying debt. Such a procedure is known as the debtor giving the creditor a "deed in lieu of termination." When a debtor undertakes such action, the debtor is voluntarily surrendering his or her redemption or reinstatement rights (discussed below). Because such an action results in the transfer of ownership and the right to possession, Minnesota courts have long held that such transactions are subject to close scrutiny to protect the debtor from oppression by the creditor. In order for such an agreement to be upheld by a court, it must not be the result of any oppressive means or overreaching on the part of the creditors and adequate consideration must be given.

### **Legal Action**

A second course of action for the creditor is to bring a lawsuit on the underlying debt based on the promises of the debtor contained in the contract for deed. If the value of the real property is less than the amount due under the contract for deed, the creditor may well elect to bring an action seeking payment of the amount due.

A significant difference between a mortgage and a contract for deed may be realized if the lender decides to sue. A promissory note and mortgage both typically include an acceleration clause, but the standard form contract for deed in use in Minnesota does not. As a result, the seller under a contract for deed, should he or she elect to sue his or her purchaser for the purchase price, must do so for each installment payment as it comes due. That is, without such a clause, he or she cannot bring one lawsuit for the entire balance due under the contract for deed. This limitation may make such an alternative a less attractive proposition to the seller. Such a course of action may be unattractive to a creditor unless the purchaser has other nonexempt assets that can be reached to satisfy the underlying debt.

### **Mediation**

Where a contract for deed involves agricultural real estate, Minnesota's farmer-lender mediation statute generally requires the seller to offer mediation of the obligation to the purchaser prior to beginning contract for deed cancellation proceedings. The farmer-lender mediation statute began requiring mediation in 1986, with the statute's expiration date being extended in the years following original passage. Generally, the statute requires, among other things, that the seller under a contract for deed on agricultural real estate seeking to cancel the contract first send notice to the purchaser and offer the purchaser the

opportunity to mediate a resolution to the contract for deed obligation prior to beginning such action. If the purchaser elects to mediate the obligation, the seller's cancellation of the contract for deed can be suspended for a period of up to 90 days pending completion of the mediation. Where the debt involved has been scheduled by the purchaser in a bankruptcy or involved in a previous farmer-lender mediation, the debt is not subject to the farmer-lender mediation statute and the seller can initiate cancellation proceedings without first offering mediation.

### **STEPS IN TERMINATION OF CONTRACTS FOR DEED**

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

1. The nature of the default (e.g., nonpayment).
2. The period of time within which the purchaser may reinstate.
3. A statement that the purchaser must either make payments in the amount owed, plus costs of service, attorneys' fees incurred and other amounts due under the cancellation statute depending on the date of the contract (discussed below); or secure a court order suspending termination of the contract for deed.
4. The name, address and telephone number of the seller or an attorney authorized by the seller to accept payments.
5. Certain specific language required by law that notifies the purchaser of the

consequences of his or her failure to comply with the notice, including that the contract will be terminated, that the purchaser will lose his or her right to possession of the property, and that the purchaser will lose all the money paid on the contract.

### **Special Requirements**

For contracts for deed executed on or after May 1, 1980, the notice also must state that the purchaser must pay any additional payments due the seller under the contract for deed through the date payment is made, rather than the date of the notice. For contracts for deed executed on or after August 1, 1985, the notice must state that the purchaser is further required to pay two percent of the amount in default at the time of service of the notice, not including balloon payment, taxes, assessments, mortgages or prior contracts assumed by the purchaser.

For the seller to recover attorneys' fees under a contract for deed executed on or before July 31, 1985, some part of the conditions of default must have existed for at least 45 days prior to the date of service of the notice upon the purchaser. For contracts for deed executed on or after August 1, 1985, this period of default is reduced to 30 days.

### **Notice**

The notice must be served upon the purchaser in the same manner as a summons according to the Minnesota Rules of Civil Procedure. Three weeks' published notice has the same effect as personal service of the notice upon the purchaser provided that certain procedures are followed, but the cure period is expanded to 90 days where service is by publication. Besides serving the purchaser, serving other parties—such as mortgagees, judgment creditors or other lien claimants—may be required.

### **Termination**

The right of the purchaser to reinstate the contract is absolute, provided that he or she complies with the payment of all sums required. If the purchaser fails to comply with the notice, the contract will terminate.

Upon termination, the purchaser will lose all sums that have previously been paid on the contract, the right to possession of the property and the right to assert any claims or defenses against the sellers. The purchaser may be evicted from the premises by the seller. Once the termination has been completed, however, the seller can no longer maintain any action for a deficiency judgment against the purchaser.

### Cure or Reinstatement Period

The period allowed to cure the defaults and the conditions of a contract for deed varies, depending on the date on which the contract

was executed and on the percentage of the purchase price that has been paid by the purchaser, as follows:

CONTRACT DATE	PERCENTAGE PAID	CURE PERIOD
<i>Before</i> August 2, 1976	Any	30 Days
<i>After</i> August 1, 1976 and <i>Before</i> May 1, 1980	Less than 30%	30 Days
	Between 30-50%	45 Days
	50% or More	60 Days
<i>On or After</i> May 1, 1980 and <i>Before</i> August 1, 1985	Less than 10%	30 Days
	Between 10-25%	60 Days
	25% or More	90 Days
August 1, 1985 or <i>Later</i>	Any	60 Days

### Right of First Refusal

Where the real estate subject to contract for deed cancellation is agricultural land or a farm homestead and the seller is a government agency, limited partnership or corporation, Minnesota law provides the purchaser with certain rights of first refusal upon the rental or resale of the property by the seller. The seller cannot offer the property for sale or lease until it has provided written notice to the purchaser at

least 14 days in advance. When a third party buyer or lessee is found, the seller must then offer to sell or lease the property to the purchaser upon the same terms as the offer made by such third party. The purchaser has a defined period of time within which to exercise his or her right of first refusal to either buy or lease the property on such terms. For leases, it is within 15 days of the seller's written offer to the purchaser, and for sales, it is within 65 days of the seller's

written offer to the purchaser. If the purchaser exercises his or her right of first refusal, he or she must fully perform the terms of the sale or lease within ten days of such exercise.

The purchaser can elect to purchase or lease a portion of the total property involved, but only where the portion is of a size, configuration and location which does not unreasonably reduce access to or the value of the remaining property. The purchaser is not allowed to resell the property if the sale was arranged prior to his or her exercise of the right of first refusal. Where the property is resold by the purchaser within 270 days of the right of first refusal, there is a presumption, subject to proof to the contrary, that the sale was arranged ahead of

the exercise of the right of first refusal. Where the purchaser violates this prohibition, the purchaser will be liable for damages and attorneys' fees.

## CONCLUSION

Procedures under Minnesota law for terminating a contract for deed are complex and detailed. They prescribe specific time periods within which both parties must take certain actions. Such time periods are critical for both parties. Any person involved in such procedures should carefully examine the specific provisions of state law that apply to his or her case.

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