

Real Estate Contracts in New Mexico

Second Edition

LARRY BUCHMILLER

Published by



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SECURITY ESCROW CORPORATION

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SECURITY ESCROW CORPORATION

Founded by Mr. Buchmiller in 1975, Security Escrow is the oldest independent escrow company in New Mexico. It was the first escrow agent in New Mexico to utilize data processing equipment. In addition to servicing escrow accounts, the company markets its software and processing services to other businesses statewide through another company, Security Software Services, Inc.

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Standard Contract Forms

The real estate contract is sometimes prepared by lawyers as a custom-drafted legal document. Most practitioners have abandoned that practice, instead using one of two standard forms generally available from office supply stores. The relative advantages and disadvantages of both forms will be discussed throughout this book.

- "Form 103," originally prepared and copyrighted by a printing company, is the oldest form in general use. A specimen is included in the Forms Appendix as Form No. 1. Form 103 was developed before the high-inflation era of the 1960's, when very little property was sold by real estate contract. Improved property was usually re-financed, with the buyer paying "cash-to-loan." Contracts were generally used only for sales of vacant lots and undeveloped land. Because there were usually no pre-existing mortgages or contracts encumbering the property being sold, sales contracts were very simple. Form 103 was created to handle such sales. During the inflationary period after 1960, prices of improved property increased dramatically, along with interest rates. A growing number of potential buyers either could not afford the larger cash-to-loan down payment requirements, or could not qualify for refinancing mortgage loans. As a result, Form 103 was pressed into use for more complex sales transactions involving the assumption of pre-existing mortgages. Since Form 103 was not designed for such transactions, it was necessary for the form preparer to write and incorporate a considerable amount of specialized material into the form. With the later advent of "wrap-around" contracts and varying methods for calculating interest, Form 103 became unsuitable for use in most transactions. The alternatives were to either revert to custom drafting by lawyers or develop a new form.
- In 1980, the Realtors Association of New Mexico (RANM) developed a new real estate contract form - RANM Form No. 11 - designed to satisfy the requirements of more complex "owner-financed" sales transactions. The form, as revised in 1981, is included in the Forms Appendix as Form No. 2. There are some shortcomings in this form; however, it is vastly superior to Form 103 for modern real estate sales contracts.
- Shortly before this edition went to press, a committee of lawyers jointly appointed by the New Mexico Bar Association and the Realtors' Association of New Mexico completed work on the first revision of the RANM form 11 since 1981. The newly revised form is included in the forms appendix as form no. 3.

Terminology

Real Estate Contracts

Form 103 describes the seller of the property as the "Owner" and the buyer as "Purchaser." The 1981 RANM form uses "Seller" and "Purchaser"; the new RANM form replaces "Purchaser" with "Buyer". Court decisions refer to the seller and purchaser as "Vendor" and "Vendee." In this book,

the terms "Seller" and "Buyer" will be used, because they are the terms generally understood by the public, and because they are used in the new RANM REC form. For the sake of brevity, the initials "REC" will generally be substituted for "Real Estate Contract." In deeds of conveyance, "Grantor" means the seller and "Grantee" means the buyer of the property.

Notes and Mortgages

When the seller takes a mortgage as security for part of the purchase price, "mortgagor" is equivalent to "buyer", and "mortgagee" refers to the seller. When the mortgage secures financing provided by a third party, "mortgagor" means either "buyer" or "borrower", depending on the context, and "mortgagee" refers to the third-party lender.

Deeds of Trust

When a deed of trust is used as the security instrument, "mortgagor" refers to the buyer, "trustee" refers to the third-party holder lienholder, and "beneficiary" refers to the seller.

Courts

In this book, the New Mexico Supreme Court will be referred to as "the Supreme Court", and the New Mexico Court of Appeals as "the Court of Appeals". All other courts will be referred to by their full titles.

Court Decisions

Full citations and briefs of court decisions appear in the Case Law Appendix. In the text, court decisions will be referenced by the plaintiff's name only, with a reference to the page number in the Appendix ('CLA') where the brief of the decision is found. Example: See *Paperchase*, p.17 CLA.

Definitions (as found in Black's Law Dictionary and Ballantine's Law Dictionary)

Alienation. The transfer of the property and possession of land from one person to another.

Common law. All the statutory and case law background of England and the American colonies before the American revolution.

Fee Simple. An absolute estate in real property, unlimited as to duration, disposition and descendibility.

Feud. An estate in land held of a superior on condition of rendering him services.

Lien. A charge upon property for the payment or discharge of a debt or duty; the right to have a debt satisfied out of a particular thing.

1

THE BASIC REAL ESTATE CONTRACT

Generally

A real estate contract, as used in New Mexico, is a legally enforceable sales agreement controlling the transfer of legal and equitable title to real property from a seller to a buyer.

- **Legally Enforceable Agreement.** A real estate contract (REC) is a legally enforceable agreement by which a seller agrees to sell, and a buyer agrees to buy the property on a deferred payment arrangement. If the buyer performs all his obligations under the contract, he is entitled to receive a deed from escrow conveying the legal title to him. The seller and buyer jointly appoint a neutral third party as escrow agent to hold documents, collect and disburse payments, maintain a payment ledger and deliver the documents upon payoff or forfeiture as instructed. If the buyer defaults, the seller has the option to either (1) declare a forfeiture of the buyer's interest in the property without court action and recover a deed from escrow conveying the buyer's equitable interest to the seller, or (2) declare the entire unpaid balance of the purchase price to be due and payable, and file suit to collect.
- **Legal Title.** The real estate contract does not transfer legal title to real estate. Instead, it obligates the seller to transfer the legal title to the buyer upon the happening of some future event. The transfer of legal title is always done by a separate deed of conveyance, usually a warranty deed, which is placed in escrow when the REC is signed.
- **Equitable Title.** The REC does, however, transfer an interest to the buyer, known as the "equitable title". If the buyer defaults on the performance of his contract obligations and the seller elects to terminate the contract, it is essential that the seller recover this equitable property interest from the buyer, in order to have clear title to the property. For that reason, the buyer signs a special warranty deed which is placed in escrow together with the seller's warranty deed to the buyer.

Essential Elements

The REC is a very flexible instrument which can contain any pertinent provisions the contracting parties consider to be necessary or desirable. However, the basic REC contains certain essential elements, as a minimum. These are described in the following paragraphs.

Date of Contract

The parties can specify the date on which they want the contract to become effective. Such specification is necessary when the parties want the contract to become effective on some date other than the date of signing the contract. It also removes ambiguity when the buyer and seller sign the contract on different dates, or when the date of signature is not shown on the document. Unless specified otherwise in the body of the contract, the contract date is used to determine when interest starts to accrue on the unpaid principal balance, and

when taxes and insurance premium accruals will be pro-rated between the buyer and seller. It is also frequently used to determine when "balloon" payments will be due: e.g., "five years after date of this contract."

Names/Addresses of Parties; Legal Capacities

To avoid clouds on the title, it is essential that there be no doubt as to who is buying and selling, exactly what property interest is being sold, the capacity in which the buyer is contracting to buy the property, and in the case of multiple buyers, what quantity and quality of title each is to receive. The legal capacity of each party (e.g.: corporation, general or limited partnership, limited liability company, unmarried individual, husband and wife or spouse dealing with separate property) is declared. Multiple buyers and multiple sellers should declare whether their interests in the REC will be as joint tenants with rights of survivorship, co-tenants or community property. If co-tenants, they should also specify their respective percentage interests in the property or the proceeds. Addresses are essential to enable the parties to give required notices to each other and to enable the escrow agent to service the REC.

Agreement to Buy and Sell

Without a specific statement of agreement of the seller to sell, and of the buyer to buy the property, no contract can come into existence. Every REC must therefore contain the requisite language of agreement and recite the consideration, more or less as follows:

"1. **SALE:** The Seller, in consideration of the promises and agreements herein made by the Buyer, agrees to sell and convey to the Buyer the following described real estate, hereinafter called the Property, in the County of _____ and State of New Mexico:

_____.

2. **PRICE AND PAYMENT:** The Buyer agrees to buy the above-described Property and to pay Seller therefor the total sum of _____ Dollars (\$_____), payable as follows: _____ cash down payment, the receipt of which is hereby acknowledged, and the balance of _____ Dollars (\$_____), payable as follows:

_____."

Legal Description

The real estate being sold must be accurately described, either by surveyed "metes and bounds" or by reference to a subdivision plat filed in the records of the clerk of the county where the property is located, or by reference to some other instrument of record in the office of the clerk of the county where the property is located. When property is described by reference to another recorded instrument, the time and place of filing or recordation of the referenced instrument must also be shown, so that it can be located and identified.

Terms of Payment

These are, of course, infinitely variable. It must be clearly stated what is to be paid, when

and where. Excessively complex payment terms can detract from the subsequent marketability of the property. Excessive vagueness can invalidate the REC itself or result in litigation. Provisions that prohibit or penalize prepayment of the debt are not enforceable, if the property consists of one to four residential units. This issue is discussed in Chapter 7. Drafting suggestions for complex terms of payment will be found in Chapters 3 and 4.

Requirement that Buyer Pay Taxes/Insurance Premiums

The buyer is required to pay all property taxes becoming due after the effective date of the contract. If the property is improved (has a building on it), he is required to insure the property against risk of loss due to fire and other hazards in the minimum amount specified in the contract, which usually is the unpaid balance of the purchase price. He is required to provide a copy of the insurance policy or a certificate of insurance to the seller. Finally, he is required to notify the county assessor of the sale, so he will be shown on the assessor's records as the property owner, and so future tax notices will be sent to him. Taxes and insurance premiums for the current year are pro-rated to the date of closing (date of contract) and the buyer is credited at closing for the amount accrued at that time. The buyer will then be required to pay all taxes and insurance premiums due at their next respective due dates.

Exactly how the buyer will pay the taxes and insurance premiums depends on the requirements of the REC and any senior mortgage or REC assumed or wrapped by the new REC. Special language may be required to assure that the insurance policy covers the risks the parties want to protect against. If the buyer fails to pay the taxes, or fails to maintain insurance, the seller has alternative rights of enforcement which require that certain notice procedures be followed. If an insured loss occurs, there is a question as to how the insurance proceeds will be used. All these subjects are discussed in detail in chapter 6.

Payment of Other Liens

Standard language in the REC requires the buyer to pay any and all other liens, such as paving assessments and "other charges" against the real estate, by which is meant debts or claims which are secured by liens against the property.

Delivery of Deed/Title Insurance

Upon performance in full of the terms of the REC (e.g., payment of the deferred purchase price and interest, payment of taxes and insurance premiums), the agreement provides that the buyer will receive delivery from escrow of a warranty deed conveying legal title to him. Also, some standard forms provide that the seller at his own expense will at that time provide to the buyer either an up-dated abstract of title showing "good and merchantable title" or a policy of title insurance. In modern practice, this provision is customarily deleted and replaced by a statement that the seller has provided a contract purchaser's title insurance policy to the buyer at closing, and releasing the seller from any further duty to provide evidence of title.

Restrictions Against Buyer's Right To Resell Property

Form 103 contains a statement purporting to void any attempted assignment by the buyer of his contract rights without obtaining the seller's written consent. This provision has been the subject of much controversy, it being alleged that such a provision violates the buyer's rights under the New Mexico Constitution. More recent practice has been to replace this clause with a "due-on- sale" clause requiring the buyer to immediately pay the entire unpaid balance to the seller if the property is resold or if the REC is assigned without the seller's written consent. Actions by the United States Congress, the New Mexico Legislature and New Mexico appellate courts have limited the effectiveness of the due-on-sale clause. This subject is treated in depth in Chapter 7.

Seller's Rights upon Default by Buyer

Generally, the REC provides that, after a buyer is in default, the seller may send written notice to the buyer alleging the default and making demand that the default be cured within a time limit specified by the REC. If the buyer fails to cure the default within the specified time limit, the seller may then elect either of two alternative remedies:

1. the seller may terminate the REC, forfeit the buyer's rights to the property and start legal proceedings to evict the buyer from the property. All payments previously made are regarded as rent (form 103) or liquidated damages (RANM form 11) for the use of the property. Until an eviction order is obtained, the buyer is regarded as a tenant at will from month to month, and must pay rent monthly in advance in an amount equal to the monthly payments that were due under the terms of the REC.
2. the seller may elect to declare the unpaid balance of the purchase price to be due and payable in full, and may file suit to collect. If the seller obtains judgment and collects his money, the escrowed warranty deed is then delivered to the buyer. The seller may also file a transcript of his judgment in the county clerk's office of the county where any property of the buyer is located, thereby obtaining a judgment lien against all real property of the buyer located in that county, and sue to foreclose the lien.

Default and termination procedures are discussed in detail in Chapter 12.

Escrow Letter

In this section of the REC, the parties jointly appoint a neutral third party, usually a licensed independent escrow company, as escrow agent to service the REC.

- The escrow agent is given custody of the original deeds of conveyance, which have been signed by the parties and acknowledged, but not recorded. The agent is also given custody of the original or a copy of the recorded REC.
- The escrow letter instructs the agent to receive and disburse payments in accordance

with the terms of the REC. The agent maintains a record of payments, and allocates the payments to principal and interest.

- The letter instructs the agent to release the escrowed documents to the buyer upon performance in full of the REC requirements. Conversely, the agent is instructed to release the documents to the seller if the buyer defaults and remains in default for a specified period of time after the seller mails a written notice of default to the buyer. (Sounds easy, doesn't it?)
- The escrow letter also should contain provisions regarding the respective duties of the seller and buyer to pay the escrow agent's fees.
- Additional instructions may be given to the escrow agent, depending on the needs of the parties and the willingness of the agent to perform additional services.

Income Tax Implications

Installment Sales Treatment. If at least one payment will be due after the end of the year in which the sale occurs, the seller may be eligible for taxation on the installment method, by which taxable gain and interest income are recognized in the year in which the payments are received. For this reason, seller-financed sales instruments can be useful in retirement planning, if the seller anticipates moving to a lower income tax bracket after retirement.

Eligibility. The seller is not eligible for installment sales treatment if the seller held the property for sale to customers in the ordinary course of the seller's trade or business. Exceptions to this rule exist for farming, timeshares and unimproved residential lots. Also, installment sales treatment is not available for depreciable property sold to a related party, although it can be used for a portion of the purchase price that is allocated to nondepreciable land. **Consult your accountant or tax lawyer!**

Constructive Receipt. The IRS deems payments to be constructively received by the seller when the escrow agent receives them, unless the escrow agreement denies the seller access to the funds until a later date. Prepayments by the buyer can have disastrous effects on the seller's tax plans. Sellers can protect themselves against this problem by transferring ownership of the REC to a qualified retirement plan, where all income tax on the gain and interest income will be deferred until the funds are withdrawn at retirement. If the property is not residential property (defined as four or less units), the inclusion of a prepayment penalty clause in the contract can also offset the tax consequences. Prepayment penalties are discussed in Chapter 7. **Consult your accountant or tax lawyer!**

Complex Contracts

The "Basic REC" described in this chapter pertains to the relatively simple situation where the seller holds clear title to the property which he intends to sell. Reality is seldom so simple. In most cases, the seller holds title subject to one or more existing mortgages on the property. Or, he may not be the legal titleholder at all. For example, he may himself be a contract buyer from a prior seller, with the expectation that he will receive title at a

later date when the prior seller's REC balance is fully paid. If the prior contract seller holds title subject to an existing mortgage, he may anticipate receiving title from the prior seller subject to the existing mortgage. All these complications must be fully dealt with in the REC, thereby adding complexity to the basic REC described in this chapter. "Complex" contracts are discussed in chapters 3 and 4.

2 PROPERTY INTERESTS of BUYER and SELLER UNDER THE REAL ESTATE CONTRACT: THE DOCTRINE OF EQUITABLE CONVERSION

Status of Legal Title: Mortgages vs. Real Estate Contracts

When a mortgage is used as the seller financing vehicle, everyone understands the title interests of the buyer and seller. The seller deeds the property to the buyer, who then signs a promissory note to the seller, and secures that note by executing a mortgage on the property, naming the seller as mortgagee. The buyer becomes the “owner” of the property, meaning that the buyer holds legal *and* equitable title to the property, subject to a mortgage for the benefit of the seller. When the note is paid in full, the seller gives the buyer a release of mortgage, which discharges the lien of the mortgage, leaving the buyer with “clear title”.

When a real estate contract is used as the financing vehicle, the title interests of the parties are not so apparent. Because a deed is not given to the buyer until the contract debt is paid off, legal title remains in the seller until that time. Consequently, it is not unusual for the seller to be regarded as the “owner” of the property until the contract is paid in full. For example, some mortgage companies will not recognize the buyer’s interest in the property when the buyer applies to formally “assume” the mortgage. The reason usually given is that the buyer is not the “owner” of the property, or does not hold title to the property.

The mortgage companies may be forgiven for their misperception of the buyer’s status under a REC. Unlike the mortgage and deed of trust, the REC is not a statutory creature. The law establishing the property rights of the buyer and seller under the REC will not be found in the statutes. It will be found instead in the case decisions of the New Mexico Supreme Court (the “Supreme Court”) and the New Mexico Court of Appeals (the “Court of Appeals”). There is no reason to expect that executive officers of mortgage lenders based in other parts of the country would be familiar with New Mexico’s court decisions.

History

For more than 50 years, the Supreme Court has consistently held that the buyer’s interest under a REC is real property, and the seller’s interest is personal property. The buyer is regarded as the “owner” of the land, and the seller is regarded as the “owner” only of the right to receive payment for the property. The Supreme Court reached this conclusion by applying to the REC what was known under the English common law as the **doctrine of equitable conversion**. In the 1942 case of *Mesich v. Board of County Commissioners of McKinley County* (see *Mesich*, p. 1 CLA), the Supreme Court quoted the doctrine as stated

in 1 Pomeroy's Equity Jurisprudence, as follows:

"In law the effect of a contract whereby the owner agrees to sell and another agrees to purchase a designated tract of land, the vendor remains the owner of the legal title to the land; he holds the legal title, 1 Pomeroy's Equity Jurisprudence, sect 367. But, in equity the vendee is held to have acquired the property in the land and the vendor as having acquired the property in the price of it. The vendee is looked upon and treated as the owner of the land and the equitable estate thereof as having vested in him. He may convey it or encumber it, devise it by will and on his death it descends to his heirs and not to his administrators. The legal title is held by the vendor as a naked trust for the vendee and any conveyance by him to one not a bona fide purchaser for value is ineffective to pass title. The vendee must bear all accidental injuries or losses done to the soil or appurtenances, by the operations of nature or third parties, and is entitled to recover all damages for injury thereto. The vendor, before payment, holds the title as trustee for security only."

The doctrine has been invoked in a long line of cases in which the characterization of the respective interests of buyer and seller as real property and personal property determined the outcome. A review of those decisions follows.

- ***Condemnation of land for public use***

---- Under New Mexico statutes of 1929, section 64-313, counties were empowered to acquire rights of way deemed necessary by the state highway commission for highways constructed under supervision of the commission "...by donation by the owners of the lands through which such highways shall pass, * * * or through the exercise of the power of eminent domain in the manner provided by law for acquiring property for public uses* * *". In *Mesich* (p. 1, CLA), the Supreme Court held that, through the application of the doctrine of equitable conversion, the buyers under an REC were the "owners" of the land, and therefore entitled to compensation for the taking of the property for public use. The County had argued, to no avail, that the buyers were not entitled to compensation because they were not the owners of the fee simple title to the property at the time of the taking.

----In 1971, the Supreme Court refined this holding by ruling that money deposited with the trial court pursuant to a condemnation award cannot be applied to the unpaid REC balance, and thus cure an existing default by the buyer! Instead, the money "stands in place of the land and is security for performance of the contract and is subject to liens just as if it were the land* * *". See *Trickey*, p. 2, CLA. This decision strongly suggests that when a payment to the buyer under a condemnation award is not sufficient to pay off the contract balance in full, the payment should go into escrow, rather than directly to the buyer, until such time as the contract is paid in full. If the buyer is in default at the time of the award, or later defaults on the contract obligations, the seller would be entitled to recover the proceeds.

----In 1980, the Supreme Court held that a school district could condemn the REC buyer's interest in a parcel of land, even though the parcel is less than the entire tract being purchased under the REC. See *Hobbs*, p. 2, CLA.

Intestate succession

Under New Mexico laws, when a person dies intestate (without leaving a last will and testament), any real property owned at death passes to the decedent's heirs.

---In 1963, the Supreme Court held in the *Gregg* case (p. 3, CLA) that the seller's interest under a REC was personal property, rather than real property. The decedent, Irma Evans, had left a will in which she devised all her *real estate* to her children or, if they did not survive her, then to her niece, Marion Hogan. She bequeathed all her *personal property* to her husband and the children, but failed to name a contingent beneficiary. The husband and the children all predeceased her, so if Irma's interest under the REC was determined to be real estate, then Marion would get the ownership of the contracts. If Irma's interest was personal property, then the will failed to dispose of the contracts, and they would pass to Irma's heirs under the laws of intestate succession. These consisted of Marion and four other nieces and nephews of Irma. As a result of the Court's decision, Marion had to share with the other heirs.

- ***Judgment liens***

A New Mexico statute (sect. 39-1-6, N.M.S.A. 1978 Comp, formerly sect. 21-9-6 1953 Comp) provides that a creditor who obtains a money judgment against his debtor can, by filing a transcript of the judgment in the county clerk's office of the county where any of the debtor's *real estate* is located, obtain a *lien on the real estate*. Section 39-4-13 of the statutes provides that "*Any person holding a judgment lien on any real estate...*" can file a suit to foreclose the lien, and the property can be sold to satisfy the judgment.

---In 1973, the Supreme Court held that such judgment liens attach to both legal and equitable interests in real estate. Accordingly, a judgment lien attached to the buyer's interest in land being purchased under a REC. See *Mutual Building and Loan Association of Las Cruces*, p. 4, CLA.

---In 1979, the Supreme Court ruled that a judgment lien, because it attaches only to real estate, does not attach to the interest of a seller under a REC. The Court noted language in the *Mutual* case stating that both legal and equitable interests in real estate were subject to judgment liens, and expressly overruled that language to the extent that the earlier Court may have intended to include the REC seller's interest in the term "real estate". See *Marks*, p. 4, CLA.

---In 1985, in another case where a judgment lien attached to the real property interest of a REC buyer, a grantee of the buyer argued that the lien attaches only to the amount of the payments made and the value of improvements placed on the property. The Supreme Court rejected this argument, and held that the judgment lien attaches to the full value of the estate of the buyer in the property. Because the grantee had actual and constructive knowledge of the judgment lien, her interest in the property was subject to foreclosure of

the lien by the judgment creditor. See *Bank of Santa Fe*, p. 5, CLA.

- ***Tax liens***

In 1977, the Supreme Court held that a federal tax lien filed against a REC buyer attached to the buyer's interest in the land being purchased, and was co-extensive with the buyer's interest in the property. See *MGIC Mortgage Corporation*, p. 6, CLA. MGIC, as holder of the first mortgage, had conducted a foreclosure sale of the property. A cash surplus remained after payment of MGIC's claim. The surplus was claimed by a judgment creditor of the seller, and by the United States, which held a tax lien on the buyer's interest. The Court noted that the buyer was in default on his REC obligations at the time of the foreclosure sale. However, since the seller had not given notice of default to the buyer, the buyer's equitable interest was still in existence, and was subject to attachment by the tax lien. (The Court noted that had the seller given notice and elected to terminate the contract, the tax lien, like other liens against the buyer's interest, would not have survived the termination. This observation, while true at the time, was later negated by a 1986 amendment to Title 26, section 7425 of the United States Code. See Chapter 12.)

- ***Mortgages of buyer's interest.***

In 1981, the Supreme Court, in a case of first impression in New Mexico, followed a line of cases from the state of Washington and held that a REC buyer owns a mortgageable interest in the property. See *Shindldecker*, p. 6, CLA. (Later in this book, mortgages on the buyer's REC interest will be referred to as equitable mortgages.) The *Shindldecker* Court emphasized two important differences between legal mortgages, which are liens against the fee interest, and equitable mortgages, which are liens against an equitable interest:

1. the interest of the buyer's mortgagee (the equitable mortgage) is subject to the prior interest of the REC seller, and remains in force only so long as the REC remains in force. If the seller elects to terminate the buyer's interest after default, the interests of the buyer's mortgagee are terminated, because he has no right of redemption;
2. recording the equitable mortgage does not give constructive notice to the REC seller of the existence of the mortgage, so the seller is not required to notify the mortgagee of his intent to retake the property. "Instead, the mortgagee must use one of several available contractual devices to insure that he receives both notice of a breach by the vendee and the opportunity to protect his interests." *Id.*

- ***Mortgages of seller's interest.***

In 1974, the Supreme Court ruled that when a REC seller borrowed money from a bank and secured the loan by giving the bank a mortgage on the property, the bank did not acquire any interest in the unpaid balance of the REC. Consequently, when the seller later assigned his interest in the REC to another party, the assignee, rather than the bank, was entitled to the contract payments. See *First National Bank of Belen*, p. 7, CLA. The Court reached three important conclusions, all resulting from the application of the doctrine of equitable conversion:

1. The seller's interest in receiving the unpaid balance of the contract was *personal property*. The seller never assigned his interest in the unpaid balance to the bank, and a mortgage of the land to the bank therefore did not attach to this interest.
2. The bank failed to comply with the Uniform Commercial Code provisions on secured transactions, and therefore held no security interest in the contract proceeds.
3. At the time the seller executed the mortgage, the only interest he held in the real estate was a possibility of reverter to him if the buyer defaulted in payment of the REC. The mortgage attached to this interest, but to nothing else. Since there was no default, there was nothing for the bank to foreclose against.

---In 1995, the Supreme Court held that while a mortgage is not an assignment, and a mortgage given by the REC seller to a lender does not create a lien against the contract proceeds, the mortgage nevertheless *as to the seller* serves as a written security agreement, and is perfected *as to the seller* upon recording in the county clerk's office. See *In Re Finch*, p. 8, CLA. The Court suggested that the recorded mortgage would not serve as a perfected security interest against the claim of a third party. The Court was reluctant to allow the seller to take advantage of the lender's unfortunate choice of security instruments, because the seller intended to give his entire interest in the REC as security for the debt. This decision does not appear to weaken the holding in the *First National Bank* case, because the claim of a third party was involved in that case.

- ***Purchase-money mortgages***

A purchase-money mortgage is defined as a mortgage executed at the same time as the deed of the purchase of land, or in pursuance of agreement as part of one continuous transaction, in favor of the seller, or a third-party lender of the purchase price paid to the seller, provided the money was loaned for that purpose. Purchase-money mortgages are generally held to have priority over prior judgment liens against a purchaser's interest in the real estate. The reason usually given is that "there is no moment at which the judgment lien can attach to the property before the mortgage of one who advances purchase money". See *C & L Lumber and Supply, Inc.*, p. 8, CLA.

---In 1990, the Supreme Court held that the refinancing of a REC did not create a purchase-money mortgage, where the seller had purchased the property under a purchase-money mortgage. *Id.* The lender had argued that the loan was for the purpose of acquiring title, since the REC buyer would not acquire legal title until the REC was paid off. The Court rejected this argument, pointing out that the REC buyer “is treated as the owner and his interest in the property is subject to a judgment lien * * * Thus, various liens in fact may attach themselves to property under a land sales contract prior to the execution of a refinancing loan and mortgage”. The Court concluded that the refinancing loan was for the purpose of discharging the REC debt, not for the acquisition of title.

- ***Interpretation of the term “owner”***

In 1981, citing the *Mesich* and *Marks* cases, the Supreme Court held that the term “owner of land” in New Mexico extends to a REC buyer. See *Withers*, p. 9, CLA. The County had published an invitation to the public to bid on property that was adjacent to property being purchased on a REC by Douglass. The invitation provided that if the successful bid was made “by a bidder other than the owner or owners of land adjacent to and adjoining such parcel and such owner or owners have also submitted a bid on the parcel, the [Board] reserve the rights to allow such adjacent and adjoining landowner or owners to meet the successful bid * * *”. *Withers*, who did not own adjacent land, was the successful bidder. The Court held that the County acted properly in allowing Douglass to meet the bid.

---Variations from the equitable conversion rule may occur when a particular statute defines the term “owner”. For example, in 1993 the Supreme Court held that a REC seller was an “owner” of the real estate for purposes of the New Mexico Property Tax Code. See *Southwest Land Investment, Inc.*, p. 10, CLA. The Court noted that section 7-35-2(F) of the Code defines “owner” as “the person in whom is vested *any title* to property.” Because the REC seller holds both legal title and a reversionary interest in the property, he comes within the statutory definition.

Miscellaneous

---In 1982, the Supreme Court held that real property was “sold, exchanged or conveyed” within the meaning of a listing agreement when the purchase agreement was signed, rather than when the property was actually deeded at a later date. See *Hertzmark-Parnegg Realty, Inc.*, p. 11, CLA.

---In 1989, the Court of Appeals held that the activity of arranging investments in REC’s – that is, the buying and selling of the seller’s interest in the REC – does not require a real estate broker’s or salesperson’s license. *Garcia v. New Mexico Real Estate Commission*, 108 N.M. 591 (App.), 775 P.2d 1308 (1989). The Court considered itself bound by a previous decision of the Supreme Court holding that the sale of a seller’s interest in a REC was the sale of personalty, and therefore was not included in the definition of “real estate” in the licensing statute, section 61-29-2(A), (B) NMSA 1978.

3. **COMPLEX CONTRACTS: The ASSUMPTION AGREEMENT**

Property may be sold by REC when an existing mortgage or REC already encumbers the property. The existing obligation can be either assumed by the buyer, or “wrapped” by the new REC (wrap-around contracts are the subject of the next chapter). When the existing obligation is assumed, it is treated like an “add-on” provision to the basic REC. The buyer agrees to pay the existing obligation in accordance with its terms, in addition to making payments on the debt owed to the seller.

Features

There are certain features that are inherent in the typical assumption agreement. Some of the features are variable, and subject to negotiation.

- Seller not Released. The contractual relationship between the seller and the holder of the assumed obligation is not normally disturbed. The seller remains liable to the holder of the assumed mortgage or REC for the performance of its obligations. In some situations, the holder is asked to release the seller from his obligations, and to accept the buyer as a substituted party on the assumed obligation. Such transactions are known as “novations”. They most often occur when the REC buyer applies to the holder of a FHA-insured mortgage to qualify as an assuming party. When a REC buyer assumes an existing REC, however, the existing contractual relationship is left undisturbed.
- Buyer is Liable to Seller. The buyer contracts with the seller to perform all the obligations of the assumed mortgage or REC in accordance with its terms. This agreement has certain consequences:
 - If the existing obligation requires that taxes and hazard insurance premiums be paid through the servicing agent (a “PITI” obligation), then the buyer must comply with any changes to the monthly payment mandated by the servicing agent.
 - The buyer must pay any required late charges resulting from delinquent payments.
 - Any default in performance of the existing obligation is deemed to be a default in the performance of the REC. This is true even after the debt to the seller has been paid in full, and the warranty deed delivered from escrow to the buyer. If the buyer subsequently defaults on an assumed mortgage, and the mortgagee obtains a deficiency judgment against the seller, the seller has a continuing right to sue the buyer under the terms of the REC for reimbursement. See *Kuzemchak*, p. 12,

CLA.

- If the existing obligation is an adjustable rate mortgage ('ARM'), then the buyer receives the burden or the benefit of any changes to the interest rate and required monthly payment amount.
- The buyer, rather than the seller, may claim interest paid on the existing obligation as a tax deduction, if he is otherwise qualified to claim the deduction. However, if the servicer of the existing obligation does not recognize the assuming buyer's position, then that servicer may report interest paid on IRS form 1098-INT in the seller's name, thereby triggering an IRS inquiry into the buyer's claim of an interest deduction on his tax return.
- Buyer Not Liable to Holder of Assumed Obligation. The buyer does not normally enter into a contractual relationship with the holder of the assumed obligation. Nevertheless, where the assumed obligation is a REC, the buyer will be entitled to receive notice of default before the holder can terminate the assumed REC for nonperformance. See chapter 12, 'Who is entitled to Notice?'. The buyer may, however, elect to become personally obligated to the holder of the assumed obligation when a HUD-insured mortgage is being assumed. See 'HUD-Insured Mortgages', this chapter.

Checklist

When contemplating an assumption by REC of an existing obligation, you may find the following check-list to be helpful.

1. Get a full copy of the existing **recorded** REC (including any amendments), note and mortgage, or note and deed of trust. Make extra copies for the title closing officer and the attorney who will prepare the documents.
2. Get a current print-out from the servicing agent showing all available information regarding the obligation, including unpaid principal balance, interest paid-through date, next payment due date, amount of required monthly payment for principal and interest, amount of required monthly payment for taxes and insurance (if applicable), balance of escrowed taxes and insurance premiums (if applicable), and any balance of unapplied funds.
3. Determine the purchase price, down payment and terms of payment on the equity balance owed to the seller, and any other terms or conditions of the sale.
4. Coordinate the payment due dates. When the new REC and the assumed obligation have different servicing agents, the new REC should require that payments on the assumed obligation and on the balance due to the seller will be paid in a single monthly remittance to the escrow agent, *no later than the 10th day prior to the due date stated in*

the assumed obligation. This will allow time for the escrow agent to process payments and mail the assumed obligation payment to the servicing agent so it will not be delinquent. Failure to allow adequate time for servicing requirements is one of the most common mistakes made in the preparation of REC's. Consider the possible consequences when the new REC and the assumed obligation have the same due dates:

- Licensed escrow companies are allowed up to 5 business days after collected funds are on hand, to disburse payments. *New Mexico Escrow Company Act, 58-22-26A.(6) NMSA 1978.* A competitive escrow company will disburse payments within 2 business days after a payment is received. Nevertheless, the law allows a much longer processing time.
- When the assumed obligation is a REC, the holder of that REC has the right to mail a formal notice of default as early as the payment due date, so that the notice will take effect on the very first day of delinquency. See *Petrakis*, p. 53, CLA. If the notice is mailed by the seller's attorney, a liability is incurred for the attorney's fee upon mailing of the notice.
- Most modern REC's contain provisions requiring a late charge to be paid when a payment is received by the escrow agent more than a specified number of days after the due date.
- Therefore, the junior buyer may incur liability for late charges and/or an attorney fee on the assumed REC, even though his payment to the junior escrow agent was timely and in compliance with the requirements of the junior REC!
- Most mortgagees do not assess a late charge until a payment is more than 15 days late, but a 10-day late charge is not uncommon. If the payment is considered delinquent, the mortgagee may report the mortgagor reflected on its records as a 'slow pay' to various credit reporting bureaus, with resulting damage to credit ratings.
- If the buyer becomes chronically delinquent, the seller may have a serious enforcement problem. A default notice cannot take effect until a payment is at least one day late, and the REC normally allows the buyer 30 days to comply. By that time, the next payment on the assumed mortgage is already past due, and most mortgage companies will not accept one monthly payment when two or more are due! I have seen mortgages go into foreclosure, even though the buyer is never more than one month delinquent on his REC payments. Under these circumstances, the seller may be forced to advance a monthly payment to the mortgagee, and pay one or more late charges, in order to prevent a foreclosure suit from being filed.

5. Determine how taxes and insurance premiums will be handled.

- (a) If taxes and hazard insurance premiums are a required part of the existing obligation payments, then the seller should be given credit on the settlement statement for any existing balance in the servicing agent's escrow fund, and ownership of the fund should be assigned to the REC buyer. The buyer's required monthly payment on the existing obligation will include Principal, Interest, Taxes and Insurance (if applicable) – i.e., 'PITI'. See 'Examples of Assumption Clauses', this chapter.
- (b) If taxes and insurance premiums are *not* being paid through the existing obligation, then the seller should be charged for taxes and premiums accrued through the date of closing. The REC will then require that the buyer pay all taxes and insurance premiums as they become due. Also, a decision must be made whether the buyer will pay taxes and maintain hazard insurance outside escrow, or through the REC escrow agent. This decision should be reflected in the purchase agreement REC addendum (see number 9, below).
6. Will the senior obligation be paid *through escrow* or *outside escrow*? This decision must be indicated on the purchase agreement REC addendum, for inclusion in the final REC. It is far better to always require that assumed mortgage/REC payments be made *through escrow*, for several reasons.
- The additional cost is minimal. Most escrow companies charge \$2.00 for each additional disbursement after the first disbursement to the seller.
 - The seller will always know the status of the assumed mortgage payments, and can act promptly if necessary to protect his interests. Because the buyer is required to make both the mortgage payment and the seller's payment at the same time to the escrow agent each month, the seller knows that receipt of his monthly payment means that a payment was also disbursed to the mortgagee. If the buyer is allowed to make the mortgage payments "outside escrow", the seller will not know the status of the mortgage loan, unless he personally checks with the mortgagee from time to time. The escrow agent has no obligation to monitor the mortgage payments when they are made outside escrow.
 - The detailed payment records of the escrow agent can assist the buyer in documenting errors made by mortgage-servicing companies. Misapplication of payments is a common occurrence in the mortgage-servicing industry. For example:
 - Some payments are posted several days after receipt, resulting in automated accrual of unwarranted late charges on the customer's account;
 - Some payments are applied to the wrong account, and the customer is reported to credit reporting agencies as delinquent;
 - Principal prepayments, although designated on the check or payment coupon as such, are often applied as advance monthly payments, with the result that the payor does not get the desired reduction in future interest costs;

- When servicing rights to large blocks of mortgages are sold from one servicing company to another, the “new” company often claims to be unable to access or correct errors made by its predecessor.

The problems are so pervasive that at least one escrow company, Security Escrow Corporation, sends mortgage payments to some mortgagees by certified mail, return receipt requested, at no cost to its customers. This allows the escrow agent to establish the date of receipt of payments by the mortgagee, so that misapplied payments and improperly assessed late charges will be corrected at no cost to the payor.

7. Check for balloon-payment requirements. The senior REC may require extra payments on principal in addition to regular monthly payments, or it may contain a balloon payoff requirement. The buyer, by the terms of his contract agrees to assume all obligations of the senior REC and therefore must make these extra payments. For the protection of the seller, the title company, both real estate agents and the contract preparer (does ‘*settlement pool*’ sound familiar?), it is a good idea to include a provision like this in the REC:

Purchaser acknowledges receipt at closing of a complete copy of said real estate contract, and is aware of the balloon payments required by said contract (or ... is aware of the early payoff required by said contract).

The clause is best inserted in the ‘Prior Obligations’ paragraph on the second page of the RANM form REC. See ‘Examples of Assumption Clauses’, this chapter. Of course, the closing officer should actually give a copy of the senior REC to the buyer at closing and obtain a receipt.

8. Check for due-on-sale clauses. If a due-on-sale clause is contained in an assumed REC, get the seller’s written consent to the sale (See ‘Assuming the Non-assumable’, below). If an assumed mortgage is HUD-insured, complete a HUD-approved assumption package. See ‘HUD-Insured Mortgages’, this chapter.). If a due-on-sale clause exists in a truly ‘non-assumable’ mortgage, add language to the REC setting forth the responsibilities of the seller and buyer if the mortgage holder accelerates the loan. See ‘Examples of Assumption Clauses’, this chapter.
9. Complete the real estate contract addendum to the purchase agreement. RANM form no. 21 should be used for this purpose. If Security Escrow Corporation is named as the escrow agent, you can use either the RANM form or the real estate contract addendum form provided by Security Escrow, which includes an extra page of service options. Be sure to include a statement on the addendum to the effect that the buyer acknowledges receipt of a copy of the assumed obligation document, and specifically stating awareness of any unusual special requirements, such as balloon payments, adjustable interest rates/payments, tax and insurance escrow requirements, prepayment penalties, restrictive covenants, and due-on-sale clauses. It would be a good idea to expressly require that this statement be incorporated into the REC. All parties that will be signing the REC should sign the addendum.

10. Deliver two copies of the purchase agreement, real estate contract addendum, the existing note & mortgage (or existing REC) and the current status printout to the title-closing officer.

Assuming the Non-assumable

Special problems arise when a buyer attempts to assume a mortgage or REC that contains a due-on-sale clause or prepayment penalty/prohibition, or purports to invalidate any transfer of the property. An analysis of the history and validity of these clauses is found in chapter 7. In this chapter, suggestions are offered for approaching each type of obstacle, based on the type of instrument involved.

- **Form 103 contracts.** Not to worry. This one is easy. Paragraph 11 of the standard form states that ‘no assignment of this contract shall be valid unless the same be endorsed hereon and countersigned by the Owner’. In the 1985 *Paperchase* decision, the Supreme Court held that a sale by means of an assumption agreement does not constitute an assignment, and therefore does not violate the contract provision. See p.17, CLA. In the 1988 *Gartley* decision, the Court held that restraints on alienation would not be upheld unless they are limited both in duration and as to the number of persons to whom transfer is prohibited. See p. 18, CLA. (See chapter 6 for a complete discussion of these cases.) It would appear that paragraph 11 poses no threat to an assumption sale, or even to a sale by assignment.
- **RANM 11 REC (1981 version, form 2, Forms App.).** Paragraph 7(B), if checked and initialed by the parties, declares that the buyer may not sell the property without first obtaining the written consent of the seller, and provides that the ‘seller shall not be under any obligation of any kind to give such consent’. Violation of this paragraph is declared to be an event of default, for which the seller can pursue the remedies set forth in paragraph 5 of the contract. That paragraph authorizes the seller to either terminate the contract or accelerate the unpaid balance, at his election. An election to terminate would effectively convert paragraph 7(B) into a forfeiture type of restraint on alienation. This result is unlikely to be upheld, because of the *Gartley* decision. However, an election to accelerate the unpaid balance is a definite threat, and would most likely be upheld. For that reason, the buyer should obtain the seller’s written consent before entering into a binding agreement to sell the property.
- **RANM 11 REC (1998 version, form 3, Forms App.).** Paragraph 6(B) of the new form provides that a ‘transfer without payment of the Balance Due Seller will require obtaining the prior written consent of Seller, *which Seller will not unreasonably withhold*’ (emphasis added). The change in language from the 1981 version is very significant. For a full discussion, see chapter 6. Buyer should request seller’s written

consent to the proposed sale. If the seller refuses to give his consent, then the buyer must make a decision as to whether or not his proposed sale would diminish the value of the seller's security interest in the property, before proceeding with the sale. **Consult your real estate lawyer!**

- **HUD (U.S. Department of Housing and Urban Development)-Insured Mortgages.**

These mortgages contain due-on-sale clauses, which purport to allow acceleration of the mortgage note if the property is sold or encumbered without the lender's prior consent. However, in reality the enforceability of these clauses depends on the date of origin of the mortgage loan. Even those mortgages that are 'non-assumable' can in fact be assumed by a REC buyer, provided certain HUD requirements are met.

1. Mortgage loans originated before December 1, 1986. These mortgages generally contain no restrictions on assumptions, and are freely assumable without any requirement for approval from the lender.
2. Mortgages originated on or after December 1, 1986 and before December 15, 1989. These mortgages may contain assumption restrictions. However, those restrictions expired 24 months after the origination date of those mortgages; therefore the restrictions are no longer applicable, and these mortgages are freely assumable.
3. Mortgages originated on or after December 15, 1989. These mortgages can be assumed on the condition that the prospective buyer formally enters into an agreement with the lender to pay the mortgage debt and is determined by HUD (or the lender, if certified by HUD to be a Department-Endorsed "DE" lender) to be creditworthy. The HUD rule provides two methods by which the prospective buyer can be determined to be creditworthy:
 - (a) **Creditworthiness determination at time of sale.** The prospective buyer submits a request to HUD or to the DE lender for a determination of creditworthiness. This procedure entails a full credit review, and requires submission of tax returns, financial statements, employment status, and other materials. If the prospective buyer is found to be creditworthy, enters into an agreement with the lender to pay the mortgage debt and pays the lender's transfer fee (HUD allows the lender to charge up to \$500 when a full credit review is involved), the original mortgagor is released from personal liability for the mortgage debt. See HUD Rule, 24 C.F.R. sect. 203.510(a), p. 12, CLA.
 - (b) **Simple assumption followed by five years of payments.** The prospective buyer may enter into an agreement with the lender to pay the mortgage debt and pay a transfer fee (HUD allows the lender to charge up to \$125 for a 'simple assumption' of this type). The buyer must thereafter maintain a satisfactory payment record on the debt for a period of five years. He will

then be deemed to be creditworthy, provided the mortgage is not in default. At that time, the original mortgagor is automatically released from personal liability for the mortgage debt. During the five-year period when the buyer is making payments, the original mortgagor and the buyer are jointly and severally liable for payment of the mortgage debt. See HUD Rule, 24 C.F.R. sect. 203.510(b), p. 13, CLA.

When the rule cited above was first published in 1991 in the Federal Register as a proposed rule, HUD's discussion of section 203.510(b) appeared in the Federal Register (Vol. 56, No. 225, p. 58765), as follows:

'This paragraph (b) would adopt the interpretation which HUD has previously given to this statutory provision in Mortgagee Letter 88-2, the "Notice to Homeowner" attached to Mortgagee Letter 88-2, and the revised "Notice to Homeowner" attached to Mortgagee Letters 89-27 and 90-9. HUD interprets the statute as intended to assure that at least one creditworthy mortgagor is personally obligated on the mortgage at all times. When a home is sold, this objective can be achieved in one of two ways. First, a purchaser may be deemed to be creditworthy at the time of sale and personally assume liability. If this occurs, the objective described above is achieved even if the selling mortgagor is released at the time of sale. **Second, the purchaser may assume personal liability and then demonstrate creditworthiness by making payments on the mortgage for a significant period of time. Section 203[®] [of the National Housing Act] establishes five years from the date of assumption as the appropriate measure of time under the second alternative; if the mortgage is not in default at that time the assumptor can be considered creditworthy and the seller can be released** (emphasis added). Default status before or after the five years is not relevant for this provision of section 203[®].

'Consistent with this interpretation, HUD considers the five-year release provision to apply both when no request for release or a creditworthiness determination is made at the time of sale, and when a request is made but is denied for lack of creditworthiness. The provision should be strictly limited to true assumption cases and not applied to sales subject to the mortgage without assumption of personal liability by the purchaser, in order to avoid conversion of the mortgage into a nonrecourse mortgage when the selling mortgagor is released after five years. This reading is supported by the statutory statement that "the homeowner and the purchaser shall have joint and several liability" for five years, since the statement could be true only for purchasers who are true assumptors.'

Unfortunately, the 5-year payment method for establishing creditworthiness is not explicitly discussed in the HUD handbooks. However, the existence of the procedure is tacitly recognized in HUD Handbook no. 4155.1 REV-4, Chapter 4 (Assumptions):

"4-2 Restrictions of the HUD Reform Act of 1989. ...Assumptions without credit approval are grounds for acceleration of the mortgage, if permitted by state law and subject to HUD approval, unless the seller retains an ownership interest in the property or the transfer is

by devise or descent.” (emphasis added)

“4-3 **Release from Liability.** ...The due-on-sale clause is generally triggered whenever any owner is deleted from title,...” (emphasis added)

Assumption by REC buyer. When a mortgagor sells the property by REC to a new buyer, the seller obviously “retains an ownership interest in the property” and is not “deleted from title”! The seller retains legal title, as well as a right of reversion of equitable title and possession upon default by the buyer. It seems very clear that a sale to an assuming buyer by means of a REC falls within the handbook’s description of a transaction that does not trigger the due-on-sale clause.

Assumption by junior mortgagor. The obscure references in the handbook seem to imply that the due-on-sale clause would be triggered when a mortgagor sells the property to a junior buyer by deeding the property to the buyer and taking a note and mortgage as security for the purchase price. To that extent, the handbook may be in error, because the rule (see p. 13, CLA) explicitly refers to the assuming buyer as the “purchasing mortgagor”. The only underlying requirement for a simple assumption of this type is that both the purchaser and the selling mortgagor remain liable on the note and mortgage during the five-year period. The rule makes no mention of the type of instrument used to consummate the sale to the assuming buyer, nor does it state any requirement as to the status of legal title during the five-year period.

It should be remembered that the HUD handbook is not law. It is only an administrative manual written by HUD for the use of lenders and HUD’s own internal staff. The actual rule as adopted by the agency and published in the Federal Register constitutes the law on the subject. Therefore, any statements in the handbook that conflict with the published rule must yield to the rule.

It may be necessary to overcome some lender resistance to this method of assumption. The official HUD interpretation of the proposed rule quoted above should certainly help. Also, it may be appropriate for the seller and buyer to jointly sign a letter to the lender that includes a statement something like this:

‘The undersigned buyer intends to assume the subject mortgage and to establish creditworthiness by making payments on the mortgage debt for five years, as authorized by HUD rule 24 CFR Part 203, section 203.510(b). A copy of the real estate contract by which the property is being transferred to the buyer is enclosed

herewith. The buyer will execute the appropriate form of agreement to become personally liable for the unpaid balance of the mortgage note, and will pay the assumption fee of \$125.00 as authorized by HUD. Buyer states that he intends forthwith to occupy the subject property as his primary residence.

'We request that you henceforth accept all mortgage payments from the buyer, and that you correspond with the buyer at his notification address at:_____. The buyer's tax identification number (social security number) is:_____.

'The parties are not requesting release of the undersigned mortgagor/seller from personal liability at this time. We do request that the mortgagor/seller be released from personal liability upon the completion by buyer of payments on the assumed mortgage note for a period of five years, with the understanding that the mortgage must not be in default at that time.'

Drafting suggestion. Some lenders will allow a REC buyer to assume the mortgage at the end of the five-year period; others will not, on the ground that the buyer does not hold legal title, and therefore does not have standing under the National Housing Act to assume the mortgage. If the lender cannot be persuaded to recognize the REC buyer, there are two ways to overcome this objection:

- Include a requirement in the REC for a 'balloon' payment at the end of the five-year period, so that the buyer will receive the warranty deed from escrow and thereby obtain legal title; or
- Replace the REC with a note and mortgage/deed of trust at the end of the five-year period. The REC could provide for delivery and recordation of the warranty deed from escrow, with concurrent recordation of the mortgage or deed of trust.

Examples of Assumption Clauses Using the RANM Standard Form

The RANM standard form 11 was designed to accommodate assumption agreements. It is necessary to state the separate payment obligations on the first page of the form. Optional paragraphs on the second page include standard clauses that allow the parties to specify whether the assumed mortgage payments will be made direct to the mortgagee by the buyer, or through the escrow agent. Shown below are some sample clauses that could be used in conjunction with the RANM form 11.

Payment terms (Assumed mortgage, payments include PITI, paid through escrow agent)

2. **Price and Payment:** The Purchaser agrees to buy the above-described Property and to pay Seller therefor

the total sum of **EIGHTY THOUSAND AND NO/100 DOLLARS (\$80,000.00)**, payable as follows: **FIVE THOUSAND AND NO/100 DOLLARS (\$5,000.00)**, cash down payment, the receipt of which is hereby acknowledged, and the balance of **SEVENTY FIVE THOUSAND AND NO/100 DOLLARS (\$75,000.00)**, payable as follows:

\$60,300.00, by payment of that certain mortgage described herein in monthly installments of **\$800.00** (which amount includes **\$614.30** principal and interest, and **\$185.70** for taxes and insurance premiums) each, or more at Purchaser's option, including interest from February 1, 1998 on the unpaid principal balance at the rate of **10.00%** per annum, commencing March 1, 1998 and on or before the 1st day of each successive month thereafter until paid in full. Purchaser will pay any increased or decreased amounts for taxes and insurance premiums as may be required by ABC Mortgage Company or its successors in interest. [Purchaser will remit payments to the escrow agent named herein in advance, on or before the 20th day of each month, in a single remittance with the seller's payments required by the following paragraph;] (Delete last sentence if buyer will be paying mortgagee outside escrow)

\$14,700.00 in monthly installments of **\$194.26** or more, at Purchaser's option, including interest from date on the unpaid principal balance at the rate of **10.00%** per annum, commencing February 20, 1998 and on or before the 20th day of each successive month thereafter until paid in full.

Payment terms (Assumed mortgage with P & I payments only, T & I paid through escrow agent)

2. Price and Payment: The Purchaser agrees to buy the above-described Property and to pay Seller therefor the total sum of **EIGHTY THOUSAND AND NO/100 DOLLARS (\$80,000.00)**, payable as follows: **FIVE THOUSAND AND NO/100 DOLLARS (\$5,000.00)**, cash down payment, the receipt of which is hereby acknowledged, and the balance of **SEVENTY FIVE THOUSAND AND NO/100 DOLLARS (\$75,000.00)**, payable as follows:

\$60,300.00, by payment of that certain mortgage described herein in monthly installments of **\$614.30** each, or more at Purchaser's option, including interest from February 1, 1998 on the unpaid principal balance at the rate of **10.00%** per annum, commencing March 1, 1998 and on or before the 1st day of each successive month thereafter until paid in full. [Purchaser will remit payments to the escrow agent named herein in advance, on or before the 20th day of each month, in a single remittance with the seller's payments required by the following paragraph;] (Delete last sentence if buyer will be paying mortgagee outside escrow)

\$14,700.00 in monthly installments of **\$194.26** or more, at Purchaser's option, including interest from date on the unpaid principal balance at the rate of **10.00%** per annum, commencing February 20, 1998 and on or before the 20th day of each successive month thereafter until paid in full.

In addition to the above monthly installments, the Purchaser will remit a monthly amount for the payment of annual property taxes and hazard insurance premiums, presently in the amount of **\$185.70** (which amount includes **\$75.00** for taxes and **\$110.70** for premiums). This sum may be adjusted for increases and/or decreases in taxes and/or insurance premiums as determined by the escrow agent. The escrow agent shall use said funds as required to pay taxes and hazard insurance premiums as they become due.

Senior obligation assumed, paid through escrow agent (page 2 of the RANM form)

The following lien(s) or obligation(s) is currently outstanding on the property:

Type of lien or Obligation Holder	Loan Number	Recording Data: Book & Page
Mortgage to ABC Mortgage Company	F97-456782	04-07-97 Bk. 97-4 Pg. 7052-7055 Document no. 97034829

Purchaser assumes and agrees to pay the above-mentioned prior obligation in accordance with its terms. Purchaser shall make the installment payments on the prior obligation, together with installment payments on this Contract, to the Escrow Agent named below, who will remit the payments to ABC Mortgage Company or its successor in interest. Purchaser shall advise the Escrow Agent of any change in the amount of the payment due on the assumed obligation. Failure to make such payments to the escrow agent at the times required shall be a default under this Contract, for which the Seller may invoke the provisions of paragraph 5. At such time as the unpaid balance of the purchase price due the Seller is fully paid, this Escrow shall terminate and the purchaser shall thereafter make the installment payments on said prior obligation directly to ABC Mortgage Company or its successor in interest.

If Purchaser fails to pay any such installment payments prior to the same becoming delinquent, Seller may pay the same for the protection of the Property and his interest therein. Payment by Seller shall not be deemed a waiver of Purchaser's default, and the amount so paid by Seller shall be immediately due and payable to Seller and shall bear interest until paid at the same rate as provided in Paragraph 2 above.

Senior obligation assumed, paid outside escrow (page 2 of the RANM form)

The following lien(s) or obligation(s) is currently outstanding on the property:

Type of lien or Obligation Holder	Loan Number	Recording Data: Book & Page
Mortgage to ABC Mortgage Company	F97-456782	04-07-97 Bk. 97-4 Pg. 7052-7055 Document no. 97034829

Purchaser assumes and agrees to pay the above-mentioned prior obligation in accordance with its terms. Purchaser shall make the installment payments on the prior obligation to ABC Mortgage Company or its successor in interest. Failure to make such payments at the times required shall be a default under this Contract, for which the Seller may invoke the provisions of paragraph 5. If Purchaser fails to pay any such installment payments prior to the same becoming delinquent, Seller may pay the same for the protection of the Property and his interest therein. Payment by Seller shall not be deemed a waiver of Purchaser's default, and the amount so paid by Seller shall be immediately due and payable to Seller and shall bear interest until paid at the same rate as provided in Paragraph 2 above.

Senior obligation assumed, special provision for non-assumable mortgage (page 2 of RANM form)

It is understood that the mortgage herein assumed contains a due-on-sale clause, meaning that the mortgagee may, as a result of this sale, elect to declare the unpaid balance of said mortgage to be immediately due and payable. If mortgagee gives notice to Seller of its intention to accelerate the loan balance, then Seller shall immediately give written notice to Buyer of said election. Buyer shall, within 20 days after Seller mails or delivers said notice to Buyer, either qualify with the mortgagee to assume the mortgage, or pay off the mortgage loan balance in full. If Buyer fails to either so qualify or pay off the mortgage loan balance within 20 days, then Seller may elect to either (a) declare a forfeiture of the Buyer's interest in the property and in this contract, obtain the special warranty deed from escrow, and take possession of the Property, or (b) pay off the mortgage loan balance, whereupon the amount of principal and interest paid by Seller to the mortgagee shall become so much additional indebtedness owed by Buyer to Seller, and shall bear interest at the rate provided in paragraph 2 herein, payable in monthly installments equal to the monthly installment payments which were required by the mortgage note.

4

COMPLEX CONTRACTS: THE WRAP-AROUND AGREEMENT

What is it?

In a wrap-around real estate contract, the contract is junior and subject to a senior mortgage or REC, but the buyer is not allowed to assume the senior obligation. Rather, the unpaid balance of the senior obligation is included in the unpaid balance of the seller's equity. The seller agrees to make all required payments, and perform all other requirements of the senior obligation, and to obtain a release of the lien of the senior obligation when the junior REC is paid in full.

Why is it Used?

The wrap-around contract or its equivalent, the 'all-inclusive' deed of trust, is used primarily for one of three purposes:

1. Interest-rate spreads. The seller benefits when the interest rate on the junior REC is greater than the rate on the wrapped obligation. By including the unpaid balance of the wrapped obligation in the amount owed on his equity balance, the seller can earn a 'spread' represented by the difference between the REC interest rate and the rate on the wrapped obligation's balance.
2. Due-on-sale avoidance. The wrap-around contract is also used to avoid the necessity for the buyer to assume an existing HUD-insured obligation. The parties hope that the mortgagee will not discover that a sale has occurred, and exercise its rights under the due-on-sale clause contained in the mortgage. This use (or abuse) of the wrap-around contract, while not a criminal violation, does violate the due-on-sale provisions of the mortgage, and presents serious planning and drafting problems for the parties.
3. Subdivisions. The seller typically buys a tract of land using some form of seller financing, then subdivides the tract into smaller lots, and sells the lots on individual REC's.

Checklist

When contemplating use of the wrap-around technique, start with the checklist in chapter 3. Then add these items:

1. Provide for payments on the senior obligation to be made by the escrow agent! This is essential for the protection of the buyer. This requirement should be stated in the purchase agreement REC addendum, so that it will be incorporated into the permanent REC. Failure to require that

the escrow agent disburse a portion of the seller's proceeds each month to the servicer of the wrapped obligation is the *single most common problem arising under wrap-around contracts*.

2. Coordinate the payment amounts. The required monthly principal and interest payment on the junior REC, less the seller's share of escrow fees, must be at least as large as the required monthly payments of principal, interest and buyer's escrow fees on the wrapped obligation. Otherwise it won't be possible for the escrow agent to make the payments on the wrapped obligation. Don't even *think* about requiring supplemental monthly payments from the seller to the escrow agent. It almost never works. Anyway, most escrow agents either will not accept this requirement, or will charge a prohibitive fee for the additional servicing requirement.
3. Coordinate the amortization periods. The junior REC must be structured to ensure that the senior obligation will be retired before the junior REC is paid off. For example, if the senior obligation will be paid off with 200 regularly scheduled payments, then the junior REC should be structured to amortize in not less than 201 payments. There are some additional risks to consider:
 - The junior REC can have a shorter amortization period, provided the amounts required to be disbursed to the senior obligation are increased to assure timely payoff. Before doing this, however, be sure to check the senior obligation for any prepayment penalties or prohibitions.
 - If the wrapped obligation contains any balloon payment provisions, it would be advisable to include matching balloon provisions in the junior REC, in order to provide sufficient funds to the escrow agent to satisfy the senior balloon obligation. If this is not done, then the buyer loses control of his own destiny, and must depend on the seller to make the balloon payments when they become due.
 - If the wrapped obligation contains an adjustable interest rate provision and/or variable payments, then the monthly disbursements from the junior REC to the wrapped obligation must be structured to retire the wrapped obligation within the amortization period of the junior REC under the worst-case scenario.
4. Require that all prepayments of principal be applied to the wrapped obligation. *Think about it.* Even if you carefully planned step 3 above so that scheduled payments on the junior REC will retire the senior obligation in the required number of payments, the buyer can 'trash' your plans by making voluntary principal prepayments. If the prepayments are disbursed to the seller, rather than to the senior obligation, then when the junior REC is finally paid off, there may well be an unpaid balance remaining on the senior obligation. That could be catastrophic if the seller has moved from the state, cannot be found, or simply doesn't want to pay off the balance! To prevent this from happening, the REC should contain an escrow instruction requiring the escrow agent to disburse the appropriate monthly amount, **plus all principal prepayments** for credit to the wrapped obligation. Include this provision in the purchase agreement addendum, to be sure it gets included in the REC. Check the senior obligation for clauses penalizing or prohibiting prepayments!

5. Determine how taxes and insurance premiums will be paid. Does the senior obligation require that taxes and insurance premiums (T & I) be paid through its servicing agent? If so, then a provision must be added to the junior REC requiring the buyer to make these additional payments to the escrow agent, for further remittance to the senior obligation. See **Examples**, this chapter.

It will also be necessary to include a provision requiring the seller to remit to buyer any refund received from the mortgagee at payoff. See **Examples**, this chapter. Because the mortgage was wrapped, the mortgagee will not recognize the buyer's entitlement to any refund from the T & I trust account. An assignment of trust funds could be executed and placed in escrow, but many mortgage servicers cannot be relied upon to abide by the assignment.

If taxes and insurance premiums are not required to be submitted through the senior servicing agent, then it would be advisable to require the buyer to pay taxes and premiums monthly to the junior REC escrow agent, who would then be responsible for paying these items as they become due. See **Examples**, this chapter.

If it is decided to require escrowing of taxes and insurance, a copy of the most recently paid tax bill and a copy of the declarations page of the insurance policy **must** be provided to the escrow agent at the time the documents are first placed in escrow. If this is not done, the escrow agent should and most likely will refuse to commence the service until the items are produced, or the T & I servicing requirement is removed from the REC.

Paying T & I through the escrow agent is a good idea, for several reasons.

- It is one of the best bargains you will ever find. Most escrow agents charge two or three dollars per month for this service. However, some agents also charge a significant disbursement fee when the taxes or insurance premiums are paid out, and they will deduct that fee from the T & I impound balance. The fee is often not shown on the escrow agent's fee schedule. It would be a good idea to "shop" escrow agents for a disclosure of the "outgoing" fee that will be charged, before selecting an escrow agent.
- It helps prevent defaults. By spreading the tax and insurance payments evenly over 12 monthly payments, the buyer avoids the burden of large annual or semi-annual tax payments. Also, because the escrow agent will be paying the insurance premium annually,

the additional fees assessed by insurance companies for paying on the installment method is avoided.

- It relieves the seller of the burden of checking periodically with the county treasurer or the insurance agent to confirm buyer's performance of these obligations. It removes the necessity for sending demand letters for proof of payment of taxes and/or insurance. Sellers frequently neglect these tasks, with the result that the property taxes may become several years delinquent or the insurance may lapse, leaving the seller's interest uninsured.
6. Be sure the correct type of hazard insurance policy is in effect. The buyer can obtain a homeowner policy, and name the seller and the mortgagee on the policy as loss payees. The insurance company will send a copy of the new policy to the mortgagee, however, which will alert the mortgagee to the sale and possibly result in an exercise of a due-on-sale clause. For this reason, some parties have attempted to allow the seller's existing policy to remain in effect, and add a provision to the REC that the buyer must obtain separate insurance coverage, if desired, to protect his interest in the property and the contents. The problem with this approach is that the seller is no longer an 'owner-occupant', and his homeowner's policy is no longer appropriate for his risk category. A failure by the seller to disclose the change of ownership and occupancy of the property could result in a denial of coverage by the insurer. The seller will need to convert his policy to a landlord - type policy. The insurance company will send a copy of the new policy or certificate to the lender, however, thereby defeating the entire purpose of this little subterfuge. For additional discussion of this issue, see Chapter 6, Taxes and Insurance.

Suggestion: A great deal of effort has been expended in the marketplace to avoid disclosure of the sale to the mortgagee, for fear of triggering a due-on-sale clause. This is a dangerous game, besides raising some possible ethical issues. If the mortgage is HUD-insured, the wrap-around approach may be completely unnecessary. If the buyer is financially unable to meet HUD's creditworthiness-at-time-of-sale requirements, consider the alternative method for establishing creditworthiness described in chapter 3.

Examples of Wrap-Around Clauses Using the RANM Standard Form

The RANM standard form accommodates wrap-around transactions. The terms-of-payment clause in paragraph 2 of the form need only state the purchase price, down payment and net balance owed to the seller, and the terms for payment of that balance. If the wrapped obligation requires PITI payments, then a separate clause should be added to paragraph 2 requiring the buyer to pay, or to reimburse the seller for taxes and insurance premiums paid through the wrapped obligation. Paragraphs 3(a) and 3(b) of the form should be amended to relieve the buyer of the obligation to provide tax receipts and copies of the insurance policy and renewals to the seller.

Payment terms (Wrapped mortgage, payments include PITI)

2. Price and Payment: The Purchaser agrees to buy the above-described Property and to pay Seller therefor the total sum of **EIGHTY THOUSAND AND NO/100 DOLLARS (\$80,000.00)**, payable as follows: **FIVE THOUSAND AND NO/100 DOLLARS (\$5,000.00)**, cash down payment, the receipt of which is hereby acknowledged, and the balance of **SEVENTY FIVE THOUSAND AND NO/100 DOLLARS (\$75,000.00)**,

payable as follows:

In monthly installments of \$800.00 or more, at Buyer's option, including interest from date on the unpaid principal balance at the rate of 10.00% per annum, commencing February 20, 1998 and on or before the 20th day of each successive month thereafter, until paid in full.

In addition to the above monthly installments of principal and interest, Buyer will remit a monthly amount for the payment of property taxes and hazard insurance premiums, presently in the amount of \$185.70. This amount may be adjusted from time to time as required by the servicing agent for the mortgage herein described. The escrow agent will remit said funds monthly [to the servicing agent for the mortgage herein described] [to the Seller as reimbursement for taxes and insurance premiums included in the mortgage payments herein described].

Payment terms (Wrapped mortgage, payments include PI only)

Same as above, except the T & I clause would be changed to read as follows:

In addition to the above-described payments of principal and interest, the buyer will remit with each monthly payment to the escrow agent, an amount for the payment of property taxes and hazard insurance premiums, presently in the amount of \$____ for taxes and \$____ for insurance premiums, which amount may be adjusted from time to time as required by the escrow agent hereinafter named. The escrow agent will use said funds to pay property taxes and hazard insurance premiums for the subject property as they become due.

Senior obligation wrapped, paid through escrow agent (page 2 of the RANM form)

The following lien(s) or obligation(s) is currently outstanding on the property:

Type of lien or Obligation Holder	Loan Number	Recording Data: Book & Page
Mortgage to ABC Mortgage Company	F97-456782	04-07-97 Bk. 97-4 Pg.7052-7055 Document no. 97034829

The Buyer does not assume or agree to pay the above-described obligation. All payments of principal and interest due on such obligation shall be remitted by the Escrow Agent to ABC Mortgage Company or its successor in interest out of the Seller's proceeds. If the payments due from Buyer are insufficient to satisfy the amounts due to be made on the above-described obligation, Seller shall pay Escrow Agent such additional funds as are necessary to keep such obligation current. Upon payment of this contract in full, Seller shall obtain a release of the premises from the lien of the obligation described above. Buyer shall pay all late payment penalties on the above-described obligation resulting from late payments. Seller shall notify Escrow Agent of any changes in the monthly payment as may be required by ABC Mortgage Company or its successor in interest.

If the Seller at any time receives a refund from the mortgagee of any impounded tax and hazard insurance premium funds, then Seller shall thereupon pay the entire amount of such refund to the Buyer herein. Seller

shall, upon request from Buyer, obtain from the mortgagee and provide to Buyer an accounting for all transactions in the mortgagee's impound fund for taxes, insurance and unapplied funds.

Subdivisions

The situation we consider here is the seller who has acquired a tract of land by a form of seller financing with installment payments, then subdivides the property into a number of lots for resale. No attempt is made in this book to discuss the requirements of the various federal, state and local laws that may regulate such subdivisions. We are concerned, however, about the use of the wrap-around contract as the vehicle for resale transactions.

The 'blanket' contract.

It is clear that a buyer under a REC can subdivide the property into two or more parcels if permitted by the terms and conditions of the REC, and provided he complies with the applicable statutes and regulations. It may seem obvious that, after the property is replatted, deeds to individual lots should be executed by seller and buyer, and substituted in escrow for the tract deeds that were escrowed before the replatting occurred. Incredibly, however, this is often not done, and there is no provision in the REC requiring that it be done! Also, there should be a provision in the REC setting forth the principal reduction requirements for release of deeds from escrow for individual lots. If appropriate, the sequence of lot releases should also be specified.

The 'wrap-around' contract.

The REC by which the subdivided lots are sold is properly classified as a 'wrap-around', because the lot buyer does not assume and agree to pay the senior obligation, which is a larger debt secured by the subdivision. When the junior REC is paid in full, the buyer will receive a warranty deed from escrow which purports to convey legal title free and clear of any senior encumbrances. The seller is therefore obliged at that time to obtain a release of the lot from the lien of the 'blanket' REC or mortgage. If the 'blanket' instrument is a REC, he must obtain a warranty deed to the paid-off lot from the escrow agent servicing the REC. If it is a mortgage, he must get a partial release of mortgage from the mortgagee. (If the 'blanket' mortgage was used as seller financing, the entire process is facilitated if an escrow agent was appointed to service the mortgage note and hold the partial lot releases.)

Drafting suggestion. The "price and payment" paragraph of the wrap-around REC will be indistinguishable from any other wrap-around agreement. However, the "Prior Obligations" paragraph on the second page of the RANM standard form should specify that the seller, rather than the escrow agent, will be required to make the payments on the blanket obligation. This is necessary, because the payment on the blanket obligation will be much larger than the payment on the junior REC, and the escrow agent for the blanket obligation will not be authorized to accept

partial payments. See **examples**, below.

Pre-approval of REC form required. If the subdivided lot is not within the boundaries of a municipality and is not within the extraterritorial subdivision and platting jurisdiction of a municipality, then before the first sale from the subdivision occurs, the county commission must approve the form of REC, warranty deed and special warranty deed to be used in the resale transactions. See the New Mexico Subdivision Act, sect. 47-6-8 (B) NMSA 1978. Violation of the Act carries severe criminal penalties, plus actual civil damages, costs and attorney fees.

Example of clause in ‘blanket’ REC for land to be subdivided

It is agreed that Buyer may subdivide the subject property into 16 lots of approximately equal size and dimensions. All costs and expenses of subdividing and replatting will be paid by Buyer. Buyer will comply with all federal, state and local laws and regulations governing the subdivision of the Property. Upon final approval by the county commission of the replat, the seller will execute separate warranty deeds for the replatted lots, and Buyer will execute separate special warranty deeds for said lots, and all said warranty deeds and special warranty deeds will be substituted for the deeds now being placed in escrow, to be held and subsequently delivered by the escrow agent in accordance with this Agreement. Warranty deeds to individual lots may be released from escrow, in such sequence as Buyer may request, upon reduction of the unpaid principal balance of this contract by \$5,000.00 for each lot, provided that accrued interest on the unpaid principal balance is paid current to the date of each release, and provided further that Buyer is not otherwise in default of any requirements of this contract.

Example of clause in REC for lot sold from a sub-division

The following lien(s) or obligation(s) is currently outstanding on the property:

Type of lien or Obligation Holder	Loan Number	Recording Data: Book & Page
Real Estate Contract dated 04-06-97	6044558	Bk. 97-4 Pg. 7052-7055 Document no. 97034829

The Buyer does not assume or agree to pay the above-described obligation. All payments of principal and interest due on such obligation, and all escrow fees shall be remitted by the SELLER to Best Escrow Company. Upon payment of this contract in full, Seller shall obtain a release of the premises from the lien of the obligation described above.

5

Principal and Interest

Before the advent of the RANM standard REC form in 1981, perhaps no other aspect of REC's caused more bickering between buyer, seller and escrow agent than the manner of allocating payments to principal and interest. The REC form 103 used before that time contained no provisions whatsoever relating to principal and interest allocations, and the matter was left to the discretion of the escrow agent. Because policies of escrow agents varied widely, there was no well-settled industry standard as to how payments should be allocated. The RANM standard form allows a choice between 'daily interest' and 'periodic interest' calculations. Both methods are within a level periodic payment type of amortization, as contrasted to the more uncommon principal-plus-interest payment type. This chapter deals with these techniques, the application of 'balloon' payments, and the phenomenon known as "negative amortization."

Level Periodic Payments

In the most common form of a simple REC, the seller's equity balance is to be paid by level - i.e., constant - periodic payments (monthly, quarterly, semi-annual or annual) until the balance is paid in full. The unpaid balance is to bear interest at a stated annual interest rate, and the interest accrued between payments is to be deducted from each ensuing payment, with the remainder of that payment allocated to reduction of the principal balance. For the purposes of this section, it is the concept of "interest accrued between payments" that causes all the trouble. There are two quite different versions of this concept:

- (A) interest accrued between due dates of scheduled payments, regardless of the dates payments are actually made, and
- (B) interest accrued between dates payments are "actually made," regardless of their respective due dates.

Periodic Interest

This method for allocating payments to principal and interest is best exemplified by a printed amortization schedule, like the one shown in figure 1. In illustration, the **first payment** will be allocated first to interest accrued **from** March 15 **through** April 1, a period of 17 days, and the remainder to principal. For subsequent payments, the actual number of days in each month is ignored. The year is divided into 12 equal units, and 1/12 of a full year's interest on the declining balance is deducted from each payment. (A

variation of this technique assumes a 365-day year, allocating interest to each month in proportion to the actual number of days contained in each month. For example, since April contains 30 days and May contains 31 days, the payment due May 1 would be charged 30/365 of a full year's interest on the balance, and the payment due June 1 would be charged 31/365 of a year's interest on the balance existing at that time.)

The critical element of this technique is that the payments are credited to principal and interest as shown on the amortization schedule. No adjustment is made for any payments made later or earlier than their respective due dates. The only exceptions are the first and last payments. We have already seen how the first payment is charged with interest accrued from the date of the contract through the due date for the first payment. In similar fashion, it is customary to charge interest on the final payment only through the day of the month when the final payment is actually made.

Advantages: The advantages of this method are simplicity, predictability and freedom from error. By examining an amortization schedule, it can be determined exactly what the remaining balance of the contract will be at any point in time during the life of the REC. There is no need for a computer or for skilled clerks. The amortization schedule itself can be stamped or initialed by a clerk, and thereby serve as a payment record. (That is how it was done throughout New Mexico before 1975, when I founded Security Escrow Corporation. The company pioneered the use of computers in escrow offices, thereby ruining the simple life forevermore.)

Disadvantages: In a word, the biggest potential disadvantage to this method is unfairness. Technically, 'interest' is the price paid for the use of money for a period of time. If the buyer habitually pays late, or falls substantially in arrears on his payments, it can correctly be argued that "due-date" interest posting is unfair to the seller because the buyer is not being charged interest on each level of the declining principal balance for the actual amount of time he had the use of that balance. Conversely, the buyer who pays early may argue that he is being penalized, since he is being charged interest for more time than he actually had use of the balance. In either case, the degree of unfairness is not usually as great as the offended party imagines it to be. See **Lost Interest**, below.

Daily Interest

This method of allocation requires that interest be calculated on the unpaid balance through the date a payment is actually made, rather than through the due date for that payment. In Figure 2, interest for the first payment is calculated **from** March 15 **through** April 11, a period of 27 days (**don't** count March 15, **do** count April 11). For the second payment, interest is calculated on the new balance **from** April 11 **through** May 11, which is a period of 30 days. The calculation is performed as follows:

$$(\text{annual interest rate} \times \text{balance}) / 365 \times (\text{days-interval}) = \text{accrued interest.}$$

Advantages: The primary advantages of this method are precision and fairness. The buyer is always charged the amount of interest accrued on the unpaid balance for the **actual number of days that the balance was unpaid**. Neither buyer nor seller is favored. This method protects the seller against loss of interest when payments are made late; it also gives a benefit to the buyer who pays early.

Disadvantages: The main problem is unpredictability. Principal and interest allocations can vary widely from month to month. Amortization schedules are useful only as a guide to show the time required to amortize a balance, with the assumption that all payments are made on their respective due dates. When there is a substantial time delay between payments, the payment may not be large enough to pay all the interest accrued, resulting temporarily in the phenomenon known as 'negative amortization', which is discussed below.

Lost Interest

Many sellers feel that they lose large amounts of interest when the escrow agent employs the "periodic" method of allocating interest, and the buyer habitually pays late. The commonly heard complaint is, "The buyer pays 10 days late every month, so I am losing 10 days' interest every month." The statement is erroneous, of course. In order to determine exactly how much interest the seller loses, we must compare the periodic method to the "daily" method in a real situation. Figures 1 and 2 show a direct comparison between the two methods. Observe that all payments are 10 days late except the 12th payment, which is made on its due date.

By using the periodic method, the seller loses only \$2.12 interest over a period of one year, even though the buyer was 10 days late with 11 of the first 12 payments! Of course, there is a compounding effect resulting from the fact that the buyer received the benefit of a \$2.12 principal reduction that he did not deserve. Even if the buyer pays on time after the first year, the seller will continue to lose about 21 cents interest on that \$2.12 annually. Nevertheless, the impact is not nearly as catastrophic as many sellers imagine it to be.

The effect is more dramatic if the buyer fails to make any payments for several months, then makes a single "catch-up" payment. In our example, suppose the buyer makes no payments until March 1, then makes a single catch-up payment of \$1,200.00. Figure 3 shows the result, using the daily method. Here, the periodic method costs the seller \$20.39 lost interest in 1 year, when compared to the daily method. It should be noted, however, that the seller has a remedy to avoid situations like this: he can issue a demand letter pursuant to the REC, and force the buyer to make payments or lose the property.

FIGURE 1 (Interest accruing from March 15 at 10.00% per annum)

Date Due	Date Paid	Payment	Interest	Principal	Unpaid
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					Balance
					\$8000.00
April 1	April 11	\$100.00	\$37.26	\$62.74	\$7937.26
May 1	May 11	\$100.00	\$66.14	\$33.86	\$7903.40
June 1	June 11	\$100.00	\$65.86	\$34.14	\$7869.26
July 1	July 11	\$100.00	\$65.58	\$34.42	\$7834.84
Aug 1	Aug 11	\$100.00	\$65.29	\$34.71	\$7800.13
Sept 1	Sept 11	\$100.00	\$65.00	\$35.00	\$7765.13
Oct 1	Oct 11	\$100.00	\$64.71	\$35.29	\$7729.84
Nov 1	Nov 11	\$100.00	\$64.42	\$35.58	\$7694.26
Dec 1	Dec 11	\$100.00	\$64.12	\$35.88	\$7658.38
Jan 1	Jan 11	\$100.00	\$63.82	\$36.18	\$7622.20
Feb 1	Feb 11	\$100.00	\$63.52	\$36.48	\$7585.72
March 1	March 1	\$100.00	\$63.21	\$36.79	\$7548.93
TOTALS			\$748.93	\$451.07	

FIGURE 2 (Interest accruing from March 15 at 10.00% per annum)

Date Due	Date Paid	Days Interval	Payment	Interest	Principal	Unpaid Balance
						\$8000.00
April 1	April 11	27	\$100.00	\$59.18	\$40.82	\$7959.18
May 1	May 11	30	\$100.00	\$65.42	\$34.58	\$7924.60
June 1	June 11	31	\$100.00	\$67.30	\$32.70	\$7891.90
July 1	July 11	30	\$100.00	\$64.86	\$35.14	\$7856.76
Aug 1	Aug 11	31	\$100.00	\$66.73	\$33.27	\$7823.49
Sept 1	Sept 11	31	\$100.00	\$66.45	\$33.55	\$7789.94
Oct 1	Oct 11	30	\$100.00	\$64.03	\$35.97	\$7753.97
Nov 1	Nov 11	31	\$100.00	\$65.86	\$34.14	\$7719.83
Dec 1	Dec 11	30	\$100.00	\$63.45	\$36.55	\$7683.28
Jan 1	Jan 11	31	\$100.00	\$65.26	\$34.74	\$7648.54
Feb 1	Feb 11	31	\$100.00	\$64.96	\$35.04	\$7613.50
March 1	March 1	18	\$100.00	\$37.55	\$62.45	\$7551.05
TOTALS				\$751.05	\$448.95	

FIGURE 3

Date Due	Date Paid	Days Interval	Payment	Interest	Principal	Unpaid Balance
						\$8000.00
April 1 thru March 1	March 1	351	\$1200.00	\$769.32	\$430.68	\$7569.32

Date of Payment

Using the "daily" method, when does interest stop accruing on the payment? The law generally is that a payment is deemed to be "constructively" received by its recipient when it is actually received by his agent. Thus, escrow agents using the daily method generally accrue interest through the date payment is received by the escrow agent. When the payment is placed in the escrow agent's post office box (or dropped through the mail-slot) on a weekend or holiday, the escrow agent's office policy will determine when interest stops accruing.

Serious problems can arise when, due to the size of a payment made by non-certified funds, the escrow agent elects to send the check for collection before processing. The collection process can consume one or two days for local checks, and as much as three weeks for checks drawn against a bank in New York City. Such delays generate disputes over the proper interest accrual cutoff date. It is for this reason that most escrow agents have adopted special rules requiring certified funds for payoffs, balloon payments, and infrequent (e.g., annual) payments.

Form 103 contains no provision whatever regarding the manner of interest accrual. It is left to the parties to insert their own provisions. If the parties fail to do so, then by default the escrow agent must decide how to calculate interest. The policies of escrow agents differ widely in this regard. Most agents now use the daily method, although some still use the periodic method. Some agents who use the periodic method will convert to the daily method upon request of either party to the REC.

The RANM form offers a choice between daily and periodic interest accrual. The parties merely check and initial the method they want to use. The choice is initially made, however, on the purchase agreement REC addendum, and incorporated from there into the final REC form.

Drafting Suggestions: If the RANM form is not utilized, then the parties should add a statement to their contract to indicate how interest is to be accrued. Any of the following statements might be used to specify that interest shall be calculated on a daily basis:

- Interest shall be calculated from date of payment to date of payment.
- Monthly payments shall be apportioned between principal and interest, and applied first to the payment of all interest accrued to date of payment, and the balance applied to principal.
- Each monthly payment shall be applied first to interest accrued to date of payment on the unpaid balance, then to principal reduction.

Either of the following statements could be used to indicate intent to post payments on a periodic basis, as they would appear on an amortization schedule:

- Monthly payments shall be credited to principal and interest as though the payments were made on their respective due dates.
- Interest shall be calculated from due date to due date of each successive installment, regardless of the date such installments are actually paid.

But please note that the following statement, while sometimes used, fails to indicate a choice between either method, because it is equally compatible with both meanings:

-Payments shall be allocated first to interest, then to principal.

The statement indicates that amortization will be of the level payment type as opposed to the principal-plus-interest type, but it fails to address the method of interest accrual.

Negative Amortization

With the advent of "creative financing" in the 1980's, many REC's called for monthly payments in an amount less than the accruing interest. The buyer actually goes "in the red" every month, even though all monthly payments are made on a timely basis. In such cases, there is usually provision for one or more future lump-sum payments ('balloons') or scheduled future increases in the periodic payment amount, or both, which will "catch-up" the unpaid interest and start amortizing the principal balance.

Treatment of Unpaid Interest

Disputes sometimes arise between buyer and seller regarding the treatment to be given to the unpaid interest during a period of negative amortization. The seller would prefer to have the escrow agent add the unpaid interest to the principal balance. This would 'compound' the unpaid interest, meaning that the unpaid interest for a given month would itself draw interest thereafter. The buyer would prefer to have the unpaid interest

cumulated as a deficiency balance separate from the principal balance. He would further expect that there would be no "interest on unpaid interest" charged, and that the principal balance would remain constant.

The RANM form and form 103 both fail to address the issue of negative amortization. In the absence of an explicit contract provision, the problem is dumped into the lap of the escrow agent, who must look to the law for guidance. New Mexico has no statutory law or appellate court decisions regarding the propriety of charging "interest on interest." However, the majority of case decisions in other states have held that, in the absence of a statute or an agreement between the parties to the contrary, interest cannot be charged on unpaid interest. See *45 American Jurisprudence 2d, Interest and Usury, Section 76 et seq.* Most escrow agents, therefore, have adopted the policy that unpaid interest will not be added to the principal balance, unless the REC states otherwise.

Non-Amortizing Debts, or the 'perpetual contract'

When the REC fails to include payment terms that would eventually terminate negative amortization, the REC becomes 'perpetual', in the sense that the buyer has no obligation to pay the unpaid principal balance at any certain or determinable time. The situation arises, either by mutual mistake or by design, when the parties specify a minimum monthly payment that is not large enough to pay more than the monthly accruing interest. If there is no provision for a balloon payment, a change in the minimum monthly payment, or a change in the interest rate that would result in a continuing reduction and ultimate retirement of the unpaid principal balance, then the balance would never be paid off unless the buyer chose to do so, at his convenience. Thus, an issue is raised as to whether the REC constitutes an enforceable contract.

As a general rule, contracts that are vague and uncertain as to their essential terms, such as price and time and place of performance, are unenforceable. While there are many exceptions to the rule, the New Mexico Supreme Court held in 1957 that where the contract does not itself set a time for payment of a deferred balance, the Court will not imply a reasonable time for performance, and will not grant specific performance of the contract to the seller. See *Snow*, p. 13, CLA.

A fundamental principle of contract law is that if one party to the contract is not obligated to perform, then the other party also has no obligation. The inescapable conclusion is that either party to the contract could declare the contract to be void, and sue to have the Court grant a rescission of the contract, and require each party to restore the other party to the status quo that existed at the inception of the contract.

Could the buyer change the situation by making a voluntary prepayment in an amount sufficient to cause amortization of the contract by the minimum monthly payment? Such an action would remove the objection that time of performance is uncertain and

indeterminable, because the projected amortization of the unpaid balance by the minimum monthly payments would create a determinable date of final payment.

In theory, at least, the buyer should not be able to unilaterally cure the fatally defective contract. The reason is that there never was a meeting of the minds as to an essential element of the contract (the date of performance). The buyer cannot supply the requisite element of mutual agreement by merely making an extra payment. By determining the amount of the voluntary payment, the buyer could unilaterally determine the remaining amortization period of the contract, without the seller's consent or agreement. For example, he could pay just enough so that the minimum monthly payment would pay off the contract in 50 years! If the seller accepts a voluntary balloon payment without objection, he may be held to have consented to the new arrangement by his silence. So long as the seller acts to rescind the contract without accepting any voluntary balloon payments, the Court should allow the rescission.

Drafting suggestion. The problems created by a non-amortizing contract are obviously great, and are likely to lead to litigation. When drafting a REC, be sure that the minimum monthly payment is greater than the monthly accruing interest on the starting balance.

Income Tax Considerations

Negative Amortization

For a taxpayer who itemizes deductions on IRS Form 1040, interest paid on a REC is generally a deductible expense. For the recipient, it is included in ordinary income. Contracts involving negative amortization present some intriguing twists to this rule.

When accrued but unpaid interest is not added to the principal balance, the effect on the taxpayer depends on whether he uses accrual or cash accounting methods. Under the accrual method, the taxpayer must recognize the interest expense or income when accrued, rather than when it is actually paid. The opposite is true for the cash method.

When unpaid interest is added to the principal balance, it becomes principal and ceases to be interest. In effect, the unpaid interest is paid by making a new loan in the amount of the interest deficiency. The accrual basis taxpayer must recognize the unpaid interest as income or expense at the point in time when the unpaid interest is added to the principal balance. Tax treatment of the cash basis taxpayer is beyond the scope of this book. To determine when the compounded interest is considered by the IRS to be "paid," consult your accountant.

Unstated Interest

When the parties to an owner-financed property sale provide for deferred payments with a zero rate of interest or a low rate of interest, section 483 of the Internal Revenue Code may require that a portion of the stated principal be treated as unstated interest at a higher imputed rate for tax purposes. The law applies:

- to any contract for the sale or exchange of any property (houses, vacant land, mobile homes);
- if the sales price exceeds \$3,000 and if some or all of the deferred payments are due more than 1 year after the date of the sale or exchange;
- to all payments due more than 6 months after the date of the sale or exchange.

To determine whether unstated interest exists, it is necessary to:

1. calculate the sum of all payments due under the contract more than 6 months after the date of the sale or exchange;
2. calculate the sum of the present values of such payments and the present values of any interest payments due under the contract, using the ‘applicable Federal rate’ as the discount rate; and
3. calculate the excess of (1) over (2). The difference constitutes ‘unstated interest’.

The ‘applicable Federal rates’ are determined each month for the next ensuing month by the Secretary of the Treasury under the authority of section 1274(d) of the Internal Revenue Code. The Secretary establishes a ‘short-term’ rate, which applies to contracts having a term of not more than 3 years, a ‘mid-term’ rate which applies to contracts with terms of more than 3 years, but not more than 9 years, and a ‘long-term’ rate which applies to contracts with terms exceeding 9 years. For example, the short-term rate is defined as the average market yield on outstanding marketable obligations of the United States with remaining periods to maturity of 3 years or less. Applicable Federal rates are available through accountants and tax lawyers who subscribe to tax services, and they are published one time each month in the “Money and Investing” section of the Wall Street Journal (good luck finding it – it would be easier to call your accountant!).

The applicable Federal rate cannot exceed 6 %, compounded semiannually, if the sale or exchange is by an individual to a family member (as defined in I.R.C. section 267(c)(4)), to the extent that the sales price does not exceed \$500,000. The rate can be higher for that portion of the sales price exceeding \$500,000.

Balloon Payments

By definition, a 'balloon payment' is a principal payment required in addition to the regular installment payments. Balloon payments are generally intended to be principal reduction payments in their entirety. Nevertheless, problems often arise because the parties fail to contemplate the existence of accrued unpaid interest at the time that a scheduled balloon payment is made.

The most typical example is a balloon payment made between due dates for regular monthly payments. Suppose an account has a \$10,000.00 balance, that the interest rate is 12.00%, that the buyer makes a balloon payment of \$6,000.00 on the 21st day of a 30-day month, and that regular payments are due on the first day of each month. Using daily interest accrual, one might expect to charge the buyer interest on \$10,000.00 for 20 days (from the 1st through the 21st) and on \$4,000.00 for 10 days. However, this is not possible, since interest for 20 days on \$10,000.00 (\$65.75) must be taken from the balloon payment, leaving only \$5,934.25 to be applied to principal. This leaves a new balance of \$4,065.75, and the interest on this amount from the 21st day will be taken from the next regular payment. Yet, many balloon payment clauses are phrased to require the extra payment to be applied entirely to the principal balance. If the clause is interpreted literally by the escrow agent, the seller will simply lose \$65.75 interest, in this example. The escrow agent cannot require the buyer to pay an extra \$65.75, because the REC by its terms simply does not require such a payment. It is not likely that the seller (or anyone else) contemplated the loss of accrued interest in this manner. In practice, the literal mandate to apply the entire balloon payment to principal is usually ignored, and accrued interest is first deducted from the payment.

The RANM form addressed this problem with the following language:

- '.... any prepayment shall be credited first to accrued interest, then to the principal balance of this contract....'

Multiple Payments vs. Prepayments

It is the custom in the real estate industry in New Mexico to draft REC's to require periodic payments of a certain amount "or more, at Purchasers option." Varying interpretations of this phrase have caused great difficulty in the administration of contracts. The problem arises when the buyer wishes to make an early payment of a required installment. For example, suppose a buyer plans to vacation in Europe for the summer. He wants to make his June, July and August payments to the escrow agent on June 1, then resume with the September payment upon his return. Can he do it?

Some sellers, who might be described as aggressive, contend that the buyer cannot prepay regular installments. They interpret the "or more" phrase to mean that any amounts paid in addition to the current installment must be applied to principal, and that such prepayment does not excuse the next regular installment. By this view, our vacationer could lose his property before returning from Europe. The seller could issue a demand notice on July 2 for the July payment, which would be deemed delinquent on that day.

Others believe that this interpretation is arbitrary, unreasonable and "shocking to the conscience" (a phrase often used by the Supreme Court when ruling on high-handed attempts by sellers to impose forfeitures on buyers). This view sees nothing wrong with allowing the buyer to prepay a regular installment, if he chooses to do so. Especially so, if periodic interest accrual is used so that the seller gets the benefit of prepaid interest (for July and August, in the example of our European vacationer.) Adherents to this view contend that no court would allow a forfeiture to occur on equitable grounds when the buyer has in good faith attempted to give the seller the use of two payments before they became due. Besides, they contend, the contrary interpretation leads to an absurdity. If the buyer must make a payment each and every month, then theoretically a payment due June 1, for example, cannot be paid on May 31. The seller could treat that payment as an extra prepayment in May, and still demand another payment in June! Furthermore, if not paid precisely on June 1, the buyer could be treated as delinquent, and a demand notice issued to him on June 2. While such conduct on the part of the seller might seem inconceivable to a reasonable person, it does occur.

Recognizing the need to avoid such nonsense, the RANM form distinguishes between payments (i.e., regularly scheduled installments) and prepayments, and allows the buyer to make the call, thusly:

- 'All payments shall be assumed to be regular payments, and not prepayments, unless otherwise specified by Purchaser in writing at the time of delivering such payments to escrow agent. Unless otherwise provided, Purchaser may prepay the unpaid balance in whole or in part at any time. Any prepayment shall be credited first to accrued interest, then to the principal balance of this contract, exclusive of assumed liens or obligations, then to any assumed lien or obligation. Notwithstanding any prepayments, Purchaser shall make the next regularly scheduled payments.'

With this language, our European vacationer is given the presumption, even without written instructions, that his triple-amount payment is intended to be applied as three monthly installments. Furthermore, if the daily interest accrual option is elected, the buyer may make installment payments early without prepaying interest. Of course, when he resumes making installment payments there will be more accrued interest to be taken from the next installment. In the example of our vacationer, the September installment would be credited first to interest accrued from June 1 to date of payment of the September installment, then to principal.

Principal-Plus-Interest Payments

Buyers sometimes wish to pay a fixed, or constant amount on principal periodically (e.g., monthly) plus the interest accrued on the principal balance since the last payment was made. Using periodic interest accrual and an interest rate of 10.00% per annum, the amortization schedule would appear as shown in Figure 4. The payments would be posted in the same manner, regardless of the date they are actually paid.

The advantage of this type of amortization is that the parties know at all times exactly how many payments remain, without the need to refer to an amortization schedule. The disadvantage is that the buyer needs to refer to an amortization schedule every month in order to know how much is required for the next payment. Also, if the buyer makes any additional payment of principal, he must immediately get a new amortization schedule, because the amount required for every subsequent payment is changed by the extra principal reduction. Because it is so cumbersome, this amortization method is seldom used.

FIGURE 4

Date Due	Payment	Interest	Principal	Unpaid Balance
				\$8000.00
April 1	\$137.26	\$37.26	\$100.00	\$7900.00
May 1	\$165.83	\$65.83	\$100.00	\$7800.00
June 1	\$165.00	\$65.00	\$100.00	\$7700.00
July 1	\$164.17	\$64.17	\$100.00	\$7600.00
Aug 1	\$163.33	\$63.33	\$100.00	\$7500.00
Sept 1	\$162.50	\$62.50	\$100.00	\$7400.00

An even more rare method is principal-plus-interest with daily interest accrual. The required monthly payment amount changes every day until the payment is made! This method is almost impossible to administer, and is hardly ever used. Most escrow agents will either refuse to service such an account or will charge a premium fee for the special handling required.

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TAXES AND HAZARD INSURANCE

Property Taxes

Regardless of the form of the seller financing instrument used (RANM REC, 103 REC, deed of trust or mortgage), the buyer is obligated to assess the property in his name, and to pay the property taxes. The contract may allow the buyer to pay the taxes directly to the county treasurer, or it may require him to pay the taxes through the escrow agent, who either pays the taxes or remits the funds to a senior lien holder who pays them. Methods available for enforcement of the buyer's obligations depend on how the buyer is required to pay the taxes. Failure to pay the taxes can result in total loss of both the buyer's and seller's interests in the property.

Purchaser's obligations, Seller's remedies

...under the RANM form.

The buyer's obligations are stated in paragraph 3(b) of the contract:

Taxes

Unless otherwise stated herein, the property taxes for the current year have been divided and prorated between Seller and buyer as of the date of this Contract, and the buyer is responsible for and will pay the taxes and assessments of every kind hereafter billed.

Buyer will have the Property assessed for taxation in buyer's name. Upon request by Seller, Buyer will send copies of the paid tax receipts each year to Seller.

The seller's remedies for noncompliance are set forth in paragraphs 3(d) and 5(a):

Seller's Rights

Should the buyer fail to pay...taxes and assessments,...Seller may pay the same (but is not obligated to do so) for protection of the Property and his interest therein. Payment of such charges shall not be deemed a waiver of any default of buyer for failure to pay such charges, and such amounts as have been so paid shall be immediately due and payable to Seller, and shall bear interest until paid at the same rate as provided in Paragraph 2 above.

SELLER'S RIGHTS IF PURCHASER DEFAULTS

Default Notice. Time is of the essence in this contract, meaning that the parties shall perform their respective obligations within the times stated. If Purchaser...fails or refuses...to maintain insurance or to pay taxes, assessments, or other charges against the Property, or fails or refuses to repay any sums advanced by the Seller under the provisions of paragraph 3 above, the Seller may make written demand upon the Purchaser, with such notice to specify the default and the curative action required,.... (procedures to be followed under the terms of this paragraph are discussed in detail in Chapter 12).

There are some problems with this language. First, the purchaser is in default only if he:

1. fails or refuses to pay the taxes, or
2. fails or refuses to repay any taxes advanced by the seller.

Although purchaser agrees to assess the property in his name, and agrees, upon request by seller, to send copies of the paid tax receipts each year to seller, *failure to do either of these things is not declared to be a default*.

Also, while the contract declares that “time is of the essence”, no explicit deadline is set for the payment of taxes. We may assume that purchaser is required to pay the taxes before they become past due, but there is no expressed provision to that effect.

Consequently, monitoring and enforcement of this provision is somewhat difficult for the seller. Before sending a formal demand letter, he must first confirm with the county treasurer that the taxes have not been paid. He should do this only after the taxes have become delinquent. (The first one-half of the annual taxes are due November 10, and are considered to be delinquent after December 10; the second half are due April 10 of the following year and are considered to be delinquent after May 10. Penalties and interest are assessed if taxes are not paid by the delinquency date.) Then, with positive knowledge that the taxes are delinquent, he may either:

- mail a formal demand letter to the purchaser, requiring that the taxes be paid within the time provided in paragraph 5(c) of the contract; or
- pay the taxes, provide a copy of the paid tax receipt to the escrow agent, request the escrow agent to add the amount paid to the unpaid balance of the contract, and notify the purchaser of these actions; or
- pay the taxes, and immediately mail a letter to the purchaser requesting reimbursement. If the purchaser fails or refuses to comply with this letter, then a formal demand letter can be mailed as provided by paragraph 5(a).

The seller cannot rely upon a written demand to the purchaser to produce proof of payment of taxes. If the purchaser pays the taxes, but fails to notify the seller that he has done so, and fails to respond to a written demand for proof of payment of taxes, he nevertheless is not in default. Thus, the seller may incur attorney fees for preparation and mailing of a demand letter which is not enforceable, and he may not be able to recover his attorney

fees!

Most sellers and their attorneys do not bother to mail a preliminary request for reimbursement of taxes advanced by seller, and I have never seen a purchaser's attorney argue that it is required. However, there is some merit to the argument that, if the purchaser has not been notified that the seller has paid the taxes, and has not been asked to reimburse the seller, he has not "failed or refused" to repay those sums.

Drafting suggestion: The last sentence in paragraph 3(b) should be modified as follows:

- *Purchaser will pay the taxes, and mail or deliver copies of the paid tax receipts each year to Seller, on or before the dates the taxes become due and payable.*

This provision sets a deadline for performance, and also removes any necessity for the seller to request production of the paid tax receipts.

You might also consider adding this clause to paragraph 5(a):

- *...,or fails to mail or deliver copies of the paid tax receipts to Seller on or before the dates the taxes become due and payable, the Seller may...*

This clause declares the failure to produce the paid tax receipts to be an event of default. While you could never hope to make a forfeiture stand on this basis, you would at least have grounds for demanding attorney's fees for the mailing of the demand letter (even if the purchaser had actually paid the taxes), because production of the paid tax receipts would now be an act for which demand can be made.

...under form 103

The purchaser's obligations with respect to payment of taxes are the same under both standard contract forms, except that the purchaser is not required to produce paid tax receipts under form 103. As noted above, while the RANM form does contain this requirement, there are no stated consequences for purchaser's failure to comply. The seller's remedies for purchaser's failure to pay the taxes or to reimburse the seller for taxes advanced, are the same under both forms of contract, except that sums advanced by seller under form 103 bear interest at eight percent (8.00%); under the RANM form they bear interest at the same rate as the seller's equity balance in paragraph 2 of the contract.

...under a mortgage or deed of trust

New Mexico has statutory forms of mortgages and deeds of trust. Both are upon the "statutory mortgage condition", which is defined and incorporated into the instrument by

section 47-1-41 NMSA 1978 (see chapter 10). The statute states the requirement for the mortgagor (purchaser) to pay taxes as follows:

- “Mortgagor shall pay when due and payable all taxes, charges and assessments to whomsoever and whenever laid or assessed upon the mortgaged premises or on any interest therein;”.

If the mortgagor fails to pay the taxes when they become due, the mortgagee may, at his option, pay the taxes, and the amount so paid “*shall be payable by the mortgagor on demand and shall be so much additional indebtedness secured by the mortgage*”. If the purchaser fails to pay the taxes, or fails to reimburse the mortgagee upon demand for taxes advanced by mortgagee, the mortgagee may, at his option, foreclose the mortgage.

As a practical matter, due to the substantial costs involved in conducting a foreclosure suit, the mortgagee’s remedy is effectively limited to paying the taxes himself, and adding the amount advanced to the unpaid mortgage note balance, where it will bear interest until paid. Unless the mortgagor is also in default for non-payment of principal and interest, it may not be worth the mortgagee’s trouble and expense to pursue foreclosure merely for non-payment of taxes.

Drafting suggestion: There is no statutory requirement for the mortgagor to assess the property in his own name, or to provide paid tax receipts to the mortgagee. If either provision is desired by the mortgagee, then it must be added to the terms and conditions of the mortgage or deed of trust instrument, and the mortgagee’s remedy for non-compliance by the mortgagor must also be added to the document.

Tax Sales

If the purchaser/mortgagor fails to pay the taxes, it is imperative that the seller/mortgagee be aware of the failure, and take appropriate measures to get the taxes paid. Failure to do so can result in permanent loss of title to the property. The property can be sold at public auction by the State of New Mexico three years after the taxes first become delinquent. *Sect. 7-38-67 NMSA 1978*. The effect of a tax sale deed has been held by the Court to convey all the interests of the purchaser and the seller in the property to the purchaser at the tax sale. (See *Connelly* and *Southwest Land Investment, Inc.* cases, p. 10 CLA)

Paying Taxes through the Escrow Agent

If taxes are not being collected and paid by a senior lien holder, the seller can eliminate virtually all his enforcement problems by including in the REC, mortgage or deed of trust a requirement that the purchaser pay a portion of the taxes each month to the escrow agent, and by directing the escrow agent to pay the taxes when they become due. Escrow agents

typically charge one or two dollars per month for receiving the monthly tax payments, either alone or with insurance premiums, and a nominal disbursement fee when the taxes are paid.

Drafting suggestion: A typical “tax and insurance” clause, when added to the second paragraph of the RANM contract, might look like this:

- In addition to the payments of principal and interest, purchaser shall pay to the escrow agent each month with such payments, an amount equal to one-twelfth (1/12) of the annual requirement for property taxes (and insurance), presently in the amount of \$____ (for taxes, and \$____ for insurance premiums), which amount shall be held by the escrow agent and used to pay taxes (and hazard insurance premiums) as they become due. The escrow agent may adjust the monthly required payment for taxes (and insurance premiums) from time to time as it deems necessary, and the purchaser shall pay the adjusted amounts.

Paying Taxes through a Senior Lien Holder

When the REC, mortgage or deed of trust between purchaser and seller is subject to a senior mortgage, deed of trust or REC which is being either assumed or wrapped by the junior instrument, and the senior instrument requires that taxes and/or insurance be collected and paid by the servicer of the senior instrument, then there is no discretion as to how the purchaser will pay the taxes. He must pay them to the escrow agent, who must remit them to the servicer of the senior obligation.

Drafting suggestion: When the senior obligation is being assumed by the purchaser, the fact that the senior assumed payment includes taxes and insurance premiums should be recited in paragraph 2 of the RANM contract, more or less as follows:

- \$60,000.00 by payment of the mortgage herein described, in monthly installments of \$800.00 (which amount presently includes \$200.00 for taxes and insurance and \$600.00 for principal and interest) or more, commencing December 1, 1997 and monthly thereafter until paid in full. Purchaser shall pay any increase in the monthly payment as may be required for taxes and insurance by ABC Mortgage Company or its successor;

When the senior instrument is being wrapped by the junior instrument, a tax and insurance clause must be added to the junior instrument, and should look something like this:

- In addition to the payments of principal and interest, purchaser shall pay to the escrow agent each month with such payments, an amount for the payment of taxes (presently \$80.00 per month) and hazard insurance premiums (presently \$120.00 per month), which will be remitted by the escrow agent to the ABC Mortgage Company, or its successor. Purchaser shall pay any increases in the monthly payment for taxes and hazard insurance premiums as may be required by ABC Mortgage Company or its successor.

In either case, the escrow instructions in paragraph 9 of the RANM REC form should instruct the escrow agent to disburse from each monthly payment, the full required PITI

(Principal, Interest, Taxes and Insurance) payment amount to the senior mortgage servicer or escrow agent.

Hazard Insurance

Whether a standard form REC is used, or a mortgage or deed of trust is used as the seller financing instrument, the purchaser is required to maintain hazard insurance for the insurable improvements on the property. The specific type of insurance coverage to be maintained is not uniform between the various financing instruments, and the type of insurance policy (or policies) to be maintained for the protection of a senior mortgagee is a problem requiring special attention. The seller's remedies for non-performance of the purchaser are different under each type of financing instrument. By statute, a mortgagor in New Mexico can require that fire loss insurance proceeds be used to rebuild, provided no applicable federal law or regulation requires otherwise.

Risk Coverage Requirements

...under the RANM and 103 REC forms.

Risks covered

Both forms require the purchaser to obtain insurance "...against the hazards covered by fire and extended coverage insurance". The meaning of "extended coverage" varies from insurance policy to insurance policy, however. Most insurance companies offer more than one form of "extended coverage", with different premiums. Nearly all policies cover the risks of lightning, riot, explosion, vehicular-caused damage, collapse, smoke, aircraft, wind and hail. Some also cover vandalism and "malicious mischief", but others offer these coverages as options with an added premium. In every case, coverage against earthquake and flood damage is offered only on a separate policy, and with a separate premium.

If the seller wants the property to be insured against vandalism, malicious mischief, earthquake or flood damage, then an appropriate risk coverage clause should be drafted and added to the purchase agreement or to the real estate contract addendum thereto, so that the clause will be incorporated into the insurance paragraph in the form REC. Otherwise, the coverage actually obtained by the purchaser might not include the desired risk, yet be in full compliance with the terms of the REC.

Property covered

The RANM form requires the purchaser to keep the “insurable improvements” insured; the form 103 requires insurance for any “buildings” on the property. This may be a significant difference. The RANM form would appear to require coverage for such things as fences, block walls, signs and water wells, while form 103 would not require coverage, because they are not “buildings”. Some of these items may be covered as “appurtenant structures” in a standard insurance policy. To the extent they are not covered, and depending on the type of policy purchased, a purchaser default may exist under the RANM form that would not exist under form 103.

If the property being sold consists of more than land and buildings, for hazard insurance purposes the seller should either require that the RANM form be used, or specify in the contract which improvements are required to be insured. If there is any doubt as to whether a particular improvement would be covered by a standard policy, a qualified insurance agent should be consulted before the purchase agreement is signed, so that a specific insurance clause can be drafted and included in the purchase agreement.

...under a statutory mortgage or deed of trust

The “statutory mortgage condition” in section 47-1-41 NMSA 1978 describes the insurance obligation of the mortgagor:

- Mortgagor shall keep the *buildings* on the mortgaged premises insured in the *sum specified* and against the *hazards specified* in the mortgage for the benefit of the mortgagee (emphasis added)....The insurance shall be in such form and in such insurance companies as the mortgagee shall approve. Mortgagor shall deliver the policy or policies to the mortgagee and at least two days prior to the expiration of any policy on the premises shall deliver to mortgagee a new and sufficient policy to take the place of the one so expiring.

Property required to be insured is the same as required by the form 103 REC. The statutory “short forms” of mortgage and deed of trust contain blanks for the insertion of the dollar amount of insurance required and the risks to be insured against.

...where hazard insurance is required/maintained by a senior mortgage holder

Before the seller entered into a seller-financed sales agreement, his position vis-à-vis hazard insurance was relatively simple: he obtained a homeowner’s policy in the type and amount required by his mortgagee, and named the mortgagee in the policy as a “loss payee”. The insurance company rated the property risk under the category, “owner-occupied residence”.

But now when the seller gives up possession of the property to his contract purchaser, the risk status of the property changes to “non owner-occupied dwelling”, which normally requires a greater insurance premium. The seller is still required by the terms of his mortgage to maintain insurance on the property for the benefit of the mortgagee. He may

be required to obtain a new type of policy, and to notify the mortgagee that the property has been sold and that he no longer occupies the property.

The REC (or mortgage or deed of trust) between the seller and the purchaser requires the purchaser to maintain hazard insurance for the benefit of the seller. The purchaser can satisfy this requirement by obtaining a homeowner's policy, and naming the seller in the policy as a "loss payee". He could also be required by the financing instrument to name the holder of the first mortgage as a loss payee under his policy, and increase the insurance amount to a figure large enough to cover the mortgagee's interest

Enforcement

...under the RANM or 103 forms

Generally, the seller's remedies for purchaser's failure to keep the property insured are the same as for purchaser's failure to pay taxes, and are the same for both standard forms, with one major exception: paragraph 8 of form 103 fails to include payment of insurance premiums in its enumeration of those things for which the seller can demand direct performance by the purchaser. *The result is that a seller can himself insure the property under the provisions of paragraph 7 and base a forfeiture upon a demand letter requiring reimbursement of the premiums advanced, but he cannot base a forfeiture upon a demand letter which requires the purchaser to obtain and pay for insurance.*

Such was the holding in the 1985 case of *Boatwright v. Howard*, where the Court was dealing with an insurance requirement clause essentially identical to the form 103 clause. Because the contract did not explicitly state that the contract could be terminated for failure to maintain hazard insurance, and because hazard insurance was not a "charge against the real estate", the seller was limited to paying the insurance premiums and then seeking reimbursement or filing suit to enforce the insurance requirement. See p. 14, CLA.

Drafting suggestion: This one is easy. If you insist on using form 103, be sure to add "*or fail or refuse to keep the buildings insured as required by paragraph 4*" to the middle of paragraph 8.

...under a statutory mortgage or deed of trust

Enforcement provisions under the "statutory mortgage condition" are the same as for failure of the purchaser to pay taxes.

Insurance Proceeds

When a loss occurs to an insured property, what happens to the insurance proceeds? Can the seller under an REC or mortgage/deed of trust insist that the funds be used to pay off the balance? Some “long-form” mortgages do contain clauses that require insurance proceeds be applied to pay off the balance owed to the mortgagee.

An answer, at least as to mortgages and deeds of trust, is provided by Section 48-7-10 NMSA 1978 Comp:

MORTGAGES; INSURANCE PROCEEDS

Where there is a mortgage of a single family residence securing a loan and where there are no federal regulations to the contrary, the mortgagor may require the proceeds of any insurance policy, which are payable by reason of damage to or destruction of the mortgaged property and which would otherwise be payable to the mortgagee, to be held jointly by the mortgagor and the mortgagee in an escrow account and to be applied toward the repair or replacement of the damaged property. Provided that it shall first be reasonably established to the satisfaction of the mortgagee that such repairs or replacement will restore the mortgaged property to a value at least equal to the balance remaining on the obligation, at the time the damage or destruction occurred, secured by the mortgage.

The Court has held that “...*the deed of trust is, in essence, a mortgage and should be enforced as a mortgage*”. (See *Kuntsman*, p 29 CLA) It is readily apparent that the section would apply to both mortgages and deeds of trust used in seller-financed transactions.

But what about REC’s? The Court held in the *Bishop* case (p. 47 CLA) that a real estate contract will not be construed to be an equitable mortgage. It most certainly cannot be a legal mortgage, because the purchaser does not hold fee simple title. It would seem, therefore, that this particular statute would not apply to a REC, and that the parties are free to contract as they wish regarding this question.

The parties to a mortgage or deed of trust could agree that, notwithstanding the statute, insurance proceeds will be applied to reduce the balance remaining on the obligation. A right conferred by statute, like almost any other right, can be waived. However, if there is no express provision requiring that the proceeds be applied to the debt, then the mortgagor would have the option under the statute to require that the proceeds be used to rebuild.

7

RESTRAINTS on ALIENATION

In its broadest sense, a 'restraint on alienation' is a provision in a mortgage or REC that inhibits the ability of the mortgagor/buyer to sell, mortgage or encumber the property. Restraints fall into two general types:

1. Forfeiture restraints, which provide that alienation by the buyer will cause a forfeiture of his interest; and
2. Disabling restraints, which prohibit alienation by the buyer, and either impose punitive consequences for an unconsented transfer or discourage refinancing of the debt. There are two major types of disabling restraints:
 - a. 'due-on-sale' clauses, which give the seller/mortgagee the option to accelerate the entire unpaid balance of the REC or mortgage when the buyer/mortgagor sells or encumbers the property without first obtaining written consent from the seller/mortgagee; and
 - b. prepayment penalty clauses and prohibitions against prepayment, which effectively prevent refinancing of the debt during periods of declining interest rates, thereby impairing the marketability of the property.

Many REC's and mortgages contain provisions which directly or indirectly restrain alienation of the property. This chapter reviews the legislative and judicial history of these provisions, within the context of the form 103 REC, the RANM REC form, FHA mortgages and mortgages used in seller-financed transactions.

Form 103 Prohibition against Assignment

This form (Form No. 1 in the Forms Appendix) contains the following "Paragraph 11":

- "11. It is further understood and agreed that no assignment of this contract shall be valid unless the same be endorsed hereon and countersigned by the Owner."

This clause is a disabling restraint that has in the past effectively discouraged use of the assignment as a vehicle for transferring the buyer's interest in a form 103 REC. Various devices have been used to circumvent the prohibition. Most common among these is the resale on a junior REC, either wrapping or assuming the REC. (Paragraph 11 does not expressly prohibit a resale of the property; it merely prohibits an "assignment of this contract.")

In 1956, the Supreme Court held that a lessee who sub-leased a portion of the premises for a shorter period than the term of the original lease did not violate a provision in the lease against assigning and transferring the lease. See *DeBaca*, p. 15, CLA. The Court distinguished the legal effect of an assignment from a sub-lease, noting that an assignment does not violate a prohibition against subleasing, and that a sub-lease does not violate a prohibition against assignment.

In 1985, the Supreme Court applied similar reasoning to a sale by holding that a resale of the property by means of a junior REC, wherein the sub-purchaser assumed and agreed to pay the senior REC, does not constitute an 'assignment', and therefore does not violate the prohibitory clause. See *Paperchase*, p. 17, CLA. The *Paperchase* case did not decide the validity of the clause; it merely concluded that the clause was not violated under the facts of the case.

In 1988, the Supreme Court held an essentially equivalent prohibition contained in an agreement and deed to be an unreasonable restraint on alienation, and reformed the deed to grant a fee simple title to the grantee. See *Gartley*, p. 18, CLA. The Court announced five tests that it would apply when determining whether a restraint on alienation is reasonable, and decided that the restriction under consideration was unreasonable, because it failed two of the five tests.

The *Gartley* decision effectively invalidated the form 103 prohibition, because it fails the same two tests that were failed by the *Gartley* prohibition: (1) it is not limited in duration, and (2) it is not limited as to the number of persons to whom transfer is prohibited.

The form 103 prohibition is a disabling restraint on alienation because it purports to nullify the offending assignment. An unauthorized assignment is not one of the acts specified by Paragraph 8 of Form 103 that enables the owner to accelerate the unpaid balance. Consequently, it cannot be regarded as a 'due-on-sale' clause.

Drafting suggestion. Thanks to *Gartley*, we can safely pronounce the paragraph 11-prohibition clause to be dead. If you *must* use form 103, then paragraph 11 should either be deleted in its entirety, or replaced by an enforceable 'due-on-sale' clause.

Due-on-Sale Clauses

A due-on-sale clause is a provision contained in a mortgage, deed of trust or real estate contract that allows the mortgagee or seller to accelerate the unpaid balance upon a sale or other voluntary disposition of the property by the mortgagor or buyer. Such clauses were included in the pre-printed "boilerplate" provisions of mortgages for many years. In the 1970's, mortgage lenders, having become trapped between low income from fixed-rate

mortgage loans and the need to pay high interest rates for deposits, began to exercise their acceleration rights. Payment of the balance due would be waived only if the mortgagor's buyer agreed to renegotiate the mortgage terms to include a higher rate of interest and a greater monthly payment.

Legislative & Judicial History

Considerable disorder resulted in the real estate marketplace. Due-on-sale clauses became the subject of a national tug-of-war between state legislatures, Congress and state courts. What follows is a brief history of the battle as it developed in New Mexico.

- March 15, 1979. The New Mexico Legislature enacted a statute declaring that due-on-sale clauses allowing escalation of the interest rate upon sale 'may constitute an unreasonable restraint upon alienation to the detriment of the public welfare.' The statute declared such clauses to be unenforceable 'unless the security interest is substantially impaired.' (Enacted as sections 48-7-11 and 48-7-12, NMSA 1978, these sections were later repealed in 1983. See below.) By its terms, the statute was applicable to 'clauses in mortgages and deeds of trust by way of mortgage of real estate on residential property consisting of not more than four housing units...'. Thus, the statute did not appear to cover real estate contracts, nor did it apply to multiple housing units exceeding four units, vacant land, or non-residential property.
- November 12, 1981. The Supreme Court held that '*based upon common law principles*, due-on-sale clauses which either permit acceleration of payment or increased interest rates upon transfer of property or assumption of mortgages without a showing of substantial impairment to the lender's security interest are unenforceable as unreasonable restraints upon alienation.' (emphasis added) See *Bingaman*, p. 15, CLA. The *Bingaman* decision was significant for REC'S, even though the Court was dealing with a statute which did not apply to REC'S. Because the holding was based on the common law, rather than an interpretation of the statute, it had apparent application to *any* due-on-sale clause, regardless of the type of instrument in which it appeared.
- October 15, 1982. Congress enacted Public Law No. 97-320, known as the 'Garn-St. Germain Depository Institutions Act of 1982'. The Act applied to HUD-insured loans, including those made by federally chartered banks, federal savings banks, federally chartered savings and loan associations, and federal credit unions. The portion of the Act relating to due-on-sale clauses appears in the United States Code (USC) as Title 12, section 1701j-3. This section of the Act includes these major provisions:
 - Lenders are authorized to 'enter into or enforce a contract containing a due-on-sale clause with respect to a real property loan, ...notwithstanding any provision of the constitution or laws (including the judicial decisions) of any state to the contrary...'

- The Act is applicable to contracts entered into after October 15, 1982. However, for loans

made or assumed before October 16, 1982 and after state enactment of a law prohibiting due-on-sale clauses (in New Mexico, March 15, 1979), the law applies only to transfers which occur after October 15, 1985 unless a state enacts legislation prior to October 15, 1985 to regulate loans made during the interval, in which case the state law governs such contracts. Loans made during the period between March 17, 1979 and October 16, 1982 thus became known as 'window period loans'.

- The Act does not permit exercise of a due-on-sale clause where the transfer by the borrower is of any of the following types:

1. The creation of a lien or other encumbrance subordinate to the lender's security instrument that does not relate to a transfer of rights of occupancy in the property;
2. The creation of a purchase money security for household appliances;
3. A transfer by will, inheritance, or operation of law on the death of a joint tenant or tenant by the entirety;
4. The granting of a leasehold interest of three years or less not containing an option to purchase (but query as to a renewal option);
5. A transfer to a relative resulting from the death of a borrower;
6. A transfer where the spouse or children of the borrower become an owner of the property;
7. A transfer resulting from a decree of a dissolution of marriage, legal separation agreement, or from an incidental property settlement agreement, by which the spouse of the borrower becomes owner of the property;
8. A transfer into an intervivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property; and
9. Any other transfer or disposition described in regulations prescribed by the Federal Home Loan Bank Board.

- The Act includes residential manufactured homes in its definition of "real property," when such homes are used as a residence.

- The Act does not cover clauses that allow the lender to raise the interest rate upon a transfer by the borrower without obtaining prior written consent of the lender. Therefore, in New Mexico, the *Bingaman* decision remained applicable to such clauses, with the result that such clauses would not be enforceable.

- April 7, 1983. The New Mexico Legislature repealed sections 48-7-11 through 48-7-14, and enacted new sections 48-7-15 through 48-7-24 NMSA 1978. The purpose of

these actions was to accommodate the *Garn* Act, and to provide for regulation of the exercise of due-on-sale clauses contained in 'window-period' loans, as permitted by *Garn*. Window-period loans will thus be permanently subject to the state law and exempted from *Garn*. Section 48-7-19 prohibits enforcement of due on sale and prepayment penalty clauses. An increase of the interest rate upon an assumption of the loan is permitted, provided that the rate increase is limited to two percentage points above the contract rate. Also, the increased rate cannot exceed one percentage point above the most recent Federal National Mortgage Association (FNMA) auction rate of interest at which bids were made. Section 48-7-20 prohibits exercise by a lender of all its due-on-sale options upon transfers of any of the types expressly exempted under *Garn*. A fee to transfer the loan is allowed, but not to exceed one percentage point of the unpaid principal balance at the time of the transfer.

Comment: This legislation was explicitly directed at state-chartered savings and loan associations. The 'purpose' clause clearly indicates that the legislation was intended to apply to commercial lenders, rather than owner-financed real estate sales. Nonetheless, the Act's definitions of 'due-on-sale clause', 'lender' and 'real property loan' are sufficiently broad to encompass such transactions. We must therefore assume, until established otherwise that the Supreme Court will hold the Act to be applicable to real estate contracts between a seller and buyer of real property.

- January 4, 1983. The Supreme Court held that a due-on-sale clause contained in a security agreement securing the sale of personal property located in a motel, is enforceable notwithstanding section 55-9-311 of the New Mexico Uniform Commercial Code, which permits transfer of a debtor's rights in collateral 'notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default'. The Court held that because the common law was displaced by the U.C.C. as adopted in New Mexico (as to personal property), the U.C.C., rather than the common law, governed the due-on-sale clause contained in the security agreement. See *Brummond*, p. 16, CLA.

----- The Court also upheld a due-on-sale clause contained in the commercial mortgage on the underlying real estate. It followed its previous ruling in *Foreman* that such a clause did not constitute an unreasonable restraint of alienation at common law. *Id.*

- May 2, 1985. The Supreme Court held that a state-chartered savings & loan association which converts to a federally chartered association during the window period, may not exercise due-on-sale clauses contained in its mortgages made or assumed before its conversion, but within the window period. Where the mortgages are made or assumed after the conversion to a federal association, and within the window period, the clause may be exercised. See *Bardacke*, p. 19, CLA.

Current Status in New Mexico

It should be apparent from the foregoing discussion that the current standing of due-on-sale clauses in New Mexico is not a simple matter. The enforceability of any such clause depends upon the governing law, which is determined by the date of the loan agreement. It also depends upon whether the clause provides for acceleration of the unpaid balance, or merely allows an escalation of the interest rate. Figure 5 summarizes the present situation.

FIGURE 5

Date of Loan	Governing Law	Acceleration of Balance	Escalation of Interest Rate
Before 03/15/79	Bingaman v. Valley (applying Common Law)	Not permitted, unless security interest is substantially impaired.	Not permitted, unless security interest is substantially impaired.
After 03/15/79 and before 10/16/82 ("Window Period")	48-7-15 to 48-7-24 NMSA (1983 Cum. Supp.)	Not permitted	Permitted, but limited in amount – with 9 exceptions
After 10/15/82	P.L. 97-320 (<i>Garn</i>)	Permitted, with 9 exceptions	Not covered by act-state policy favors

Consent Requirements

The requirements for seller's written consent contained in due-on-sale clauses are of two general types:

1. the seller is under no obligation to give consent (as in the existing RANM form), and
2. the seller shall not unreasonably withhold consent (as in the proposed RANM form).

New Mexico decisions upholding the due-on-sale clause in REC's have all dealt with clauses of the first type. How will the Court limit the seller's right of acceleration when the clause requires the seller to have a reasonable basis for withholding consent?

Where the buyer does not seek consent prior to a sale, it is reasonable to assume that the seller's right to accelerate will be upheld, because the failure to seek consent is defined in

the agreement as an event of default. The seller must be given the opportunity to assert any reasonable objections to the sale.

Where the buyer seeks consent prior to the sale, it would appear that the seller has an obligation to act reasonably in withholding consent, else the language would be meaningless.

The Supreme Court has ruled on the 'reasonable consent' clause in three commercial lease cases.

- In 1982, the Court held that a lessor acted unreasonably when he withheld consent to a sub-lease on the ground that the proposed sub-lessee was financially unstable, then rented to the same rejected party within a week after the lessee abandoned the property. See *Cowan*, p. 20, CLA.
- In 1982, the Court imposed a duty on the lessor to act reasonably when withholding consent to a sub-lease, even where the language of the lease was of the 'no obligation to consent' type. See *Boss Barbara, Inc.*, p. 20, CLA. The Court said that the lessor could not arbitrarily withhold consent. This case can probably be distinguished from the REC cases involving "no obligation to consent" clauses because the Court has said that due-on-sale provisions do not unreasonably restrain alienation, whereas refusal to consent to a sub-lease broadly prohibits the lessee from transferring the leasehold interest.
- In 1991, the Court held that a lessor of an automobile dealer's lot acted unreasonably in withholding consent to a proposed sublease where the lessor's primary motivation was to share in the increased economic benefit from the lease. See *Economy Rentals, Inc.*, p. 21, CLA. The lease contained a requirement that consent would not be unreasonably withheld. The Court reasoned that the lessor could reasonably have withheld consent when the proposed sublease would injure or impair the lessor's interest in the leased property, but not when the lessor attempts to secure a benefit not bargained for in the original lease.

The Court's reasoning in *Economy Rentals, Inc.* would appear to be applicable to seller-financed real property sales, whether in the form of a REC or mortgage, because the seller has a security interest in the property to the extent of the unpaid debt. However, it may be difficult for a seller to show that the proposed sale would impair or diminish the value of the seller's security interest, especially since the original buyer remains liable to the seller for the debt. When the debt-to-value ratio is small, either because the value of the property has increased since the date of the original sale, or because the original buyer has significantly reduced the principal indebtedness, the Court may well be skeptical of the seller's motives for withholding consent.

Language requiring the seller to act reasonably in withholding consent can be expected to significantly limit the seller's right to exercise the due-on-sale clause to those situations where some combination of the following facts exist:

- The existing debt-to-value ratio is very high (e.g., no down payment);
- The seller relied heavily on the original buyer's strong financial status;
- The proposed buyer is financially weak in comparison to the original buyer;
- There is a substantial remaining term on the existing contract;
- The original buyer is planning to leave the state, thereby weakening the seller's ability to pursue collection of the debt;
- Any other demonstrable facts tending to diminish the value of the seller's security interest.

Prepayment Penalties and Prohibitions

Provisions in mortgages or REC's that penalize or prohibit prepayment of the loan balance are considered to be restraints against alienation because they effectively discourage refinancing during periods of falling interest rates, and therefore impair marketability of the property. The New Mexico Legislature and the Supreme Court have a long history of barring prepayment penalty clauses in pursuance of a stated public policy favoring free alienability of real property. The *Garn* Act has preempted the State's policy with regard to loans by federally chartered banks, savings and loan associations and credit unions. The Legislature and the Supreme Court have both acted to preserve state policy as to 'window period' loans and other transactions not preempted by *Garn*. This section reviews the history of state and federal legislation and court decisions leading to the present status of prepayment penalty and prohibition clauses in New Mexico.

1980. The Legislature enacted the Residential Home Loan Act as sections 56-8-22 through 56-8-30 NMSA 1978. The Act imposed civil penalties for charging or receiving interest rates greater than those allowed by the Act, and declared prepayment penalty clauses in mortgages and REC's to be unenforceable. The Act applied to dwellings and the underlying real property designed for occupancy by one to four families, and included mobile homes & condominiums.

1981. The Legislature repealed sections 56-8-25 through 56-8-28 of the Act, relating to interest rates. The remaining sections are still in effect.

1982. Congress enacted the *Garn-St. Germain Depository Institutions Act*. See discussion in the due-on-sale section, above.

1983. The Legislature enacted sections 48-7-15 through 48-7-24 NMSA 1978. Section 48-7-19 prohibited the exercise of due-on-sale clauses and limited transfer fees and interest

rate increases upon assumption of 'window period' real property loans, and further declared "There shall be no enforcement of a prepayment penalty in said mortgages."

1985. The Supreme Court held that a provision contained in a REC prohibiting prepayments constituted a penalty within the meaning of the Residential Home Loan Act, and therefore was unenforceable. See *Naumburg*, p. 22, CLA. The Court held that a log cabin vacation home, notwithstanding its location in a commercial area, satisfied the statutory definition of 'residence'.

1990. The Supreme Court held that the statutory prohibition in section 48-7-19 NMSA 1978 against enforcement of prepayment penalty clauses in 'window-period' loans applies whether or not there has been a sale, and whether or not the lender is exercising an option under the due-on sale clause. See *Los Quatros*, p. 23, CLA. Also, the prohibition applies to real property bans as defined in the Act, not just to loans secured by residential real estate consisting of not more than four housing units. *Garn* does not preclude the State from enlarging the class of loans to which the window-period exemption from *Garn* applies.

8

ASSIGNMENTS

Contract sellers frequently sell their right to receive contract payments to investors, either by selling their entire interest in the contract, or by selling a 'stream of payments' from the contract. Buyers who sell the property, and are 'cashed out' of their equity in the property, may convey their rights in the property and assign their interest in the REC to the new buyer. Sellers and buyers can also use their respective interests in the contract and property as security for loans. This chapter discusses the documentation that is necessary to complete these transactions.

Sales of Seller's Interest in REC

The seller has two important assets that are of interest to investors.

1. He has the right to receive principal and interest payments until the principal balance is paid in full. An investor may purchase all or a portion of this right at a discount. The size of the discount determines the yield, or return on the purchase price.
2. He has legal title and the right to recover equitable title and possession of the property if the buyer defaults. This right is security for the debt owed by the buyer. If the buyer defaults, the seller gets the property back. Any payments made prior to default are deemed to be liquidated damages (RANM form) or rent (form 103) for use of the property, and are forfeited by the buyer. Thus, if the property appreciates in value, the seller gets a "windfall" gain. The amount of the gain would be the market value of the property at time of default less the REC purchase price.

Therefore, the completion of a sale of the seller's rights in the REC requires two steps: assignment of the contract rights and conveyance of title to the property. These steps are usually executed in two separate documents, although they can be combined in a single document. Although not mandatory, the investor should sign a special warranty deed conveying title to the buyer. The unrecorded deed is placed in escrow for delivery to the buyer when the REC is finally paid off.

Assignment of Contract Rights

An Assignment is the correct instrument to use for the transfer of the seller's right to receive payments. This document transfers all of the seller's rights in the REC to the investor. It recites the consideration for the transfer (the amount paid by investor to seller), contains words legally effective to accomplish the transfer, and describes the REC and the property with sufficient clarity to enable the document to be recorded. It should also contain the investor's mailing address. See no. 6, Forms Appendix. The form is signed by the seller, acknowledged and recorded in the office of the county clerk of the county where the property is located. (Note: The seller is described in this document as "Assignor" and the investor is described as "Assignee.")

A copy of the recorded assignment is promptly given to the escrow agent, along with any instruction which the assignee wishes to include regarding how his future payments are to be disbursed by the escrow agent (e.g., bank name and address, savings or checking account number). Also, if not included on the assignment, the assignee must provide his current mailing address to the escrow agent. Finally, it is very desirable for the assignee to send a notice of the assignment to the REC buyer, including a copy of the recorded assignment.

Acceptance of Assignment

It is good practice to require the assignee to execute a document by which he expressly accepts the assignment of seller's rights and agrees to deliver a warranty deed to the buyer upon payment in full of the REC. The assignee signs the form, and his signature is acknowledged. See no. 6 in the Forms Appendix. The lack of a written acceptance of assignment does not destroy the legal effectiveness of the document, however, because acceptance is presumed as a matter of law.

Conveyance of Title

It is essential for the seller to convey legal title to the property to the investor, so that if the buyer defaults on the REC, recordation of the special warranty deed from escrow will pass equitable title through the seller to the investor. To do this, the seller must execute a warranty deed or special warranty deed to the investor. A quitclaim deed is not sufficient, because it does not convey after-acquired title. See the discussion of this issue at page 71. The deed is signed, acknowledged and promptly recorded in the county clerk's office in the county where the land is located. A copy of the recorded deed is given to the escrow agent for informational purposes. See no. 6 in the Forms Appendix. The legal description typed on the deed is the same as the legal description contained on the warranty deed from the seller to the buyer. A 'Subject to' clause like the one shown below should be added, which

makes it clear that the existing REC is excepted from the warranty covenants.

- ... Subject to a certain real estate contract dated _____ wherein Grantor is named as seller and _____ is named as purchaser, recorded in Book _____, Pages _____, as document number _____ of the records of the Clerk of _____ County, New Mexico on _____ (date) _____.

Combined Assignment and Conveyance of Title

It is possible to combine in one document the assignment of seller's contract rights, acceptance of assignment by assignee and conveyance of legal title, subject to the contract, from the seller to the investor. See no. 7 in the Forms Appendix. The advantages of this form are that it saves recording fees and is simpler to use.

Assignee-to-Purchaser Conveyance (the "performance deed")

It is preferred practice for the investor to sign a special warranty deed or warranty deed, conveying legal title to the REC buyer. The deed is placed in escrow, unrecorded, for later delivery to the buyer when the REC is paid in full. This practice creates a complete chain of legal title running from the seller through the investor to the buyer. A quitclaim deed should not be used for this purpose, because it does not convey after-acquired title. See discussion at page 71. If the REC is junior to another REC on the same property and the junior REC is paid off first, then there will be an 'after-acquired' title passing from the seller in the senior REC through the intermediate parties to the junior REC buyer.

A 'performance deed' is not absolutely essential to complete the REC buyer's title. Most title company underwriters will accept the original seller's warranty deed delivered out of escrow, in lieu of a deed from the investor, even though there may be a warranty deed of record conveying legal title from the seller to the investor! The rationale is that the delivery of the deed from escrow 'relates back' to the delivery of that deed *into* escrow, thereby giving it priority over the deed subsequently executed and delivered by the seller to the investor. See discussion at page 85.

The 'relation back' doctrine is critical to the effectiveness of escrows generally. The rule is that, once the deed is delivered into escrow, there is nothing the seller can do to defeat or encumber the buyer's title resulting from a later delivery of the deed out of escrow. Not even the intervening death of the seller will invalidate the subsequent delivery of his deed from escrow. As the discussion below of buyer's assignments indicates, the same is true of the delivery from escrow of the buyer's special warranty deed to the seller.

‘Fractional’ Sales of Seller’s Interest in REC

An increasingly popular practice is to sell a segment (the term ‘fractional’ is not an accurate description of the product) of the seller’s future payment stream from the REC. For example, if the REC has an unpaid principal balance of \$50,000, the seller might assign a number of payments representing \$5,000 of that balance, and the interest thereon. For the right to receive those payments, the investor pays the seller an amount calculated to generate a target yield. When the investor has received the specified amount, the REC is assigned back to the seller. A re-assignment document is executed and placed in escrow for that purpose. See no. 8-9, Forms Appendix.

The assignment document transfers all the contract rights of the seller to the investor, including rights of enforcement upon buyer’s default. This avoids the creation of fractional ownership interests in the REC, which may require a state securities registration. For the protection of the seller’s reversionary interest in the unpaid balance, the agreement normally provides that the investor must give the seller notice of the buyer’s default and an opportunity to repurchase the investor’s interest in the contract, before the investor may exercise the election of remedies set forth in the REC.

Collateral Assignments of Seller's Interest in REC

The seller may use his right to receive future payments as collateral for a bank loan. For an example of a collateral assignment, see no. 11, Forms Appendix. The collateral assignment is perfected by filing it in the county clerk's office in the county where the property is located. Even though the seller's interest in the contract proceeds is personal property, it is not necessary to file a financing statement in the office of the Secretary of State. See *In Re Anthony*, p. 25, CLA.

A mortgage given on the property by the seller does not give the lender a security interest in the payments that will prevail against a subsequent assignee of the payments. The Supreme Court has held that where a seller gave a mortgage on the property to his lender, but did not assign the right to receive the payments, the lender acquired a lien only against the seller's possibility of equitable title reversion. The lender acquired no interest in the unpaid balance of the REC, so a subsequent assignee of the payments prevailed against the lender. See *FNB of Belen*, p. 7, CLA.

Nevertheless, if there is no subsequent third-party assignee, the mortgage constitutes an enforceable security agreement as between the lender and the seller. See *In Re Finch*, p. 8, CLA.

Practice and procedure.

A lender would be well advised to take a collateral assignment of the seller's interest in the REC proceeds as security, rather than a mortgage on the seller's property interest. The collateral assignment should specify whether the escrow agent is instructed to disburse the seller's proceeds from the REC to the lender, or whether the lender will have the right to redirect payments upon default by the seller on the loan agreement. The assignment should be recorded in the county clerk's office, rather than in the office of the Secretary of State.

For additional security, the lender could take a mortgage on the seller's property interest. As noted above, the mortgage would attach only to the seller's possibility of reversion, however, and would have no value as collateral unless the buyer defaults on the REC. The mortgage should contain a provision that it is a lien on any after-acquired property of the seller, to ensure that the lien of the mortgage will attach to the equitable title interest conveyed to seller by special warranty deed after buyer's default.

There is no need for a 'performance deed' from the lender to the buyer. If the buyer pays off the REC, the seller's warranty deed, when delivered from escrow, will terminate any title interest of the lender, by virtue of the 'relation-back' of the delivery from escrow. See

chapter 11.

A release of the collateral assignment should be executed by the lender, and placed in escrow for delivery to the seller upon payment in full of the loan. See no. 12, Forms Appendix. If a mortgage was taken from the seller as additional security, then a release of the mortgage should also be placed in escrow. See form no. 17.

Sales of Buyer's Interest in REC

The buyer's interest in the REC is real estate, consisting of equitable ownership of the property itself, and the contractual right to acquire legal title upon completion of the requirements of the REC. There are four different methods by which the buyer can sell his interest in the property and in the REC.

1. He can enter into an assumption agreement, by which the new buyer assumes and agrees to pay the REC in accordance with its terms. See chapter 3.
2. He can enter into a wrap-around agreement, by which the new buyer does not assume the REC, but the unpaid balance of the REC is incorporated into the debt owed by the new buyer to the buyer. See chapter 4.
3. He can sell the property by means of a warranty deed to the new buyer, subject to the REC, and take back a promissory note secured by an equitable mortgage on the property.
4. He can assign his rights in the REC to the new buyer, and deed the property to the new buyer, subject to the REC.

Assumption Agreements and Wrap-around Contracts

When the buyer enters into a new REC with his purchaser, whether the agreement is an assumption or a wrap-around, the existing contractual relationship between the buyer and seller remains undisturbed. There is no substitution of parties to the existing contract. Rather, a new contractual relationship, involving a completely separate set of corresponding rights and duties, is created between the buyer and the sub-purchaser. See chapters 3 and 4 for a full discussion of the implications arising from this important distinction.

There are two reasons for creating a new contract with the sub-purchaser. First, it is necessary when the sale involves installment payments on the buyer's equity in the property, rather than a 'cash-to-loan' sale. The new contract serves as a debt instrument, and provides a mechanism for escrowing of title documents, just like the senior REC. Second, it provides the buyer with a security interest in the property, not only for the payment of his equity, but also (in the case of an assumption agreement) for the sub-purchaser's obligation to pay the assumed REC.

Equitable Mortgages

The buyer can deed the property to the sub-purchaser, subject to the REC. He can then take back a promissory note for his equity in the property, and secure the note with an equitable mortgage. See chapter 10 for a full discussion of this procedure.

The sub-purchaser is benefited by this technique. He gets the greater protection afforded by a mortgage against a default on the debt to the buyer. If he pays off the senior REC at some point, he will then terminate the risks of forfeiture inherent in the REC, and have the full protection of a legal mortgage against any default on the mortgage note to the buyer. Having acquired the legal title, he would also be able to obtain a home improvement or equity loan without the need to pay off the buyer.

Assignment and Conveyance of Buyer's Interest

If the buyer sells the property on a "cash-to-loan" basis - i.e., the buyer's interest in the property is to be fully retired for a payment or property exchange - then an assignment of the REC and conveyance of equitable title can be used as vehicles for the sale. The buyer does not retain a security interest by using this method. That would be of no consequence, if the seller elects to terminate the REC upon a future default by the assignee. However, if the seller elects to accelerate the REC balance and files suit against the buyer to collect, the buyer may wish that he had sold on a dollar-for-dollar wrap-around agreement! Without the security interest provided by a REC, he will have to file a third-party claim against the assignee, obtain a judgment, then file a judgment lien against the property and foreclose in order to recoup his loss.

Nature of Assignment

Unlike a resale on a new REC, a new security interest is not created when the buyer assigns his interest in the REC and deeds equitable title to the assignee. Instead, the assignee acquires all the contractual rights and title interests of the buyer. By accepting the assignment, he agrees with the buyer to perform the obligations of the REC. Unless the seller consents to the assignment and agrees to mail copies of default notices to the assignee, however, no contractual relationship is created between the assignee and the seller. The buyer's contractual relationship with the seller remains unchanged. If the assignee defaults, the seller will be obliged to mail notice of default to the assignee as well as to the buyer, but his remedy of acceleration of the unpaid balance is against the buyer only.

If the assignee and the seller enter into an agreement whereby the assignee agrees with the seller to be bound by the REC, and the seller agrees to release the buyer from the obligations of the contract and to accept the assignee as a substituted party, then a *novation* occurs. The difference between a resale on a new REC and an assignment with full substitution of parties can be compared to the common law *alienation by sub-infeudation* and *alienation by substitution*.

Assignment & Acceptance

The buyer must sign an appropriate form of assignment. The signature must be acknowledged, and the document should be promptly recorded in the county clerk's office in the county where the property is located. A statement should be included by which the assignor makes a representation regarding the escrow, the currently unpaid balance of the

REC and the due date for the next payment to be made by the assignee. It would also be a good idea to include a statement that assignee acknowledges receipt of a copy of the REC, as well as copies of any mortgages and contracts senior to the REC, and to which the REC is subject.

The assignee signs and acknowledges a document accepting the assignment of the buyer's REC interest, and agrees to be bound by all the terms and conditions of the REC. The document is promptly recorded with the assignment. The acceptance can be incorporated into the assignment, or it can be executed and recorded as a separate document. Using a combined form can reduce recording fees.

Conveyance of Title

The buyer executes a warranty deed, conveying title to the property to the assignee. This deed is promptly recorded with the assignment and acceptance of assignment. Because the buyer does not yet have title (the warranty deed conveying title to him is still in escrow, undelivered), this warranty deed must contain a statement that the deed is subject to the REC and that the grantee (assignee) has assumed and agreed to perform all the terms and conditions of the REC in accordance with its terms. Here is an example:

Subject to a certain real estate contract dated _____ wherein Grantor herein is named as Purchaser and _____ is named as Seller, recorded in Book _____, Pages _____ as document number _____, of the records of the Clerk of _____ County, New Mexico on ____ (date) _____, which contract Grantee herein has assumed and agreed to be bound by the terms thereof.

If the REC being assigned is itself an assumption agreement, then a similar "subject to" clause should be added for each mortgage or contract that is assumed in the REC.

If the REC being assigned wraps around any senior mortgage or REC, then a "subject to" clause should be added for the wrapped mortgage or REC, but no statement should be made that grantee assumes that mortgage or REC. The assignee is succeeding to the buyer's position in the REC. Since the buyer did not assume the wrapped mortgage or REC, neither does his assignee. However, since the buyer's contractual rights to acquire legal title are subject to the retirement of the wrapped mortgage or REC by the seller, the assignee's conveyance from the buyer must be subject to the same condition.

The form of conveyance in this situation must be a warranty deed or special warranty deed. As noted above, the buyer does not yet have legal title at the time his deed to the assignee is executed and recorded. The warranty deed placing legal title in the buyer will be released from escrow and recorded when the assigned REC is paid in full at some future date. By operation of the after-acquired title doctrine, legal title will at that time pass through the buyer to his assignee, but only if the buyer's conveyance to assignee contained warranty covenants or special warranty covenants. A quitclaim deed would be ineffective, because it includes no covenants. See chapter 9.

Combined Assignment and Conveyance

For economy of effort and to save on recording fees, a combined form of assignment and conveyance can be used. See no. 10, Forms Appendix.

‘Performance Deed’ (or ‘non-performance deed’, if you like)

By the terms of the assignment, the assignee agreed to be bound by all the terms and conditions of the REC. One of those requirements is that the buyer will deliver into escrow an unrecorded special warranty deed, naming the seller as grantee. Since the assignee has succeeded to the buyer's position in the REC, he should now satisfy that requirement. Therefore, the assignee should sign a special warranty deed similar to the one already in escrow. The signature is acknowledged, and the original deed is placed in escrow along with the other deeds already there. The deed is not recorded at this time. The escrow agent will release it to the seller for recording only if a default and forfeiture subsequently occurs under the terms of the REC.

Failure by the assignee to deliver a special warranty deed into escrow should not, however, cloud the seller's title if a default and forfeiture occur. Delivery from escrow of the buyer's special warranty deed should be sufficient, because that delivery ‘relates back’ to the delivery *into* escrow of that deed, and takes priority over any subsequent assignment or conveyance executed by the buyer. The rationale here is exactly the same as the reasoning that excuses the delivery of a ‘performance deed’ from the seller's assignee.

Seller's Consent

If the REC contains a due-on-sale clause, it will be necessary to obtain the seller's written consent prior to executing an assignment and conveyance of the buyer's interest. See the discussion of this issue in chapter 7.

Collateral Assignments of Buyer's Interest in REC

The buyer executes a collateral assignment to the lender similar in form to the seller's collateral assignment. The differences are that no rights to receive payments are involved, and the lender has the right to succeed to the buyer's position in the REC upon any default by the buyer, either on the REC or on the secured note. The same considerations regarding releases apply here as for release of seller assignments, and the same form is used. Because the buyer's interest under the REC is represented by equitable title to real estate, there should also be a mortgage of the buyer's equitable interest to the lender. As noted above, the buyer's equitable interest is mortgageable. See *Shindledecker*, p. 6 CLA.

Escrow Considerations

Since preservation of the lender's security interest depends entirely upon the buyer's continued performance of the requirements of the REC, it is critical that the lender arrange to be notified of any default by the buyer. Merely recording the mortgage/collateral assignment does not give the seller constructive notice of the lender's interest, such as would require the seller to notify the lender of seller's intent to retake the property. See *Shindlegdecker*. The lender should send a copy of the recorded collateral assignment and mortgage to the seller with a letter requesting that the lender be added as a copy addressee of any notice of default issued in the future by the seller. A copy of this correspondence should be sent to the escrow agent.

Three forms of deeds are generally used in conjunction with REC'S: Warranty Deeds, Special Warranty Deeds, and Quitclaim Deeds. These are "statutory forms," meaning that when a deed in substance follows a form incorporated in the New Mexico Statutes, the legal effect of the deed is controlled by the statute. Statutory forms can be purchased from most office supply stores.

Warranty Deed

A copy of the statutory form appears as no. 13 in the Forms Appendix. The governing statute is Section 47-1-29 NMSA 1978:

A deed in substance following the form entitled "warranty deed" in the appendix to this Act (47-1-44 NMSA 1978) shall, when duly executed, have the force and effect of a deed in fee simple to the grantee, his heirs and assigns, to his and their own use, with covenants on the part of the grantor for himself, his heirs, executors, administrators and successors, with the grantee, his heirs, successors and assigns, as specified in the definition of "warranty covenants" in Section 10 (47-1-37 NMSA 1978) of this act.

Section 47-1-37 defines "warranty covenants" as follows:

In a conveyance of real estate the words, "warranty covenants" shall have the full force, meaning and effect of the following words: "The grantor for himself, his heirs, executors, administrators and successors, covenants with the grantee, his heirs, successors and assigns, that he is lawfully seized in fee simple of the granted premises; that they are free from all former and other grants, bargains, sales, taxes, assessments and encumbrances of what kind and nature soever; that he has good right to sell and convey the same; and that he will, and his heirs, executors, administrators and successors shall warrant and defend the same to the grantee and his heirs, successors and assigns forever against the lawful claims and demands of all persons."

A warranty deed, then, is a conveyance of real estate which contains the words "warranty covenants" in the grant language. The grantor warrants to the grantee, et al., that no encumbrances exist against the property, whether incurred by the grantor or anyone in the chain of title before him. Thus, failure to recite on the deed any exceptions to the warranty may result in a breach of warranty subjecting the grantor to a claim for damage. Following are some examples of disclaimers, which are inserted on the form immediately following the legal description:

Subject to taxes for 1998 and all subsequent years;

Subject to all easements, reservations and restrictions of record;

Subject to a certain mortgage (real estate contract) (deed of trust) dated June 15, 1995 by and between, etc. (see chapter 3), which the Grantee herein assumes and agrees to pay in accordance with its terms;

In conjunction with REC'S, warranty deeds are generally used to convey title:

- (a) from seller to buyer;
- (b) from seller's assignee to buyer (see chapter 8).

Special Warranty Deed

For the statutory form, see no. 14, Forms Appendix. The governing statute is 47-1-31 NMSA 1978:

A deed in substance following the form entitled "special warranty deed" shall, when duly executed, have the force and effect of a deed in fee simple to the grantee, his heirs and assigns, to his and their own use, with covenants on the part of the grantor, for himself, his heirs, executors, administrators, and successors, with the grantee, his heirs, successors and assigns as specified in the definition of "special warranty covenants" in Section 11 (47-1-38 NMSA 1978) of this act.

Section 47-1-38 defines "special warranty covenants" as follows:

In a conveyance of real estate the words "special warranty covenants" shall have the full force, meaning and effect of the following words: "The grantor for himself, his heirs, executors, administrators and successors, covenants with the grantee, his heirs, successors and assigns, that the granted premises are free from all encumbrances made by the grantor, and that he will, and his heirs, executors, administrators and successors shall warrant and defend the same to the grantee and his heirs, successors and assigns forever against the lawful claims and demands of all persons claiming by, through or under the grantor, but against none other."

The special warranty deed is identical in form to the warranty deed, except for the title and the granting language, which contains the words "special warranty covenants" in place of the words "warranty covenants." The scope of the warranty is much less than the warranty deed:

- The grantor does not warrant that he is lawfully seized in fee simple of the granted premises;
- There is no warranty regarding any encumbrances placed against the property by those in the chain of title before him. The grantor merely warrants that there

are no encumbrances existing against the property which were made by him. The grantor is responsible to defend the grantee's title only against claims of persons claiming an interest "by, through or under the grantor." Thus, in order to avoid a breach of warranty, it is necessary to recite on the deed as exceptions to the special warranty covenants only those encumbrances that came into existence subsequent to the grantor's acquisition of an interest in the property.

In conjunction with REC'S, special warranty deeds are used to convey:

- (a) equitable title from buyer to seller upon a default and termination of the REC;
- (b) legal title from seller's assignee to buyer (but query whether this satisfies the obligation of seller's assignee to perform the REC in accordance with its terms);
- (c) legal title from seller to buyer in situations where the status of land title is unclear or title insurance cannot be obtained.

Quitclaim Deed

The statutory form is found in the Forms Appendix as Form No. 15. Section 47-1-30 NMSA 1978 states:

A deed in substance following the form entitled 'quitclaim deed' shall, when duly executed, have the force and effect of a deed in fee simple to the grantee, his heirs and assigns, to his and their own use of any interest the grantor owns in the premises, without warranty.

A quitclaim deed is a grant only of whatever title the grantor has, and no warranties whatever are made. Thus, any deed that does not contain the words "with warranty covenants" or "with special warranty covenants" is a quitclaim deed. Let the grantee beware!

This form is usually used to convey the interest of a joint tenant or co-tenant to a spouse in conjunction with a property settlement incidental to a divorce or legal separation. It has also been frequently used to convey title from a seller's assignee to the buyer. However, this use of the quitclaim deed must be seriously questioned. First, the REC gives the buyer the right to acquire title by warranty deed. A quitclaim deed therefore does not satisfy the obligation of seller's assignee to perform the REC in accordance with its terms. Also, the quitclaim deed, because it does not convey after-acquired title, may cause a break in the title chain. See discussion below of after-acquired title.

Partial Property Releases

When multiple property lots are sold in a single REC, the parties may desire to arrange for piecemeal transfer of title to the buyer as the REC balance is reduced. For example: owner sells 4 lots to buyer on a REC, with a purchase price of \$50,000.00, \$10,000.00 down payment, and \$40,000.00 payable in monthly installments. The REC provides that with each principal reduction of \$10,000.00, buyer shall receive title to one lot from escrow. Following is a discussion of the necessary elements to consummate the transaction.

Deeds of Conveyance

At closing the seller should execute a separate warranty deed for each lot, and the buyer should execute corresponding special warranty deeds for each lot. A total of 8 unrecorded deeds will be placed in escrow with the designated escrow agent.

It is not a good idea to ask the escrow agent to draft and execute the deeds, for several reasons:

- Most escrow offices and banks are not staffed for such work, and will refuse to accept the responsibility;
- Such activities by the escrow agent may constitute the unauthorized practice of law;
- A recorded power of attorney would be required to give the escrow agent the authority to execute a valid deed. This would be unsatisfactory, because a power of attorney is extinguished by the death of the grantor of the power.

When the parties desire to have the escrow agent prepare and execute the partial releases of title, a note and deed of trust should be used rather than a REC. That instrument grants a lien to the trustee, and the trustee can be authorized to prepare and execute individual releases from the lien of the deed of trust. See chapter 11.

Drafting Considerations

A provision must be inserted in the REC authorizing piecemeal release of the deeds upon written request by the buyer and specifying the sequence in which the deeds are to be released by the escrow agent, or alternatively, stating that the buyer may choose the deeds to be released. Typically, escrow agents will not initiate lot releases, but will act only upon a written request from the buyer.

If it is specified that lots released must be contiguous to lots previously released, then a statement must also be included that the escrow agent shall not be required to determine

whether the buyer's lot release requests satisfy the contiguity requirement. The escrow agent is in no position to verify contiguity, unless a plat or map showing the lot numbers is also placed in escrow.

Most agents charge a fee for each partial release request processed, so there should be a specification that the buyer will pay the agent's fee for any partial releases processed.

Following is a sample REC partial release provision, using the factual situation described above. The provision may be inserted in Paragraph 3 of form 103 or Paragraph 2 of the RANM form.

"PARTIAL RELEASES. The buyer shall be entitled to release from escrow of a warranty deed to one (1) lot for each principal reduction of \$10,000.00 from the unpaid balance of this contract.

[Deeds shall be released from escrow in any sequence desired by the buyer, upon written request to the escrow agent.]

-or-

[Deeds shall be released from escrow for lots 1, 3, 4 and 2 in that sequence, upon written request by the buyer.]

-or-

[Deeds shall be released from escrow in any sequence desired by the buyer, upon written request to the escrow agent, provided that each succeeding lot released must be contiguous to one or more lots previously released. The escrow agent shall not be required to verify contiguity of requested lots to lots previously released. The escrow agent is authorized to rely upon the buyer's written requests for lot releases, provided that the principal reduction requirements are satisfied.]

All fees of the escrow agent for processing partial release requests shall be paid by the buyer."

Escrow Letter

The standard form escrow letter should be amended to itemize all the deeds being placed in escrow. In form 103, the instruction to the escrow agent to 'deliver all the above-mentioned papers to said Owner' upon the buyer's default should be amended to "deliver to said Owner all special warranty deeds for lots not previously released or eligible for release to buyer pursuant to the partial release provisions of this contract."

Senior Encumbrances

It is imperative that the seller be in a position to give good title to the buyer for each lot released from the REC, at the time of release from escrow. Thus, if the seller purchased a tract of land by REC and subsequently subdivided the tract into four lots, he ordinarily could not acquire title to any one of the lots without first paying the senior contract in full. If it is not the seller's intention to accelerate payment on the senior REC in this way, then

he should arrange with the owner of the senior REC to amend that REC to provide for partial releases, and to substitute new deeds for the deeds already in the senior escrow agent's file. Of course, the legal description of the tract would also have to be amended to describe the property as subdivided. If the property is subject to an existing mortgage the seller would need to make similar arrangements with the mortgagee. Finally, the escrow agent servicing the junior REC should be authorized to disburse sufficient amounts from payments made on the junior REC to the senior escrow agent and/or mortgagee to obtain the necessary partial releases from the senior REC and/or mortgage.

After-Acquired Title Doctrine

It may be accepted as a general rule that a grantor may not convey more or better title than he owns. How then can he convey title that he does not yet own, but expects to acquire at a future date? In any assumption agreement, it is entirely possible that the junior REC buyer may pay off his seller and acquire the warranty deed from escrow before paying off the senior REC. This means that the seller's warranty deed to the buyer will be delivered and recorded before the seller acquires legal title under the senior REC.

The seller's warranty deed contains a "subject to....." clause which prevents a breach of warranty resulting from the existence of an unsatisfied REC, but is the seller's warranty deed effective to convey legal title? Since he did not have the legal title when the warranty deed was delivered to his buyer and recorded, is it not necessary for him to execute and deliver another deed after he acquires title under the senior REC?

No. (A fortunate thing, for otherwise thousands of titles acquired in New Mexico through assumption agreements, wrap-around agreements and buyer and seller assignments would be invalid.) It was well established at common law that when a grantor conveyed real estate by a deed containing covenants of warranty, then later acquired title to that property, the court would not allow the grantor to claim title adverse to his grantee. The doctrine is known as "estoppel," or more specifically, "estoppel by deed." The basis for invoking the doctrine was the presence in the deed of warranties of title. Where no warranties existed, the doctrine did not apply. It was reasoned that when warranties existed, the doctrine was necessary to prevent "circuitry of action," for although the grantor might successfully assert an after-acquired title against his grantee, he would be liable in damages to his grantee for breach of warranty. If no warranties were present, then no breach would result from assertion of after-acquired title, and no need for application of the estoppel doctrine would exist.

The rule has carried forward into the case law or statutes of nearly every state, and is a well-settled principle of law. Some states have modified the rule, but generally it is true that deeds containing warranties of title (e.g., warranty deeds and special warranty deeds) convey after-acquired title to the grantee by operation of law, whereas deeds not containing

warranties of title (e.g., quitclaim deeds) do not.

For this reason, it is imperative that a quitclaim deed not be used in any situation where the grantor may not have legal title at the time the deed is ultimately delivered to the grantee. Since this situation frequently arises, sometimes unpredictably, in connection with the escrow of REC'S, great caution should be observed in using the quitclaim deed for escrowed transactions.

Nevertheless, situations may arise where the grantor is not in a position to warrant status of title, but desires to convey to grantee a title that will be subsequently acquired. Most courts that have considered the question have applied the estoppel doctrine to quitclaim deeds if the deed contains a clear statement of the grantor's intent to convey such title. Therefore, the problem might be avoided by adding to the quitclaim deed language to the following effect:

- Grantor covenants with grantee, his heirs, successors and assigns that he will, and his heirs, executors, administrators and successors shall warrant and defend all hereafter-acquired title to the Grantee and his heirs, successors and assigns forever against the lawful claims and demands of all persons, to the extent of the title acquired.

Thus, the grantor expressly supplies a warranty that would otherwise be lost by the omission of warranty covenants of title, and thereby prevents the failure of pass-through of after-acquired title.

Any real estate sale in which the seller becomes a creditor of the buyer for a portion of the sales price might be described as an "owner-financed" transaction. Owner financing became popular during the high-interest inflationary period of the 1970's when prospective buyers simply could not afford to 'buy out' the seller's ownership interest in real estate, or could not qualify for a traditional refinancing loan from a bank or savings and loan company.

In New Mexico, the most popular owner-financing tool is the real estate contract. Its popularity is due primarily to the simple, inexpensive and informal remedy by which the seller can recover the property if the buyer fails to maintain payments. In many owner-financed sales, the buyer can afford to make only a relatively small down payment. It is not surprising, then, that a property owner would be unwilling to sell to such a buyer unless he could readily recover the property without great expense if the buyer defaults. Traditional financing devices like the mortgage and the deed of trust are not adequate for this purpose, because they involve an initial transfer of legal title to the buyer with a mortgage back to the seller or a trustee. Upon default, title can only be recovered after an expensive and often lengthy judicial foreclosure proceeding.

Thus, the real estate contract came to be known as the "poor man's key to property ownership." As continuing inflation and high interest rates placed property ownership out of the reach of an increasingly large segment of the public, the real estate contract in truth became the key to property ownership for the middle economic class as well. Consequently, thousands of people have been enabled to purchase homes and business property who otherwise could not have done so.

Notwithstanding the popularity of the real estate contract, there are situations when the parties to a sale might wish to use a mortgage or deed of trust. For example, a buyer who makes a substantial down payment might insist upon the greater protection provided by the judicial foreclosure requirements of such instruments. Also, a buyer who anticipates making improvements to the property may discover that he cannot get a home improvement loan unless he holds legal title to the property. Finally, a seller may be willing to allow the buyer to convert from a real estate contract to a mortgage or deed of trust after a substantial portion of the purchase price has been paid. For these reasons, the statutory forms of mortgage and deed of trust are briefly described in this chapter and compared to the real estate contract.

Mortgage and Deed of Trust – Statutory Forms

The New Mexico Legislature has adopted statutory forms of mortgage and deed of trust, also commonly known as 'short forms'. Copies of these forms are included in the Forms Appendix as Forms 16 and 18. Use of the short forms avoids the need to include detailed provisions in the instruments which are standard in virtually every case. The mortgage form contains only three sentences:

(1). '_____(mortgagor) grants to _____(mortgagee), whose address is _____, the following described real estate in _____ County, New Mexico: _____ with mortgage covenants.'

(2). 'This mortgage secures the performance of the following obligations:

(Here attach a copy of or summarize the note or other obligation.)

and is upon the statutory mortgage condition for the breach of which it is subject to foreclosure as provided by law.'

(3). 'The amount specified for insurance as provided in the statutory mortgage condition is \$_____ and the hazard__ to be insured against ____fire_____.'

When this form is used, the governing statute, which is section 47-1-39 NMSA 1978, dictates the effect of the form, as follows:

A deed in substance following the forms entitled "Mortgage" or "Deed of Trust" shall, when duly executed, have the force and effect of a mortgage or deed of trust by way of mortgage to the use of the mortgagee and his heirs and assigns with mortgage covenants and upon statutory mortgage condition as defined in the following two Sections (47-1-40 and 47-1-41) to secure the payment of the money or the performance of any obligation therein specified. The parties may insert in such mortgage any other lawful agreement or condition.

Section 47-1-40 then goes on to define the meaning of "mortgage covenants" as follows:

In a mortgage or deed of trust by way of mortgage of real estate "mortgage covenants" shall have the full force and meaning and effect of the following words and shall be applied and construed accordingly:

"The mortgagor for himself, his heirs, executors, administrators and successors, covenants with the mortgagee and his heirs, successors and assigns that he is lawfully seized in fee simple of the granted premises; that they are free from all encumbrances; that the mortgagor has good right to sell and convey the same; and that he will, and his heirs, executors, administrators and successors shall, warrant and defend the same to the mortgagee and his heirs, successors and assigns forever against the lawful claims and demands of all persons."

Section 47-1-41 defines the meaning of "statutory mortgage condition" as follows:

In a mortgage or deed of trust by way of mortgage of real estate the words, "Statutory mortgage condition" shall have the force, meaning and effect of the following words and shall be applied and

construed accordingly: "In the event any of the following terms, conditions or obligations are broken by the mortgagor, this mortgage (or deed of trust) shall thereupon at the option of the mortgagee, be subject to foreclosure and the premises may be sold in the manner and form provided by law, and the proceeds arising from the sale thereof shall be applied to the payment of all indebtedness of every kind owing to the mortgagee by virtue of the terms of this mortgage or by virtue of the terms of the obligation or obligations secured hereby:

- A. Mortgagor shall pay or perform to mortgagee or his executors, administrators, successors or assigns all amounts and obligations as provided in the obligation secured hereby and in the manner, form, and at the time or times provided in the obligation or in any extension thereof-
- B. Mortgagor shall perform the conditions of any prior mortgage, encumbrance, condition or covenant;
- C. Mortgagor shall pay when due and payable all taxes, charges and assessments to whomsoever and whenever laid or assessed upon the mortgaged premises or on any interest therein;
- D. Mortgagor shall, during the continuance of the indebtedness secured hereby keep all buildings on the mortgaged premises in good repair and shall not commit or suffer any strip or waste of the mortgaged premises;
- E. Mortgagor shall pay when due all State and Federal grazing lease fees; and
- F. Mortgagor shall keep the buildings on the mortgaged premises insured in the sum specified and against the hazards specified in the mortgage for the benefit of the mortgagee and his executors, administrators, successors and assigns. The insurance shall be in such form and in such insurance companies as the mortgagee shall approve. Mortgagor shall deliver the policy or policies to the mortgagee and at least two days prior to the expiration of any policy on the premises shall deliver to mortgagee a new and sufficient policy to take the place of the one so expiring. In the event of the failure or refusal of the mortgagor to keep in repair the buildings on the mortgaged premises; or to keep the premises insured, or to deliver the policies of insurance, as provided; or to pay taxes and assessments, or to perform the conditions of any prior mortgage, encumbrance, covenant or condition, or to pay State and Federal grazing lease fees, the mortgagee and its executors, administrators, successors or assigns may, at his option, make such repairs, or procure such insurance, or pay such taxes or assessments, or pay such State and Federal grazing lease fees, or perform such conditions and all monies thus paid or expenses thus incurred shall be payable by the mortgagor on demand and shall be so much additional indebtedness secured by the mortgage."

The third sentence on the short form provides the information required to complete obligation 'F' relating to hazard insurance. By statutory incorporation, then, a mortgagor who signs the statutory 'short' form is legally obligated by all the warranties and obligations stated in the statute to the same extent as if they were fully set forth in the mortgage itself.

The short form deed of trust is exactly the same as the short form mortgage, except for the first sentence, which states:

‘ _____ (mortgagor) grants to _____ whose address is _____, as trustee for _____, whose address is _____, Beneficiary, the following described real

estate etc.’

Thus, the lien holder is a neutral third party, who holds the lien for the benefit of the seller or lender, who is described in the instrument as ‘Beneficiary’.

The advantages of the statutory forms are that they are easy to use and they save recording fees, which are based on the number of pages contained in the instrument. The disadvantage is that, unless the parties are attorneys or real estate professionals, they probably don’t have a clue as to all the legal implications of using these forms. If it is necessary or desirable to delete, change or add to the warranties and obligations, then the ‘long form’ documents should be used, and tailored according to the needs and requirements of the parties. For example, see the ‘Equitable Mortgages’ section below. Also, by using the ‘long form’, attorneys and real estate professionals representing clients can better protect themselves against the charge that the client was not properly advised as to the consequences of signing the document. When all the warranties and obligations are explicitly set forth in the document, the client is presumed to have read and understood those provisions when he signed the document.

Distinguished From Real Estate Contract

When an owner-financed sale is secured by a mortgage, the seller first transfers legal and equitable title to the buyer by warranty deed. The buyer signs a promissory note for the unpaid balance of the purchase price, and secures the note by executing a mortgage naming the seller as mortgagee. The mortgage constitutes a lien on the equitable and legal title. When the promissory note is paid in full, the seller (mortgagee) executes a ‘Release of Mortgage’ which releases the property from the lien of the mortgage.

When a REC is used, legal title remains in the seller, and is held by the seller ‘in trust’ for the buyer. By operation of the doctrine of equitable conversion, equitable title passes to the buyer, and the buyer is regarded as the ‘owner’ of the real estate for most purposes. The seller executes a warranty deed, which is delivered into escrow for subsequent delivery to the buyer when the REC is paid in full. Delivery of the deed from escrow to the buyer conveys the legal title. See chapter 2 for a complete discussion of the respective property interests of the buyer and seller.

Prior Encumbrances

The mortgagor covenants "...that they (the granted premises) are free from all encumbrances...". However, one of the statutory mortgage conditions is that "...Mortgagor shall perform the conditions of any prior mortgage, encumbrance, condition or covenant". The covenant and the condition would appear to be in conflict. Fortunately, Section 47-1-40 provides some leeway: "The parties may insert in such mortgage any other lawful

agreement or condition." If the buyer is taking the property subject to one or more prior mortgages or deeds of trust, then those exceptions to the mortgage covenant must be explicitly declared in the mortgage, so the buyer will not be in violation of the covenant. If the intention is to "wrap" the prior mortgage or deed of trust rather than assume it, then that intention must also be clearly declared, because the statutory mortgage condition would otherwise require the mortgagor to perform the prior obligation. The drafting suggestions contained in chapters 3 and 4 regarding "Subject to" clauses are applicable here.

Assignments

The holder of a mortgage and the beneficiary of a deed of trust can assign their interests to a third party. The right to receive future payments, represented by the promissory note, is sold, usually at a discount, to a third-party investor. The security for those payments, represented by the mortgage, is also assigned to the investor. The investor takes the place of the mortgagee or beneficiary and receives, in addition to the right to receive payments, the right to foreclose upon default by the buyer (mortgagor). To consummate this transaction, the mortgagee executes an "Assignment of Mortgage" or "Assignment of Deed of Trust." These are statutory forms, set forth in Section 47-1-44 NMSA 1978 as forms (12) and (13). See no. 19 and 20, Forms Appendix. The mortgagee also assigns ownership of the promissory note to the investor, either by an endorsement on the back of the note, or by a separate form of assignment.

Legislation

There are a number of statutory provisions that govern mortgages and deeds of trust, some of which do not apply to REC's. Accordingly, these statutes must be taken into account in the selection and servicing of seller-financing documents.

- Recording statute. Section 14-9-1 NMSA 1978 provides in part:

'All deeds, mortgages, ...and other writings affecting the title to real estate shall be recorded in the office of the county clerk of the county or counties in which the real estate affected thereby is situated.'

Section 14-9-3 states:

'No deed, mortgage or other instrument in writing not recorded in accordance with Section 14-9-1 NMSA 1978 shall affect the title or rights to, in any real estate, of any purchaser, mortgagee in good faith or judgment lien creditor, without knowledge of the existence of such unrecorded instruments. Possession alone based on an unrecorded executory real estate contract shall not be construed against any subsequent purchaser, mortgagee in good faith or judgment lien creditor either to impute knowledge of or to impose the duty to inquire about the possession or the provisions of the instruments.'

Possession is 9/10th (oops, make that 1/10th) of the law. The first sentence of section 14-9-3 has been in the statute since 1887. The second sentence was added in 1990, in order to terminate the effect of a string of Supreme Court decisions. Those decisions had held that when the buyer under an unrecorded REC is in possession of the real estate, the fact of his possession alone is sufficient to create a duty on the part of any subsequent buyer or mortgagee to make inquiry into the rights of the possessor. Failing to make such inquiry, the subsequent buyer or mortgagee takes his interest in the property subject to the prior rights of the unrecorded REC buyer. See *McBee*, p. 26, *CLA* and *Nelms*, p. 27, *First National Bank of Belen*, p. 7, and *Citizens Bank of Clovis*, p. 28. When the second bank went down in these century-old waters, the banking lobby apparently decided to take action to stop the carnage (and save those expensive Gucci shoes from the wear and tear of field inspections). The result is that the holdings in the four cited cases, to the extent they ruled on this particular issue, have been effectively overruled by legislative action.

Interestingly, the added sentence is limited to unrecorded *executory* real estate contracts. Presumably, the possession of a buyer under an unrecorded, but fully performed REC would still give rise to the duty of inquiry as held by the four Court decisions. Since a prospective purchaser or lender would have no way to know, in the absence of inquiry, whether the possessor's claimed property rights derived from an executory or a fully performed REC, it would seem prudent to make inquiry, notwithstanding the statute.

- Payment to holder of record as a complete defense. A mortgagor may make payment to the holder of the last recorded assignment of a mortgage, and such payment is a complete defense to any claim by any holder of an unrecorded assignment, unless the mortgagor has actual notice or knowledge of the assignment. This is true, even though the secured note may have been assigned or endorsed to the holder of the unrecorded assignment. *Sections 48-7-2 and 48-7-3 NMSA 1978.*
- Duty of mortgagee/trustee to record release. When a debt secured by a mortgage or deed of trust is paid in full, it is the duty of the mortgagee, trustee or assignee to record a full satisfaction of the debt in the office of the county clerk of the county where the mortgage or deed of trust is recorded. Any person who violates this requirement is subject to a fine of \$10.00 to \$25.00, and is liable in a civil action to the owner of the real estate for all costs of clearing title to the property, including a reasonable attorney's fee. *Sections 48-7-4 and 48-7-5, NMSA 1978.* For this reason, knowledgeable escrow agents will refuse to accept a note and mortgage into escrow unless an executed release of mortgage is also placed in escrow. Statutory forms are set forth in Section 47-1-44, and are reproduced in the Forms Appendix as forms no. 17, 21, 22 and 23. The "Partial Release" forms should be used when the land is to be released piecemeal.

- Limits on tax/insurance escrows. A mortgagee may collect a monthly charge to be held in escrow for the payment of taxes and insurance premiums, provided the balance in the escrow fund does not exceed two months' total charges plus the pro rata accrual for such charges. Once each year, the mortgagor may demand that any excess balance above the allowed accumulation be applied to the principal balance of the mortgage. Failure of the mortgagee to comply with the demand within 60 days results in a penalty of 6% per year to run on the amount of the excess accumulation, payable to the mortgagor. *Section 48-7-8 NMSA 1978.*
- Priority of security as to future advances. A mortgage may secure future advances, provided the lien of the mortgage never exceeds at any one time the maximum amount stated in the mortgage. The lien of the mortgage has priority from the time of its recording as to all advances. *Section 48-7-9 NMSA 1978.* **Drafting suggestion.** It is important that language be incorporated in the mortgage stating that the mortgage is intended to secure all future advances. The statute is permissive; it states that the mortgage *may* secure future advances.
- Application of hazard insurance proceeds. When an insured loss occurs to a single-family residence, the mortgagor may require that the proceeds of the insurance policy be held jointly by the mortgagor and mortgagee in an escrow account and be applied to the repair or replacement of the damaged property, provided that it be reasonably established to the satisfaction of the mortgagee that the repair or replacement will restore the property to a value at least equal to the balance that remained on the obligation at the time the damage or destruction occurred. *Section 48-7-10 NMSA 1978.*

Since a REC is not a mortgage (see *Bishop*, p. 47, CLA), of the statutory provisions described above, only the recording statute is applicable to REC's.

Deeds of Trust

A deed of trust is, in essence, a mortgage and will be enforced as a mortgage. See *Kuntsman and McInerny*, p. 29, CLA. Accordingly, the Court held that the deed of trust is governed by the recording provisions of sections 14-9-1 and 14-9-2 NMSA 1978, and that recordation of a deed of trust gives constructive notice to subsequent title interests of the beneficiary's claim. It follows that all the mortgage statutes described above relating to payment, releases, escrow funds, future advances and insurance proceeds would be equally applicable to deeds of trust.

Equitable Mortgages

"You can't put a mortgage behind a real estate contract". True, if you are talking about a traditional legal mortgage, which is a lien on the legal and equitable title. One of the statutory mortgage covenants of the mortgagor is that he is seized in fee simple title. Since the buyer in a REC does not hold legal title, he is not in a position to make that representation.

However, the Supreme Court has held that the REC buyer's equitable interest in the property is a mortgageable interest. See *Shindledecker*, p. 6, CLA. The buyer can deed the property to the sub-purchaser, provided the deed recites that it is subject to the existing REC, thereby passing equitable title to the sub-purchaser. The buyer can then take a promissory note from the sub-purchaser for his equity in the property, and secure the note with an **equitable mortgage**.

Drafting suggestion. A long form of mortgage deed should be used, rather than the statutory short form, because the covenant of seizin must be revised to represent that the mortgagor is the holder of an equitable title interest under the existing REC. The mortgage should also include a provision that it is a lien upon any after-acquired legal title interest. Delivery of the warranty deed from the senior REC to the buyer would result in pass-through of legal title to the sub-purchaser, effecting a merger of the legal and equitable titles. At that point, the equitable mortgage would effectively become a full-blown legal mortgage, provided that its lien attaches to the legal title.

Why would anyone want to do this? The sub-purchaser arguably doesn't gain any greater protection, because his interest can be cut off by a non-judicial forfeiture on 30 days' notice if there is a default on the existing REC. True, but he does get the greater protection afforded by a mortgage against a default on the debt to the buyer. If he pays off the senior REC at some point, he will then terminate the risks of forfeiture inherent in the REC, and have the full protection of a legal mortgage against any default on the mortgage note to the buyer. Having acquired the legal title, he would also be in a position to obtain a home improvement or home equity loan without the need to pay off the buyer.

Escrow Considerations

Like a REC, a mortgage or deed of trust, when used as an owner-financing device, should be placed in the hands of an escrow agent for servicing. The escrow agent should be employed as a neutral party to receive and disburse payments, allocate principal and

interest, maintain a payment record and, in the case of a mortgage, to hold the mortgagee's executed release of mortgage pending satisfaction of the debt. When a deed of trust is used, the escrow agent is named as trustee. Since the trustee is authorized to execute the release, there is no need for the beneficiary to place any executed releases in escrow.

The parties can jointly substitute a new escrow agent for a mortgage by a written instrument discharging the escrow agent and appointing the new agent. However, in a deed of trust the escrow agent is a party to the instrument. Therefore, the mortgagor and beneficiary must execute an amendment to the deed of trust, discharging the trustee and appointing a new trustee. The amendment should be recorded. Without the formal amendment, the new trustee is powerless to execute a release of deed of trust when the debt is fully paid.

The RANM REC forms contain detailed provisions regarding the rights, duties and compensation of the escrow agent. Form 103, while inadequate in this regard, does at least contain a rudimentary set of instructions for the agent. The statutory forms of mortgage and deed of trust contain no instructions. When either of these forms is used in a seller-financed sale, the parties must execute a separate set of written instructions.

Default and Foreclosure

When the mortgagor defaults on the note, or fails to perform any of the other conditions of the statutory mortgage covenants, the mortgagee (or beneficiary of the deed of trust) has two separate and independent remedies, which may be pursued separately, or concurrently. He may sue on the promissory note and collect on the money judgment, or he may sue to foreclose the mortgage. Because the remedies are separate, he may sue to collect on the note, even when a first mortgage holder has already foreclosed against the property. See *Kepler*, p. 55, CLA.

When the acceleration remedy in the promissory note is optional, rather than automatic, the mortgagee must give notice to the mortgagor of his intent to accelerate the note, before he can file suit on the note. See *Comer*, p. 56, CLA. Before notice is given, the mortgagee is barred from accelerating the note if he refuses a tendered payment on the note, and he is held to have waived his right to accelerate if he accepts a payment! *Id.* Therefore, if he desires to accelerate the note upon default, it is critical that notice of intent to accelerate be given to the mortgagor immediately upon default.

Where the note provides that the holder may accelerate without notice, payments tendered before the suit is filed could presumably be refused.

Definition

An escrow agent is a special agent or trustee, appointed jointly by the buyer and seller to administer certain provisions of a REC, mortgage or deed of trust. The escrow agent is not a principal party to the transaction (except in the case of a deed of trust), but acts only as a neutral agent for the parties. The escrow agent is also a depositary for holding title documents, stock, money or other documents pursuant to the terms of an escrow agreement between the buyer and seller. Unlike other agents, the escrow agent's capacity, once created by the joint act of the parties to the escrow, cannot be terminated by either party unilaterally or by the death or incapacity of either party.

Functions

Functions of the escrow agent in a seller-financed real estate sale are typically threefold:

1. to receive payments from the buyer and disburse them in accordance with written instructions to senior lien holders and to the seller or the seller's representatives (e.g. realtor's commissions);
2. to maintain a record of payments received and disbursed, including allocation of payments to principal and interest; and
3. to act as custodian of certain title documents in accordance with written instructions, pending performance or default of the sales agreement by the buyer. In the case of a deed of trust, the escrow agent holds the mortgage lien on the legal and equitable title to the property as trustee, subject to the terms of the deed of trust.

Functions of the escrow agent do not normally include preparation of documents or acting as closing agent. These tasks are performed by lawyers and title companies. The escrow agent is appointed by the parties to the real estate contract or deed of trust, or in a separate agreement incidental to a mortgage. Consequently, its duties are created upon execution of the appointing instrument, and not before. The escrow agent is not represented at the

closing. For these reasons, the escrow agent is not responsible for the adequacy or accuracy of the documents placed in escrow.

Historical Development

Before the advent of complex escrows, REC's were serviced by banks and savings & loan companies. Form 103 was the instrument universally employed for this purpose. Typically, the seller's bank would be appointed as escrow agent. Banks charged little or no fees for this service, because the seller was already a depositor and/or borrower from the bank, and banks performed the escrow service as a 'loss-leader' service to maintain good will with an existing customer. Because most escrowed transactions were relatively simple, requiring only one disbursement from each monthly payment into the seller's account at the bank, one or two bank clerks could be assigned the task of maintaining the escrow files. Calculation of principal and interest was not usually required, because the 'periodic interest' method was universally accepted, and payments could be lined through and initialed by a clerk on a pre-printed amortization schedule. Payment records were maintained on the amortization schedule or on a separate ledger card.

With the arrival of inflation and high interest rates in the 1970's, seller-financed sales transactions became more popular. Because such sales increasingly involved improved property burdened with existing encumbrances, REC's also became more complex: the typical REC required the assumption or wrap-around of prior mortgages and contracts. Banks were overwhelmed by a large volume of difficult and time-consuming escrow accounts. Bank clerks, untrained in law and real estate, made more errors and banks were confronted with a growing number of liability claims. The low-cost 'goodwill service' had become a costly burden.

Banks and savings institutions responded by boosting fees and by imposing severe limitations on the types of escrows which would be accepted. For example, some banks refused to accept wrap-around contracts. Others refused to accept any escrow which required the escrow agent to make disbursements outside the bank, thus eliminating all assumption agreements and wrap around contracts where the bank did not hold the prior encumbrance. As a result, a fertile environment was created for the development of a new service industry comprised of independent escrow companies.

Independent Escrow Companies

The first independent escrow company, Security Escrow Corporation, was incorporated in 1975, followed shortly thereafter by several others. These companies were owned and operated by individuals with professional backgrounds in law, real estate and accounting.

They specialized in the servicing of REC'S, mortgages and deeds of trust, and accepted most escrow transactions, regardless of difficulty.

The independent companies introduced data processing techniques, and developed the ability to process payments faster and more accurately than banks and savings institutions. Security Escrow Corporation was the first escrow agent in New Mexico to employ a computer in the processing of escrow payments.

The independent companies prospered. Real estate agents, title companies and lawyers preferred them as escrow agents. Many banks contracted with them to service the banks' inventory of escrow accounts, and stopped accepting new escrow accounts. Other banks increased their fees to levels above the fees charged by the independent companies, to encourage the referral of new accounts to the new companies. By 1982, over 25 independent escrow companies were doing business in New Mexico.

Unfortunately, success also bred abuse. There were several trust account defalcations, and some companies failed, causing significant disruption of service. The industry was in need of governmental regulation for the protection of the public.

State Regulation

In 1983, the New Mexico Legislature enacted the Escrow Company Act (sections 58-22-1 to 58-22-33 NMSA 1978) to regulate the new independents. Regulatory authority was delegated to the Financial Institutions Division of the Regulation and Licensing Department of the state government's executive branch. Banks, savings institutions and title companies were exempted from the Act's coverage.

The Act requires anyone, other than exempted institutions, as a condition to engaging in the business of an escrow agent to be licensed by the Financial Institutions Division. Licensees are required to employ a qualified office manager, and to obtain a fidelity bond. Licensees must maintain adequate books of account and records, and submit to unannounced examinations of their records and files by the Division. Banks, savings institutions and title companies, when acting as an escrow agent are not regulated by the Act and hence are not required to meet these standards.

The Division also investigates complaints filed by the public against independent companies. Licensees are prohibited from engaging in certain 'unauthorized business practices', such as:

- accepting escrow instructions containing blanks to be filled in after the signing of the documents,
- failing to faithfully carry out escrow services pursuant to the written escrow instructions,

- refusing to allow parties to an escrow transaction or their designated agents access to the records of the escrow transaction, and
- failing to distribute funds pursuant to escrow instructions promptly, but in no event later than five days from the final payment as defined in Section 55-4-213 NMSA 1978.

See section 58-22-26 NMSA 1978.

The Act allows escrow agents to charge reasonable set-up, closeout, and other fees, and may charge fees based on the number and amount of disbursements made pursuant to the escrow instructions. Alternatively, escrow agents may charge fees based on the amount of the outstanding loan balance, provided the fee does not exceed one percent per year on the outstanding loan balance.

When an escrow agent files suit to recover trust funds disbursed to or on behalf of a party, or in reliance on a check or draft which is subsequently dishonored, it may recover its attorney's fees and costs. Sect. 58-22-21.1 NMSA 1978.

Duties of Escrow Agent

Generally

An escrow agent's duties are defined by the escrowed documents and the escrow agreement or letter of instructions. For REC'S, these are contained in the "Escrow Letter" section of form 103 and the RANM form. For mortgages and deeds of trust, a separate escrow agreement is usually executed by the buyer and seller. Because the title company closing officer acts as the agent for the buyer and seller in making the escrow deposit, a cover letter of instructions to the escrow agent signed by the closing officer may constitute the escrow instructions, or may supplement an escrow agreement.

When judicial interpretation of the escrow agreement or instructions is necessary, ordinary principles of agency are applied to determine the duty of the escrow agent. Also, the escrow agent is a fiduciary with respect to both buyer and seller, and therefore must be fair, honest and impartial to both parties.

Duty to Deliver

Every escrow is subject to certain conditions, the occurrence of which creates an obligation on the part of the escrow agent to deliver the deposited money or documents to the buyer. The failure of the conditions, or the occurrence of other conditions may obligate the escrow

agent to deliver the escrowed money or documents to the seller.

Effect of Delivery from Escrow

At the inception of the escrow of a REC, the seller delivers a signed and acknowledged, but unrecorded warranty deed to the escrow agent, for subsequent delivery to the buyer upon the occurrence of a condition, which is usually payment in full of the deferred portion of the purchase price. At the same time, the buyer delivers into escrow a signed and acknowledged, but unrecorded special warranty deed, for subsequent delivery to the seller if the buyer defaults and fails to cure within the specified time after written notice of default is mailed to him.

It is basic law that a deed does not convey title to the grantee until there is a delivery of the deed to the grantee. When the parties deliver the deeds to the escrow agent, they are making what is known as a delivery subject to a condition subsequent. When the condition is satisfied, the escrow agent, acting as the agent of the respective grantor, completes the delivery to the named grantee. Generally, the delivery is completed at that time, and the conveyance of title, whether legal or equitable, becomes effective at that time.

Events can occur between the delivery into escrow and the delivery out of escrow that would logically take precedence and block or prevent the second delivery from becoming effective. For example, the grantor of the particular deed could die, or become incompetent. A judgment lien could attach to the interest of either buyer or seller, and encumber the title arising from the second delivery.

It is the peculiar nature of escrows that none of these events in fact encumber or defeat the second delivery. As stated in chapter 2, through the so-called 'doctrine of equitable conversion', the seller's interest under an executory (not fully performed) contract is considered to be personal property, rather than real property, so that judgment liens against the seller which attach to real estate do not attach to the property being sold. In chapter 12, it is stated that judgment liens against the buyer's interest in the real property are terminated by a default and forfeiture, when the special warranty deed is delivered out of escrow to the seller. How can this be?

The 'Relation Back' Doctrine

Since the early common law, when necessary to prevent frustration of the intention of the parties to an escrow, the courts have indulged in the fiction that the second delivery from escrow 'relates back' in time to the first delivery into escrow, and is given effect from the time of the first delivery. See 28 *Am Jur 2nd Escrow*, section 29. As an early English writer stated the doctrine,

"the second delivery hath all its force by the first delivery, and the second is but an execution and consummation of the first; and therefore in case of necessity, *et ux res magis valeat quam pereat*, it

shall have relation by fiction to be his deed *ab initio*, by force of the first delivery". Butler & Baker's Case, 3 Coke 25a, 76 Eng Reprint 684. Id. (The English writers were fond of validating their conclusions by resort to Latin phrases.)

The doctrine has been invoked to validate a second delivery occurring after the death of the grantor (*Id.*, sect. 31), or after the grantor becomes insane or is otherwise legally incapable of making a deed (*Id.*, sect. 33). Also, voluntary conveyances of title by the grantor to other parties after delivering a deed into escrow are of no effect, and judgment liens attaching to the grantor's interest after the first delivery into escrow are cut off by the second delivery from escrow. *Id.*, sect. 34-35. The doctrine is recognized in New Mexico. See *Mosley*, p. 32, CLA.

In short, as a general rule, after the first delivery into escrow, there is nothing that either the seller or buyer can do, voluntarily or involuntarily, to defeat the title conveyed by the second delivery from escrow. As we will see in chapter 12, the only exceptions are federal tax liens attaching to the buyer's interest in the property and, in New Mexico, mechanics' liens attaching to the buyer's interest when the seller had knowledge of the improvements being made to the property, but failed to post a notice of non-responsibility on the property within 3 days after learning of the work. Both of these liens survive the second delivery from escrow by virtue of statutory law.

Performance of Conditions Precedent to Delivery

Furthermore, the rights of the grantee of a deed delivered from escrow do not depend upon the actual delivery of the deed from escrow to the grantee. A series of New Mexico Supreme Court decisions have established the principal that performance of the actions required to create the grantee's right to delivery of the deed is sufficient to vest the title at the time the required acts are completed, whether or not the deed is actually delivered to the grantee.

Delivery is considered to be complete and title vested upon the completion of performance of all necessary conditions by the party entitled to delivery, and not upon the actual delivery of the deeds by the escrow agent. See *Val Verde*, p. 30, CLA.

The Supreme Court has held that payment of the purchase price to the seller or to the seller's attorney-in-fact is sufficient to vest the legal and equitable title in the buyer, and that manual delivery of the deed from escrow is not necessary to vest the title. See *Albarado*, p. 30, CLA.

When the REC is fully performed by the buyer, the buyer automatically acquires the legal title, and does not have to bring suit to establish that title. Therefore, the six-year statute of limitations on claims to enforce written contracts does not bar a buyer's suit to quiet title, even though the statute would have barred an action on the contract for delivery of the deed. See *Garcia*, p. 31, CLA. In the *Garcia* case, no deeds had ever been placed in escrow!

Delivery Obtained by Fraud

If performance of the conditions required to entitle the grantee to delivery of the deed is sufficient to vest the title conveyed by the deed, regardless of actual delivery, the converse is also true. Failure to perform the required conditions defeats the vesting of title, even though the deed is actually delivered from escrow and recorded, whether by mistake or as the result of a fraud.

If the erroneously delivered deed was obtained from escrow by fraud of one of the parties, then even a subsequent buyer from that party who is unaware of the fraud acquires no title, and the record title can be restored to the victim. See *Otero*, p. 31 CLA and *Mosley*, p. 32.

In the majority of states, the subsequent bona fide purchaser is not protected, even when the unauthorized delivery was not obtained by fraud of the grantee. Some states have ruled otherwise, on the theory that a mistakenly delivered deed is voidable, but not void (in which case the court may exercise its discretion, and weigh the equities). The majority view holds the delivered deed to be void as a matter of law. New Mexico has followed the majority view. See *Roberts*, p. 32, CLA.

Consequences of Erroneous or Premature Delivery

A deed which is delivered and recorded in error conveys no title, and the REC remains in effect. See *Martinez*, p. 32, CLA.

An escrow agent can be liable in damages to a party to the escrow as a result of erroneously or prematurely delivering the escrowed documents. See *Allen*, p. 33, CLA. In *Allen*, where the buyer acquired a deed from escrow by giving the escrow agent an NSF check, the Supreme Court ruled that the erroneously recorded deed conveyed no title to the buyer. The measure of damages was held to be the amount required to quiet the title, or place record title back in the seller. The Court suggested that, had title actually been irretrievably lost by the seller, then the measure of damages would have been the unpaid balance of the purchase price. See also *Buhler*, p. 34, CLA.

Re-establishing the Escrow

Where a deed has been erroneously released from escrow and recorded, and the parties have agreed to 'reinstate' the REC, the general practice has been to prepare a new REC with a new set of deeds and establish a new escrow. This procedure is probably not necessary. Where a forfeiture was wrongfully declared and the special warranty deed was released from escrow and recorded, the Supreme Court ordered the parties to place the

special warranty deed back in escrow, and to prepare an appropriate instrument evidencing that the deed had been delivered and recorded in error. See *Ortiz*, p. 40, CLA. The *Martinez* and *Ortiz* decisions hold that the REC remains in effect, and that the erroneously delivered and recorded deed conveys no title, and is therefore still entitled to be in escrow.

It would appear to be sufficient to record an affidavit establishing the facts of erroneous delivery and recording, stating that the REC and the escrow remain in effect, and that the deed has been returned to escrow. The escrow agent would be the appropriate party to make the affidavit, either on its own initiative or pursuant to an agreement of the parties, because only the escrow agent is in a position to disavow the validity of its delivery of the deed.

The difference in procedures used to re-establish the escrow is important, because of the effect of the 'relation-back' doctrine. If the original REC and the escrow remain in effect, then a later delivery from escrow of either deed will relate back to the time of the original delivery into escrow, and thereby cut off any intervening liens established against the granting party. If a new contract and deeds are prepared and placed in escrow, the new contract will be junior in priority to any intervening liens, because the parties by their new agreement will be held to have abandoned the original contract and any title priority it may have had.

Effect of Exculpatory Clause in Escrow Agreement

A bank, when acting as an escrow agent can by agreement limit its liability to losses caused by its willful or gross negligence. In the *Lynch* case (p. 34, CLA), the Supreme Court held that a bank could contractually limit its liability when acting as an escrow agent. While exculpatory clauses 'are not favorites of the law', they will be upheld unless there is a showing of an absence of alternative service providers, or unless the clause has the effect of exempting a party from the performance of a public duty. Since the bank's escrow department was not performing a banking function, it was not performing a regulated activity. The Court observed that there was no regulation of the escrow business in New Mexico; therefore the escrow business could not be considered a 'public service'.

One year after the *Lynch* decision, the Legislature enacted the Escrow Company Act. Although banks are exempted from the coverage of the Act, the Act served the important function of bringing escrow services within the category of a regulated public service. Because the logical underpinning of the *Lynch* decision has been removed, it seems unlikely that the Court would allow either a bank or a regulated escrow company to enforce an exculpatory clause in today's environment.

Conflicting Demands on Escrow Agent

It frequently happens that the escrow agent is trapped between conflicting demands made

upon it by the parties to the escrow. For example, the parties may disagree as to whether the buyer has complied in a timely manner with a demand letter issued by the seller. If compliance was not timely, the seller would be entitled to delivery of the escrowed deeds. If timely, the buyer would be entitled to continue making payments and to delivery of the deeds upon payment in full. The escrow agent often resolves such conflicts by interposing its own judgment; however, it does so at peril of being sued by the dissatisfied party.

The escrow agent is not required to interpret its instructions, or to resolve conflicts between the parties. See *Davisson*, p. 35 and *Dunlap*, p. 34, CLA. It may file suit against both parties, asserting that conflicting demands have been made upon it, require the parties to interplead their claims, and ask the Court to determine the rights of the parties. This procedure is authorized by Rule 22, New Mexico Rules of Civil Procedure for the District Courts when the claims of the defendants "...are such that the Plaintiff is or may be exposed to double or multiple liability." The interpleader remedy is also given to licensed escrow agents by the Escrow Company Act, and by provisions contained in the RANM REC form. The escrow agent is authorized to collect its court costs and attorney fees from either or both parties to the escrow.

Duties of Principals to Escrow Agent

Duty To Make Payments Through The Escrow Agent

The RANM forms explicitly require all equity payments to be paid to the escrow agent, including equity payments which "wrap" senior encumbrances. The forms allow the parties to formally elect whether assumed senior encumbrances will be paid through escrow or outside of escrow. Preparers who use form 103 or a note secured by mortgage or deed of trust customarily insert language in those forms clarifying the buyer's responsibility as to direction of payments.

Duty to Inform

The RANM form obliges the buyer to notify the escrow agent by written statement of a change of address. A similar duty is implicit in any other form of REC. The RANM form also requires the seller to send a copy of any default notice to the escrow agent. While there is no explicit requirement in form 103, it is probable that a seller who fails to provide a copy of a default notice to the escrow agent cannot complain if the escrow agent fails to collect seller's attorney fee or allows the buyer to pay less than the number of payments in default.

Duty to Document Change of Legal Status

Upon the buyer's failure to comply with a default notice, the seller should provide a copy of a recordable "Affidavit of Uncured Default and Election of Termination" to the escrow agent. Neither of the standard forms expressly requires this action; however, it is the only action that obligates the escrow agent to recognize the seller's right to possession of the special warranty deed.

If the buyer sells or assigns his interest in the property or REC, he is required by the RANM form to provide a copy of the document to the escrow agent, specifying the address of the assignee. The form imposes a corresponding duty on the seller to contact the escrow agent to verify the current name and address of the buyer or buyer's assignee as shown on the escrow agent's records before mailing a notice of default.

Duty To Pay Fees

The RANM form entitles the escrow agent to collect its standard fees current as of the date services are rendered. The escrow agent may change its fees after 60 days advance written notice to the party or parties paying the fee.

Duty to Indemnify

The RANM form requires the parties to indemnify the escrow agent against all costs, damages, attorney's fees, expenses and liabilities which it may incur or sustain in connection with the contract, including any interpleader suit. When form 103 is used, the law would probably provide a similar result in the case of an interpleader suit.

Duty to Select Successor Escrow Agent

An escrow agent may resign its position upon notice to the parties. This action does not terminate the escrow, but it does oblige the parties to agree upon a new escrow agent, and so advise the resigning agent. Under the RANM form, failure to appoint a new agent within 60 days authorizes the resigning escrow agent to make the selection and deliver the escrowed papers to the new agent. When a deed of trust is used, a trustee may resign and, upon failure of the parties to appoint a new trustee, the Sheriff of the county where the property is located automatically becomes the new trustee, by operation of statute. *Section 47-1-42, NMSA 1978.*

Buyer Default

Under the standard forms of REC, there are a wide variety of acts and omissions of the buyer that may constitute an event of default. If an event of default has occurred, and if the buyer has not filed for protection under the federal bankruptcy laws, the seller, if he has the standing and capacity to enforce the REC, may give a notice of default to the buyer. Requirements of form and content of the notice have been established by the REC and various federal and state laws and court decisions. If the seller has given notice of default in the form and manner required to all the persons who are entitled to notice, and if the default is not cured within the required amount of time, then the seller may elect one of the alternative remedies available to him, provided the criteria for imposition of the remedy have been satisfied.

Events of Default

The following acts or omissions of the buyer are declared by the standard RANM form to be events of default, for which the seller may pursue his remedies:

- failure to make payments on the debt to the seller as required by the contract;
- failure to make payments on an assumed obligation in accordance with its terms;
- failure to pay property taxes or other assessments as they become due;
- failure to reimburse seller for payment of delinquent taxes;
- failure to maintain hazard insurance as required by the contract;
- failure to reimburse seller for insurance premiums advanced to protect the property;
- selling or encumbering the property without seller's prior written consent, if required.

Refusal to consummate; repudiation.

In addition to the events of default defined by the REC, the buyer may be in default by failing or refusing to close on a sale after signing a binding purchase agreement obligating him to execute a REC or mortgage, make the down payment and take possession of the property. After entering into a binding contract, the buyer may also default by repudiating the contract and refusing to perform its obligations.

A buyer who refused to consummate a purchase agreement requiring him to execute the required closing documents and pay the amounts due was held liable to the seller for the costs incurred in selling the property to another party. See *Roberson Construction Company*, p. 36, CLA.

Where a buyer signed a contract to purchase a furnished motel but repudiated the contract and

returned possession of the property to the seller after operating the motel for only 8 days, the Supreme Court held that the seller could recover the full contract price less the market value of the property at date of breach, and less any payments received. See *Aboud*, p. 36, CLA. This is known as the 'loss of bargain' rule of damages.

Timeliness. As to all the obligations of the buyer and seller under the terms of the REC, it is the general rule that the parties have a reasonable time to perform their respective obligations, unless the contract contains a 'time is of the essence' clause. Both the RANM forms and form 103 contain the clause, so timeliness of performance is a strict requirement. When any obligation is not performed on or before the required date, the delinquent party is considered to be in default. See *Petrakis*, p. 53, CLA.

Failure to make equity payments. This is easily the most common form of buyer default. REC's generally require that the buyer pay a specified amount, 'or more', in monthly, quarterly or annual installments. There may also be provisions for additional 'balloon' payments. The 'or more' phrase has been a source of contention when buyers in default have attempted to claim that overpayments made in the past should be credited to currently past-due payments in order to avoid a default.

The Supreme Court held in 1968 that overpayments in one period do not relieve the buyer from the obligation to pay 'the specified amount on each and every payment date thereafter'. See *DeVilliers*, p. 37, CLA. However, this decision predated the RANM form, which contains the provision that 'all payments shall be assumed to be regular payments, and not prepayments, unless otherwise specified by Purchaser in writing at the time of delivering such payments to Escrow Agent'. Thus, if the excess portion of the payment is equal to or greater than the minimum regular payment amount, the RANM form requires that the excess amount be treated as a regular payment, and not as a prepayment, unless the buyer instructs the escrow agent otherwise in writing at the time of delivering the payment to the escrow agent. If the excess portion of a payment is less than the minimum regular payment amount, it must be credited as a prepayment. The *DeVilliers* decision requires that such prepayments, and all prepayments made on a form 103 REC, regardless of amount, may not be used to reduce or eliminate a future scheduled payment.

Failure to make payments on an assumed obligation. The Appeals Court has questioned whether failure to make payments on an underlying assumed mortgage or REC would constitute an event of default. See *Ott*, p. 38, CLA. However, the doubt expressed by that Court in 1976 could probably be disregarded. In 1967, the Supreme Court had already held that the buyer remains liable to the seller for performance of his promise to pay an assumed obligation, even after the debt to the seller is paid in full and the warranty deed is delivered from escrow and recorded. See *Kuzemchak*, p. 12, CLA. In 1977, the Supreme Court held that a REC requiring the buyer to assume and pay a first mortgage was enforceable, but disallowed a forfeiture because the default notice was 'premature'. The seller's attorney had mailed the notice before the expiration of an extension granted by the mortgagee to the buyer to cure a delinquency. See *Eiferle*, p. 39, CLA.

The RANM forms, first adopted in 1981, specifically declare that 'failure to make such payments at the time required shall be a default under this Contract'. The provision is

applicable whether the assumed payments are made ‘outside escrow’ or through the escrow agent. **Drafting suggestion:** form 103 does not contain a similar provision, so additional language should be added to the form when the buyer is assuming an existing obligation.

Failure to pay property taxes. The first half of annual property taxes is due November 10, and is considered to be delinquent after December 10. The second half is due the following April 10, and is considered delinquent after May 10. The 1981 RANM form requires the buyer to have the property assessed in his own name for taxation, and to send copies of paid tax receipts each year to the seller. However, failure to do either of these things is not declared by the contract to be a default. The event of default consists in the failure to pay the taxes. See the full discussion of property taxes in chapter 6.

Failure to reimburse seller for payment of delinquent property taxes. This is an event of default under both the RANM forms and form 103. See the full discussion in chapter 6.

Failure to maintain hazard insurance or reimburse seller for premiums advanced. Under the RANM forms, failure to maintain insurance is defined as an event of default. However, it is not an event of default under form 103. See *Boatwright*, p. 14, CLA. If form 103 is used, the seller must pay the insurance premiums, then demand reimbursement under the provisions of paragraph 8. For more discussion, see chapter 6.

Selling or encumbering the property without seller’s prior written consent. If the parties have made paragraph 7(B) of the 1981 RANM form applicable, then violation of that paragraph by the buyer is defined as an event of default. That provision prohibits any sale, assignment or encumbrance by the buyer of all or any portion of his interest in the REC or in the property without first obtaining the written consent of the seller. Form 103 purports to void any assignment of the buyer’s rights in the REC without the seller’s prior written consent. However, the contract form fails to state that any such assignment is an event of default for which the seller may invoke the remedies of the contract. In any event, the clause is probably unenforceable as a prohibited restraint on alienation. For full analysis, see chapter 7, *Restraints*.

Notice of Default

Requirement for notice.

By agreement, the parties may provide that upon default title documents will be delivered from escrow without notice or demand. Where there is no requirement in the contract for notice, the Supreme Court has upheld an ‘automatic’ forfeiture, stating that it will not rewrite the agreement for the parties. See *Melfi*, p. 39, CLA. Provisions for forfeiture without notice are very rare, however. They are sometimes added to REC’s by amendment after the seller has allowed a defaulted buyer to reinstate the contract. Under such circumstances, the buyer has lost all his bargaining power, and is willing to agree to the

'no-notice' provision as a condition to reinstatement of the contract.

Form 103 and the RANM forms require the seller to mail a written demand letter to the buyer after an event of default occurs, and to wait for a specified period of time thereafter for the buyer to cure the default. After the waiting period has elapsed, the seller may make an election of remedies and proceed to enforce his rights.

If the seller establishes a pattern of granting extensions of time to the buyer for compliance with demand letters or accepting partial cure of the default, he may be held to have waived his right to strict enforcement of a subsequent demand letter, unless he first puts the buyer on notice that no more extensions or partial cures will be granted. See *Nelms*, p. 27, CLA.

If notice of default is required by the contract and the seller fails to give the required notice, the contract remains in effect. The Supreme Court held in 1977, before passage of the federal tax lien 'survival' law (see below), that where a seller failed to give a notice of default to the buyer, a federal tax lien could attach to the defaulting buyer's equitable title. See *MGIC Mortgage Corp.*, p. 6, CLA.

Who may send the demand letter? The seller or his agent (his lawyer or the holder of the seller's power of attorney), or the seller's assignee or his agent may issue a demand letter. When a non-lawyer agent is used, a power of attorney showing his authority should be recorded, and a copy of the recorded Power furnished to the escrow agent. It would be a good idea to attach a copy to the original demand letter, too, so the buyer cannot question the agent's authority.

The demand letter may be mailed only by the current owner of the contract rights. A demand letter mailed by a former owner of the REC who had assigned his contract rights to another party was not enforceable. See *Graham*, p. 40, CLA.

Who is entitled to notice?

Buyer named in the contract. In every case, a demand letter must be mailed to the buyer(s) named in the contract. See *Nelms*, p. 27, CLA. Even if the buyer has resold the property with the seller's consent, the buyer remains liable on the contract and owns a reversionary interest in the property, and therefore is entitled to notice.

Sub-purchasers. If the buyer has sold his interest in the property to a sub-purchaser with the seller's written consent, then the seller is also obliged to send a copy of the demand letter to the sub-purchaser. But what if the buyer sold his interest to a sub-purchaser without the seller's consent? Some sellers have chosen to ignore the sub-purchaser and not send a copy of the demand letter to him. In 1980, the Supreme Court gave its approval to this procedure, holding that since the seller has no contract with the sub-purchaser, he has no legal duty to provide him with a notice of default. See *Campbell*, p. 41, CLA. In a

confused decision in 1986, the Court ruled that a sub-purchaser who had paid off his contract with the buyer was entitled to notice. See *Martinez v. Logsdon*, p. 42, CLA. The Court's position became considerably clearer in 1992, when it ruled that **'a vendor with knowledge of a subvendee's interest in property subject to the contract, cannot declare a forfeiture of the subvendee's interest without giving the subvendee notice of default and an opportunity to cure'** (emphasis added). See *Yu*, p. 43, CLA.

Assignees/grantees. Buyers sometimes deed the property to a third party, having been 'cashed out' of their equity in the property. The deed may or may not be accompanied by an assignment of contract rights. These cases are different from a sub-purchaser who buys the property on a junior REC, because the original buyer does not retain a reversionary interest in the property.

The Supreme Court held in 1979 that the grantee/assignee of the buyer's interest is entitled to notice of default before the seller can terminate the REC. See *Ortiz*, p. 40, CLA. The odd thing about this decision is that the Court apparently ignored it a year later in the *Campbell* decision. Fortunately, the entire matter was cleared up in 1992 by the *Yu* decision.

The Court held in 1982 that it is not necessary to send a demand letter to the original buyer. Because the buyer has divested himself of any interest in the property, an election to terminate the contract would affect only the assignee/grantee, and would not be prejudicial to any rights of the buyer. See *Albuquerque National Bank*, p. 45, CLA. However, this case should not be relied upon if the seller intends to elect the acceleration remedy, and enforce payment of the debt. The Court was dealing with a forfeiture of the buyer's interest in the land, under circumstances where the buyer had already divested himself of all title interests in the land. It would not be reasonable to expect that the Court would excuse a lack of notice of default and opportunity to cure, where the seller intends to accelerate the unpaid balance under the terms of the REC. In that situation, the buyer's lack of a title interest in the property would be irrelevant.

Collateral assignees. The buyer's equitable title interest under a REC is mortgageable, and can therefore be used as collateral for a loan. However, recordation of the lender's equitable mortgage is not sufficient to put the seller on constructive notice of the lender's interest in the property. If the lender has given the seller written notice of the lender's mortgage, then the lender is entitled to notice of default, and a copy of the demand letter must be sent to the lender, and an opportunity given to cure the default. See *Shindledecker*, p. 6, CLA.

Practice suggestion: Lenders frequently send a copy of their mortgage or security agreement to the escrow agent, and ask to be notified if the seller mails a demand letter to the buyer. While this is a good idea, it is not sufficient to protect the lender. Sellers and their attorneys sometimes fail to send a copy of the demand letter to the escrow agent. Escrow agents might fail to notify the lender when a

copy of a demand letter is received. It is very doubtful whether the escrow agent has any obligation to notify the lender, because there is no contract between the escrow agent and the lender, and the lender pays no consideration to the escrow agent for this service. The lender should also send a copy of its mortgage to the seller, and request that it receive a copy of any demand letter mailed to the buyer.

Assignees of the buyer's interest in a junior REC. When the buyer resells the property on a junior REC, the buyer becomes the *seller* or owner of the junior contract. It has become common practice for the buyer/seller to sell his interest in the junior REC to an investor, who acquires the right to receive payments from the sub-purchaser, but accepts no responsibility for performance of the senior REC. Is the investor/assignee entitled to notice of default? Although the investor's primary interest is in the proceeds of the junior contract, the investor does hold a reversionary interest in the equitable title. If the sub-purchaser defaults, the investor can acquire the equitable title to the property, subject to the senior REC. That means the investor is essentially in the same position as a mortgagee of the buyer's interest in the property. It follows from the *Shindlegdecker* decision that the investor is entitled to notice of default if the seller has been given notice of the investor's interest in the property.

Escrow Agent. Finally, a copy of the demand letter should be provided to the escrow agent, and if a junior contract exists, to the escrow agent named in that contract. The RANM forms expressly require that a copy of the demand letter be sent to the escrow agent. Timing is critical. If payment is made to the escrow agent before it receives a copy of the demand letter, the escrow agent is not obliged to enforce any demand for attorney's fees contained in the letter. **Practice suggestion:** fax a copy of the demand letter to the escrow agent on the same day the letter is mailed.

Internal Revenue Service.

--- Pre-1986 law. Until 1986, tax liens of the United States enjoyed no greater priority than any other lien attaching to the REC buyer's interest in the property. When the seller gave notice of default to the buyer and subsequently terminated the REC, all liens attaching to the buyer's interest in the property, including federal tax liens, were terminated by the forfeiture. See *MGIC Mortgage Corp.*, p. 6, CLA.

--- Tax Reform Act of 1986. Section 7425 of the Internal Revenue Code (IRC) had long provided that federal tax liens filed against property more than 30 days before a judicial sale of the property would survive the sale unless notice of the sale was given to the Secretary of the Treasury at least 25 days prior to the sale, in which case the U.S. would have a right of redemption. However, federal appellate courts in the state of Washington had held that the law did not apply to land contract forfeitures, because they were not 'sales'. The Tax Reform Act of 1986 amended the law to provide that '...a sale of property includes any forfeiture of a land sales contract'. The amendment took effect on November 22, 1986.

---Date of 'sale'. By regulation, the 'sale' occurs when junior liens are divested under local law. See *26 CFR sect. 301.7425-2(b)(3)*. In the case of REC's in New Mexico, that occurs when the seller elects to terminate the REC. Normally, the election is made when the seller presents an affidavit of default to the escrow agent and takes delivery of the special warranty deed from escrow.

---Qualified tax liens. The notice provisions of section 7425 apply to any federal tax liens recorded in the county clerk's office *more than 30 days* before the date the seller makes an election to terminate. It thus becomes important for the seller to document the date of the election, perhaps by obtaining a date-stamped copy of the affidavit of default and election to terminate from the escrow agent.

---Notice requirement. Written notice of the sale must be given by certified or registered mail, or by personal service, to the district director of the Internal Revenue Service for the district in which the sale is to be conducted, marked to the attention of the chief, special procedures staff, at least 25 days before the sale (date of election). *26 CFR sect. 301.7425-3(a)*. Notice is effective as of the postmark date on the envelope. [*Sect. 7502 I.R.C.*] By regulation [*26 C.F.R. sect. 301.7425-3(d)(1)*], the notice must contain the following information:

- the name and address of the person sending the notice;
- a copy of the Notice of Federal Tax Lien (form 668) or the following information as shown on the Notice:
 - the internal revenue district named thereon,
 - the name and address of the taxpayer, and
 - the date and place of filing of the notice;
- a description of the property to be forfeited, which must include the street address, city, state and the legal description contained in the title or deed to the property;
- the date, time, place and terms of the proposed sale (since this is not a sale, it would probably be sufficient to state that the seller will elect to terminate the REC and declare a forfeiture of all the taxpayer's right, title and interest in the subject property as full and complete satisfaction of the unpaid debt).
- the approximate amount of principal, interest and other expenses 'which may be charged against the sale proceeds'. In the case of a REC forfeiture, this would probably include the attorney fee for the demand letter and the escrow agent's closeout fee. It would not include any late charges due under the terms of the REC, because late charges are not an 'expense of sale'.

---Right of redemption. The U.S. has the right to redeem the property (i.e., buy it) for a period of 120 days after the date of sale (date of election). If the U.S. elects to redeem, it must pay the seller the unpaid principal balance of his equity, 6% per annum interest from the date of sale (date of election) and certain allowable expenses. *28 USC sect. 2410(d)*. The U.S. is not required to pay for any improvements made to the property by the seller after forfeiture. However, the U.S. will pay for the excess of any 'expenses necessarily incurred in connection with the property' over any

income from the property. Qualifying expenses include repair and maintenance, utilities, and a proportionate amount of casualty insurance premiums and ad valorem taxes. The U.S. will also pay for any payments of principal and interest made to the holder of a senior lienholder after the date of sale (date of election). *26 CFR sect. 301.7425-4(b)(3-4)*.

---Termination of right of redemption. If the U.S. does not elect to redeem the property within the allowed 120-day period, then the redemption right terminates, and the seller's title is no longer encumbered by the redemption right.

---Effect of failure to notify. If the requisite notice is not given to the IRS, or if the notice is defective for failure to give the required information, the tax lien survives the forfeiture. A number of federal court decisions have held that the tax lien, while it is not extinguished by the forfeiture, is not elevated in priority, and retains its status as junior to the seller's lien.

Practice suggestions.

- Because the regulations require that the notice to the IRS contain a copy of the federal tax lien, it is necessary to conduct a tax lien search before sending the notice. This costs money, so it is impractical to conduct a tax lien search every time a demand letter is mailed to the buyer. It would be better to wait until the notice period specified in the REC has expired after mailing the written demand, then order a tax lien search before picking up the special warranty deed from the escrow agent, and before delivering an affidavit of default to the escrow agent.
- If the search report shows no tax liens of record, then the seller can safely deliver the affidavit to the escrow agent and pick up the special warranty deed. If a tax lien is revealed by the search, and if it was recorded more than 30 days earlier, the notice procedure should be followed.
- It is debatable whether it is necessary to send a new demand letter to the buyer. The statute requires only that notice be given to the IRS at least 25 days prior to the date of sale (date of election). Therefore, it is probably not necessary to send another demand letter to the buyer, thereby giving the buyer more time to cure the default. It is only necessary to wait at least 25 days after the notice is mailed to the IRS before picking up the special warranty deed from escrow.
- The seller must wait until the IRS notifies him that it does not intend to redeem the property, or until the expiration of 120 days after the date of sale (date of election), before reselling the property.
- The seller would be well advised to think twice before accepting a voluntary termination of the REC by the defaulting buyer. A mutual agreement to rescind and terminate the REC would not constitute a 'judicial sale' or a forfeiture as defined in the I.R.C. Therefore, the entire code section is probably not applicable. Since the conveyance to the seller is made pursuant to the rescission agreement, and not under the terms and conditions of the REC, the seller almost certainly would be taking the equitable title subject to the IRS tax lien. The only way the seller could protect himself would be to order a tax lien search before entering into the rescission agreement. If a tax lien is disclosed by the search report, then the seller should follow the

notice and termination procedure under the terms of the REC, and give the required notice to the IRS.

Where should the demand letter be mailed?

The RANM forms and form 103 state that the demand letter is effective on the day it is mailed, whether or not the buyer actually receives the letter. However, since the remedy of non-judicial forfeiture is equitable in nature, there is an implicit requirement that a good faith effort be made to give actual notice of default to the buyer. Therefore, the demand letter should be mailed to the buyer:

1. to buyer's address as shown in the REC, or
2. to any subsequent address communicated in writing by the buyer to the seller or to the escrow agent, or
3. to any address where the seller has actual knowledge that the buyer may be reached.

When the demand letter is being mailed by a debt collector on behalf of the seller, the federal *Fair Debt Collection Practices Act* prohibits communication with the consumer (buyer) without his prior consent at his place of employment if the debt collector knows or has reason to know that the consumer's employer prohibits the consumer from receiving such communication. See Requirements of the Fair Debt Collection Practices Act, below.

The FDCPA also prohibits direct communication with the consumer if the debt collector knows that the consumer is represented by an attorney *with respect to the debt* and has knowledge of, or can readily ascertain, the attorney's name and address, unless the attorney fails to respond within a reasonable period of time to a communication from the debt collector or unless the attorney consents to direct communication with the consumer.

The 1981 RANM form requires that the demand letter be mailed to the buyer at the address designated in the REC or at such other address that the buyer may designate by a notarized statement delivered to the escrow agent, and provides that the change of address will be effective on the seventh (7th) calendar day after receipt by the escrow agent. The new RANM form requires that the change of address notice be signed and in writing, but the notarization requirement and the 7-day delay as to effectiveness are deleted.

Form 103 contains no provision for the buyer to give a change-of-address notice to the seller or to the escrow agent. Fortunately, common sense and the requirement to demonstrate good faith usually govern. Most escrow agents will refuse to recognize the validity of a demand letter mailed to a buyer's former address when the escrow agent's records reflect a properly documented (written) change of address, unless the letter is actually received by the addressee. Of course, if the seller can prove that the buyer actually received the demand letter at any address, then it would not be necessary to show the mailing to any other address. See *ANB v. Albuquerque Ranch Estates, Inc.*, p. 45, CLA.

Choice of mail service.

The RANM forms require that the notice be sent by certified mail, return receipt requested. Form 103 does not require any particular type of mail service to be used. The seller will usually be required by the escrow agent to produce some proof of mailing, and it is obviously preferable to the seller to be able to prove actual delivery of the letter to the buyer. Certified mail with return receipt requested is therefore the best choice. Some attorneys go a step further and send a duplicate original of the letter by first class mail. If the buyer fails or refuses to accept the certified delivery, and the duplicate original is not returned undelivered by the postal service, these facts can be recited in seller's affidavit of default. The seller is thereby aided by the legal presumption of delivery of a first class letter that is not returned. As noted below, it is not necessary to prove actual delivery of a notice properly mailed. Nevertheless, any special effort made by the seller to give actual notice of default to the buyer demonstrates good faith, and will weigh in his favor in any subsequent litigation where the Court's decision may turn on issues of fairness and good faith.

Effective date of demand.

A demand letter cannot start the 30-day cure period running until after the required payment or other performance is past due. However, the demand is not invalid because it is mailed on the same day that the payment being demanded becomes due. The Supreme Court has held that such a demand letter would be 'given effect as a demand made upon the first day of default' and that 'it would start running of the 30-day period of default, within which payment could be made, with the very first day of default'. See *Petrakis*, p. 53, CLA.

Both RANM forms and form 103 all state that a demand letter is effective when it is mailed. So does a certified mail receipt signed by the buyer two days later change the effective date? No! The signed receipt merely proves that the buyer received the letter, and therefore had an opportunity to be aware of and comply with the demand letter requirements.

The terms of the demand letter itself can, however, change the effective date of the demand. Clearly, if the letter says "unless you comply within thirty days after receipt of this letter..." then the seller will be required to prove delivery of the letter, and the thirty days time limit will not begin to run until the buyer receives the letter.

Also, ambiguity in the letter itself can change the effective date. In the *Ott* decision (see p. 38, CLA), the demand letter said "if (15) days from the effective date of this notice..." The Appeals Court ruled that, since the terms of the letter were not clear, the question would be resolved in favor of the buyer, and the words 'effective date' would be construed to mean the date of receipt. Since the letter was returned unclaimed, the demand never became

effective.

Deadline for compliance.

If the demand letter by its terms requires cure of default within, say, 30 days, this would normally mean that the last day on which the buyer can cure the default is the 30th day following the date the letter was mailed. The day of mailing is not counted. Thus, if the demand letter was mailed on March 15, the final date for compliance would be April 14 (March has 31 days).

But what if the deadline falls on a Saturday, Sunday or holiday or a day when the escrow agent is closed for business? The 1981 RANM form expressly provides:

“ If the final day for curing the default shall fall on a Saturday, Sunday, or non-business day of the escrow agent, then the period for curing the default shall extend to the close of business on the next regular business day of the escrow agent. ”

Note that no extension is given if the deadline falls on a holiday, unless the escrow agent is closed for business on that day. The new RANM form addresses this problem by substituting the phrase “....If the final day for curing the default falls on a non-business day of escrow agent,”. Form 103 makes no provision for extensions of deadlines to cure defaults. However, most escrow agents will accept a tendered cure of default on the next regular business day when the deadline falls on a Saturday, Sunday or other day when the escrow agent was closed for business. The practice is so universal that it could constitute a standard of the industry established by custom.

Drafting suggestion.

The language of the letter should clearly state the number of days from the date of the letter within which the buyer must comply. Better yet, it should specify the date by which compliance is required, to avoid the buyer's claim that he didn't realize the month contained 31 days. The seller should be prepared to prove the date of mailing (an unclaimed certified mail envelope with postmark is the best evidence).

Contents of the demand letter.

Requirements of the contract.

The RANM forms require that the demand letter specify the default and the curative action required. Form 103 contains no requirement as to content. The Supreme Court has held that the provisions of the contract govern the requirements for notice of default. See *ANB*, p. 45, CLA. In that case, where a form 103 was used, the Court ruled that the seller had no duty to reiterate the amounts required to be paid under the contract.

When one of the RANM forms is used, the demand letter should:

- state the nature of the default and the performance required to cure;
- specify the deadline for compliance;
- state a demand (not a request) for performance;
- specify the place of performance of the actions demanded (in the escrow agent's office, not in the seller's attorney's office or some other place); and
- state that noncompliance will result in the seller electing a remedy under the contract.

Requirements of the Fair Debt Collection Practices Act.

Congress enacted the FDCPA in 1977 'to eliminate abusive debt collection practices by debt collectors'. The Act is found at *41 U.S.C. sect. 1692*. The requirements of the Act apply to any person '*who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another*'. The Act thus applies to an attorney who sends a demand letter on behalf of a seller to a buyer under a REC.

The Act requires that a debt collector, as defined in the Act, send a written notice to the consumer containing the following information, either in the initial communication to the consumer in connection with the collection of the debt, or within five days after the initial communication:

1. The amount of the debt;
2. The name of the creditor to whom the debt is owed;
3. A statement that unless the consumer, within thirty days after receipt of the notice, disputes the validity of the debt, or any portion thereof; the debt will be assumed to be valid by the debt collector;
4. A statement that if the consumer notifies the debt collector in writing within the thirty-day period that the debt, or any portion thereof, is disputed, the debt collector will obtain verification of the debt or a copy of a judgment against the consumer and a copy of such verification or judgment will be mailed to the consumer by the debt collector; and
5. A statement that, upon the consumer's written request within the thirty-day period, the debt collector will provide the consumer with the name and address of the original creditor, if different from the current creditor.

If the consumer notifies the debt collector in writing within the 30-day period that any portion of the debt is disputed, or that the consumer requests the name and address of the original creditor, then the debt collector is required to cease collection of the debt until the debt collector mails a verification of the debt or the name and address of the original

creditor to the consumer.

Any violation of the Act subjects the debt collector to civil liability to the consumer for any actual damages sustained, plus additional damages as the court may allow up to \$1,000, plus costs and reasonable attorney fees.

Model demand letter.

The following demand letter is based upon a simple contract (no senior encumbrances) using a RANM form, incorporating statements required by the Fair Debt Collection Practices Act:

January 15, 1998

Sam Smith
1000 Manana NE
Albuquerque, New Mexico 87110

Dear Mr. Smith:

Please be advised that this office represents Jerry Jones and Martha Jones, who are the sellers named in a real estate contract dated April 15, 1995 wherein you are buying the house and lot at 1000 Manana NE. I am advised by the escrow agent that the payment of \$200.00 which was due on January 1, 1998 has not been received.

Demand is hereby made that you make the January payment in the amount of \$200.00, plus \$75.00 as an attorney fee for making this demand. Your payment must be received by Security Escrow Corporation, 1721 Girard NE, Albuquerque NM 87106 on or before February 17, 1998. The escrow agent is hereby instructed to accept no less than the sum of \$275.00 from you.

Unless you dispute the validity of this debt or any portion thereof within 30 days after the date of this letter, we will assume the debt to be valid. If you notify this office in writing within 30 days after the date of this letter that you dispute the debt or any portion thereof, this office will obtain verification of the debt and mail the verification to you. Upon your written request within 30 days after the date of this letter, this office will provide you with the name and address of the original creditor, if different from the current creditor.

Your disputing of any portion of this indebtedness does not extend the deadline for payment to the escrow agent. If you fail to pay said sums to the escrow agent as herein demanded, the seller may elect to either terminate the contract and evict you from the property, or to declare the unpaid balance of your contract to be then due and payable, and sue to collect said balance.

Please be advised that this letter does not cancel or extend the deadline for compliance with any previous demand already sent to you.

Sincerely,

Barney Barrister
Attorney at Law

cc: Security Escrow Corporation

Anticipatory demands.

Sellers sometimes demand not only the payment that is past due, but also any additional payments that will become due before the expiration of the 30-day period. In other words, the demand requires the buyer to be current within 30 days. Such a demand is invalid, and should not be enforced by the escrow agent (although the escrow agent should enforce the valid portion of the letter). Form 103 and both RANM forms allow the seller to terminate the contract only if the buyer fails to make a required payment at the specified time and continues in default for a specified number of days after written demand for such payment has been mailed to him. In short, demand cannot be made for a payment that is not past due at the time the demand is made.

The *Petrakis* decision (see 'effective date', above) makes it clear that where the contract provides a period of time after notice for the buyer to cure a default, that period of time cannot be shortened by mailing a demand letter before the default occurs. Even if the Court would be inclined to give effect to the anticipatory type of demand described above, it would allow the buyer a period of 30 days after the second payment becomes due to make that payment.

The standard forms allow the seller to collect attorney fees only if the contract is placed by the seller in the hands of an attorney upon default for the purpose of mailing the demand letter. When the seller does not employ an attorney to send the letter, he is not entitled to collect an attorney fee.

Demand letters returned undelivered.

The seller's chances for having the forfeiture upheld by the Court will be improved if he can show that failure of delivery of the letter resulted from some neglect or willful action of the buyer, and not from the fault of the seller or the postal service. Letters returned undelivered by the postal service are usually rubber-stamped to show the reason for non-delivery. Depending upon the indicated reason, it may be necessary for the seller to take further action. Following are some examples of reasons for non-delivery, and their significance for the demand letter.

Refused or Unclaimed. Indicates the buyer's willfulness in avoiding the obligation or his neglect, especially if other demand letters have been sent in the past. No further action is required. Try sending another copy of the letter uncertified, by first-class mail. If it isn't returned, the Court may indulge the presumption that the letter was delivered to the addressee.

Not at this Address or Unknown. Indicates someone is there, who claims not to be the addressee. No further action is required. Check the phone directory. Compare notes with the escrow agent. Has the buyer re-sold, assigned his contract, or rented the property to a

tenant? If so, add the name of the assignee or tenant to the demand letter, and re-mail to the tenant. Does the escrow agent have a new address for the buyer? If not, does the escrow agent know what title company handled the re-sale closing? If so, the seller should contact the closing officer, to see if he/she has the buyer's forwarding address.

Not Deliverable as Addressed. May indicate an error by the seller or the escrow agent in transcribing the address. It may (and often does) indicate an inexplicable failure of the postal service to deliver the letter to a valid address. Either way, the seller must make further efforts to deliver the letter. Mail it again. Send an additional copy by first-class mail. If necessary, use a process server!

Election of Remedies

Under the RANM forms and form 103, the seller has two remedies available to redress a breach of contract by the buyer.

1. *He may rescind (terminate) the REC, retain all previous payments as liquidated damages for the use of the property, and recover possession of the property (non-judicial forfeiture).*
2. *He may declare the unpaid balance of the purchase price as due, and file suit to collect (acceleration).*

There is a third remedy which the Supreme Court has recognized, but it must be provided for in the contract in order to be available to the seller: repossession of the property and legal foreclosure with a right to recover any deficiency not realized in the foreclosure sale. See *Graham v. Stoneham*, p. 45, CLA. Since I have never seen this option included in any REC, it will not be discussed here.

The remedies are mutually exclusive. The seller cannot repossess the property, then sue for the unpaid balance. See *Graham*, above. Nor can the seller, after electing to rescind the REC, sue the buyer on a separate promissory note for an unpaid part of the down payment. See *Davies*, p. 46, CLA.

Practice suggestion. Because of the *Davies* decision, any attempt to use a separate note for any part of the purchase price as stated in the REC runs the risk that the note will be held to be unenforceable after a forfeiture of the REC. This problem could be avoided by creating the REC and the secured note as totally separate instruments, each representing a portion of the purchase price. If this is done, then a provision should be included in the REC that a default of the note & mortgage will constitute a default under the REC, and the converse provision should be included in the note & mortgage. To ensure that the instruments are properly prepared, it should be clearly stated in the initial purchase agreement that the instruments will be separate, each representing a specified portion of the purchase price, and that default of either will constitute default of the other.

Making the election.

Irreversible consequences follow once the election of a remedy has been made. As held by the cases cited above, electing to rescind the REC precludes any possibility of recovering any additional money from the buyer. Also, an election to rescind constitutes a non-judicial 'sale' within the meaning of section 7425 of the Internal Revenue Code. See the discussion above of the notice requirements for discharging an IRS tax lien against the buyer's interest in the property. The seller must therefore exercise great care to avoid prejudice to his rights by inadvertently or prematurely making an election of a remedy.

The election of a remedy can be made in several ways.

Repossession of the property. At common law, repossession of the property by the seller

constituted an election to rescind the contract, thereby precluding any further recovery from the buyer. See *Graham*, above. That is because repossession is incompatible with the alternate remedy of acceleration, or 'specific performance'. If the seller wants to enforce the payment requirement, he must leave the property in the buyer's possession.

Termination of the escrow. Accepting delivery of the special warranty deed from escrow constitutes an election of the rescission remedy. Conveyance of the buyer's equitable title to the seller is obviously inconsistent with acceleration and specific performance of the contract. If the seller wishes to specifically enforce the contract, he must not only leave the buyer's possession of the property undisturbed; he must also allow the conditional delivery of legal title into escrow to remain in effect.

Recording or delivery to escrow agent of the affidavit of default. Form 103 specifically provides that the seller's recordation in the county clerk's office of an affidavit of default constitutes an election to terminate the contract. The RANM forms state that *delivery to the escrow agent* of an affidavit of default constitutes an election to terminate. Title companies usually require recordation of the special warranty deed from escrow and the affidavit of default before insuring the seller's title after forfeiture. For that reason, the affidavit is usually presented to the escrow agent before picking up the special warranty deed from escrow, and therefore represents the point in time when the election of a remedy is made.

The Affidavit of Default.

The affidavit of default serves several purposes:

1. It is a vehicle for making the election to terminate the REC and forfeit the buyer's interest in the property and it provides notice to the world, upon recordation, of such election;
2. It provides protection to a subsequent bona fide purchaser for value from the seller, or to a subsequent secured bona fide lender to seller, against claims of the defaulted buyer; and
3. It documents and discloses the default, notice and termination procedures followed, and thereby provides some degree of protection to the escrow agent and to the seller against any subsequent claims based upon defective termination procedures.

Most escrow agents require that the seller or his attorney produce an executed copy of an affidavit of default as a condition to surrendering the escrowed documents. Upon termination and surrender of documents to the seller, a closeout fee is usually charged to the seller.

Contents of Affidavit.

When termination is predicated upon a refused or unclaimed demand letter, the affidavit

should positively recite the details of mailing and return. It should also state that the affiant has made a diligent effort to determine the buyer's whereabouts, but has been unable to do so. Finally, a copy of the demand letter and the envelope in which it was mailed should be attached to the affidavit, and incorporated by reference. If the seller refuses to produce such an affidavit, or relies upon an inadequate or incomplete affidavit, then the escrow agent should require the seller to execute a release and indemnification agreement as a condition to surrendering the escrow documents. If not satisfied that adequate termination procedures have been followed, it should refuse to surrender the documents, and if necessary, file a civil suit asking the court to declare the rights of all interested parties.

When termination is based upon a delivered letter of demand, a copy of the document evidencing delivery (certified mail receipt or affidavit of process server) should be attached to the affidavit. The affidavit should state in detail the date of mailing, the fact that affiant caused the letter to be mailed, the address used, and the fact of delivery. The affidavit should refer to and incorporate the certified mail receipt as an exhibit to the affidavit. In all cases, the affidavit should identify the parties and state the legal description of the property.

For an example of an affidavit of default see no. 24, Forms Appendix.

The Forfeiture Remedy

History

The cornerstone for the remedy of non-judicial forfeiture was laid in place in 1960 by the Supreme Court in the case of *Bishop v. Beecher*. See p. 47, CLA. The Court upheld a forfeiture after proper notice and failure to cure the default, even though the buyer had paid 1/3 of the total purchase price over a period of 6 years. The Court refused to construe the REC as an equitable mortgage, and held that the buyer had no right of redemption. The seller was entitled to enforce the contract as written, 'absent unfairness which shocks the conscience of the Court'.

For the next 25 years, the Court and various litigants wrestled with the question as to what circumstances would sufficiently 'shock the conscience of the Court' to allow relief to the defaulting buyer. Here is a chronology of the Court's rulings on that issue:

1979. A trial judge did not abuse his discretion in allowing the buyer an additional 15 days to pay off the entire balance of the REC before imposing the forfeiture remedy. See *Hale*, p. 47, CLA.

1983. Forfeiture is upheld, but the seller was required to refund that portion of the down payment exceeding the fair rental value of the property for the period of time the

buyer was in possession. The down payment was \$45,000 and the fair rental value for the period was between \$4,200 and \$10,500. See *Huckins*, p. 48, CLA.

1983. Forfeiture is upheld, but the seller's title is subjected to a resulting trust in favor of the estate of a non-party spouse to the extent that separate funds of the spouse were used to make the down payment and the first five payments on the REC. See *First National Bank in Alamogordo*, p. 49, CLA.

1984. The Court upheld a forfeiture involving a large down payment and did not require a refund to the buyer. The Court stated that the size of the forfeited down payment is only one of the factors the Court will consider, observing that the buyer had been late with 23 payments, and that default notices had issued on 11 occasions. See *Manzano Industries, Inc.*, p. 49, CLA.

1985. A forfeiture is upheld where the seller incurred a loss on the resale of the property, and incurred substantial post-default expenses to repair and re-sell the property. See *Jacobs*, p. 50, CLA.

1985 The Court reversed a trial court's refusal to enforce the forfeiture remedy, even though the

buyer had significantly reduced the unpaid balance and the property value had increased

substantially from date of purchase to date of default. See *Russell*, p. 50, CLA. The Court listed the equitable considerations that would determine whether a forfeiture shocks the conscience of the Court:

- the amount of money already paid by the buyer to the seller;
- the period of possession of the real property by the buyer;
- the market value of the real property at the time of default compared to the original sales price;
- the rental potential and value of the real property.

Procedure.

The seller can enforce the forfeiture remedy without instituting a lawsuit. Upon default by the buyer, the seller may, after satisfying any notice requirements and making the election to terminate the contract, obtain the deeds from the escrow agent and record the special warranty deed. The seller thereupon becomes entitled to possession of the property. If the buyer fails to voluntarily surrender possession, the seller may take legal action to recover possession (the RANM forms allow the seller to collect reasonable attorney's fees and costs

if such proceedings are filed). The contracts allow the seller to collect rent for the period of time the buyer remains in possession after the forfeiture becomes effective.

Termination of junior interests.

When the special warranty deed is delivered from escrow to the seller, the delivery relates back to the inception of the escrow, so that all intervening interests junior to the REC are terminated by the rescission of the REC. The only exceptions are federal tax liens on the purchaser's property interest, as discussed above and, under certain conditions, mechanics' liens.

Leasehold interests. The buyer under a conditional sales contract can create no greater interest in a lessee than the buyer held, and the lessee takes the property subject to all claims of title enforceable against the buyer. Upon default by the buyer, the seller was entitled to recover the property free of the leasehold. See *Campos*, p. 51, CLA. (a case of first impression in New Mexico)

Security interests in personal property. Where land and equipment were both sold on a conditional sales contract (REC), a bank claiming a U.C.C. security interest in the equipment through the buyer was held to be junior to the prior title claim of the seller. Upon buyer's default and forfeiture, the bank lost any security interest it had. See *Western Bank*, p. 52, CLA.

Mechanics' liens. Section 48-2-11, NMSA 1978 provides that the interest in land owned or claimed by a landowner who has knowledge of the construction, alteration or repair of buildings or other improvements on the land, and who fails to post a written notice of non-responsibility in a conspicuous place on the land or building within 3 days after obtaining such knowledge, is subject to any mechanics' lien properly filed under the statute.

A seller under a REC who knows that such work is being done on the property comes within the statute, and must post a notice of non-responsibility within 3 days after gaining knowledge of the work in order to avoid subjecting his reversionary interest in the property to the lien. See *Hill*, p. 53, CLA. The Court held the seller's interest to be subject to a properly filed mechanics' lien for work performed at the request of the buyer, where the seller failed to post the required notice.

The Court also held that the buyer qualified as an 'owner' of real estate for purposes of the mechanics' lien statute. Therefore, a carpenter employed by the buyer to perform alterations or additions to a building on the property was deemed to be an original contractor, so that the carpenter was allowed 120 days after default on payment to file a lien, rather than 90 days as allowed for subcontractors.

In the earlier *Petrakis* decision (p. 53, CLA), the Court had held that the seller under a REC satisfied the posting requirement, and his interest was not subjected to the lien. The

seller had posted a timely notice with regard to the construction of a dance hall, but failed to post a new notice when construction of an adjacent game room began within two weeks after completion of the first project. The Court held that the seller had no reason to know or suspect that the second project was commenced under a new contract, rather than being a continuation of the first contract, and therefore was not required to post a new notice.

By way of dictum, the *Petrakis* Court had expressed its opinion that a mechanics' lien would not survive a forfeiture of the REC buyer's interest in the property. The *Hill* Court, however, ruled otherwise seven years later.

Buyer's lien for improvements.

The defaulted buyer has a statutory lien for the value of any improvements he may have made on the property, against the subject property and *all other property of the seller located within the county*. See sect. 42-4-14 to 42-4-19, NMSA 1978. The lien arises upon the service of a summons on the buyer in an ejectment action or any other action to deprive the buyer of possession, and endures for a period of ten years. The Supreme Court has held that the lien is limited to the cost of the improvements, rather than fair market value, and does not include the value of improvements made after the date of service of the summons. See *Cano*, p. 54, CLA.

Waiver of lien for improvements. The RANM forms contain a statement that in the event of termination, the buyer 'waives any and all rights and claims for reimbursement for improvements he may have made upon the Property'. There have been no court decisions on the issue as to whether the buyer's statutory lien can be waived by agreement.

Drafting suggestion.

Form 103 does not contain a waiver clause, so the buyer's lien for improvements would certainly survive a forfeiture when that form of contract is used. Inclusion of a waiver clause is necessary to give the form 103 seller protection on a par with the RANM forms. Whether the contractual waiver would be upheld remains an unanswered question.

The Acceleration Remedy

If the seller does not wish to recover the property, he may elect instead to declare the unpaid principal balance and accrued interest to be immediately due and payable. The acceleration remedy is very seldom used, for three reasons:

1. The seller usually gets a "windfall" benefit by electing the termination remedy. In most situations, the property has maintained or increased its value since the date of sale. The seller can therefore sell the property again on terms equal to or better than the terms of the defaulted REC while retaining all payments made

by the buyer under the REC.

2. The acceleration remedy is usually inadequate, because a buyer who cannot maintain payments on the REC ordinarily will be found to be lacking sufficient assets to satisfy a money judgment.
3. Acceleration and foreclosure is costly and time consuming, because it requires litigation.

Nevertheless, there are situations where the acceleration remedy would be preferable. If the property has declined in value, and the buyer has other assets subject to execution, the seller may achieve better results by accelerating the unpaid balance.

If the seller elects to accelerate, the REC is not terminated, the deeds are not recovered from escrow, and the buyer's possession of the property is not disturbed. Election of this remedy presumes that the seller will be paid the balance of the purchase price and that the buyer will thereupon acquire title to the property.

To enforce this election, the seller must file suit against the buyer for the unpaid balance. In effect, the suit seeks 'specific performance' of the contract. The RANM forms allow the seller to recover a reasonable amount as attorney's fees if such a suit is filed. Form 103 does not provide for attorney's fees. This is an important distinction, because it is a well-settled rule that a litigant cannot recover his attorney fees unless they are expressly allowed by statute or by an agreement between the parties. See *Aboud*, p. 36, CLA.

If a money judgment is obtained against the buyer, there are then two separate methods of enforcement available to the seller:

- He can collect in the same manner as for any other money judgment, including execution against the buyer's assets (sect. 39-4-1 NMSA 1978) and garnishment of his employer or his debtors.
- He may also record a transcript of the judgment in the county clerk's office in any county where the buyer owns real property, and thereby acquire a judgment lien against the property. See section 39-1-6 NMSA 1978. He can then foreclose on the judgment lien. See section 39-5-1 et seq.

The Supreme Court has held that the seller can seek both forms of relief in the same lawsuit, when no third-party rights are involved. See *Armstrong*, p. 55, CLA.

Seller Default

Events of Default

New Mexico Supreme Court decisions have documented the following types of seller default on a REC:

- Repudiation (refusal to consummate sale or convey title);
- Failure to deposit deed in escrow;
- Failure to deliver title (acreage deficiency);
- Misrepresentation of the property; and
- Failure to provide title insurance.

Repudiation

Where an owner contracts to sell a house, then repudiates the contract and refuses to convey the property to the buyer, the buyer may recover damages measured by the fair market value of the property, less the contract price. See *Wall*, p. 56, CLA. This is known as the 'loss of bargain' rule, and is the inverse of the same rule applied in the case of buyer repudiation. See *Aboud*, p. 36, CLA.

The 'loss of bargain' measure of damages was applied in a repudiation case where the seller's wife did not join in signing the contract of sale. See *Hickey*, p. 57, CLA. The property was the separate property of the husband. The wife had contributed management services to the property, and claimed that her lien against the property for services made her joinder in the contract mandatory. The Court ruled that the right of the community to be reimbursed for the amount of the lien does not change the character of the property from separate to community. Separate property may be conveyed by the owner without the joinder of the spouse.

A buyer under a REC can specifically enforce the contract against the seller who had owned the house as her sole and separate property, even though the seller had previously conveyed the property to herself and her husband by an unrecorded quitclaim deed. The community property law which provides that a conveyance of community real property by one spouse alone is void (sect. 40-3-13(A)) must yield to the recording statute (sect. 14-9-3 NMSA 1978) which provides that an unrecorded conveyance does not affect the title of a subsequent innocent purchaser for value. See *Jeffers*, p. 58, CLA.

Failure to deposit deed in escrow

The RANM forms and form 103 state that the parties have executed deeds and deposited them in escrow, subject to the terms and conditions of the contract. The requirement for the seller to deposit the warranty deed in escrow has been held to be 'an absolute condition precedent so vital and essential to the contract that a failure to so deliver the deed relieved the vendees of any obligation whatsoever until such deed was so deposited'. (emphasis added) See *Montgomery*, p. 58, CLA. The Court held that the sellers could not complain of buyers' failure to make a scheduled annual installment payment, until the deed was placed in escrow.

This case underscores the importance of delivering all documents to the escrow agent as required by the REC, mortgage or deed of trust. Title closing officers sometimes send the REC to the escrow agent without one or more of the deeds, which are to 'come later', because the first payment due date is imminent and the seller wants to collect the payment. This is dangerous practice, because the failure to deposit a required deed constitutes a breach of the contract.

Failure to deliver title

Where a REC buyer pays off the contract and receives the warranty deed from escrow, then discovers that the actual acreage of the property is less than the acreage described in the warranty deed, the buyer may recover damages based on the seller's breach of the covenant of seizin contained in the title warranties. See *Gonzales*, p. 59. The buyer was able to purchase the deficient acreage from the actual owner, so the Court awarded the buyer the cost of acquiring title to that property. Had the buyer not been able to acquire the deficient acreage, the Court suggested that it would award a ratable abatement of the purchase price, plus interest, assuming that all the land had approximately equal quantitative value, based on the seller's innocent mistake.

A seller may enter into a contract to sell real estate which he does not presently own, provided he is able to deliver title after the final payment is made or tendered. See *Campbell*, p. 41, CLA and *English*, p. 44, CLA. Consequently, the buyer cannot rescind or repudiate the REC on the basis that the seller does not have title to the property that he has agreed to sell. The buyer must first tender payment in full of the unpaid REC balance to the seller or the escrow agent, thereby maturing the seller's obligation to deliver title to the property.

Practice suggestion: This problem should never arise, if a contract purchaser's title insurance policy is obtained at closing. The seller's title to the property should be established before signing the REC!

Effect of 'as is' clause.

When the REC contains an 'as is' clause, the Supreme Court has held that the clause

provides absolute protection to the seller only when the buyer and seller possess equal knowledge of the property. See *C. Lambert & Associates, Inc.*, p. 59, CLA. Thus, when hidden or latent defects are known only to the seller, it is unlikely that selling the property 'as is' will provide very much protection to the seller.

Misrepresentation

A buyer who, in entering a contract, justifiably relies on a seller's misrepresentation of a material fact can rescind the contract, irrespective of the good or bad faith of the seller, provided the buyer can place the seller in the status quo that existed before the sale. See *Robison*, p. 60, CLA. However, the restoration to status quo requirement will not be enforced if it has been rendered impossible by circumstances for which the buyer is not responsible, or for which the seller is responsible.

In addition to rescission, the buyer may recover 'consequential damages', or 'restitutionary damages' if necessary to put the buyer back in as good a position as he occupied before entering the contract. These damages will be limited to those expenses that must have been or should have been contemplated as probable consequences of the fraud by the parties whose actions are the basis for the rescission, and will be assessed against those parties. In *Robison*, 'everything was arranged by' the real estate broker, rather than the seller, so he was required to pay the consequential damages.

The Court held that 'reckless behavior will warrant the award of punitive damages, if the injured party is able to prove actual damages'. Since it was the real estate broker who made 'material misrepresentations in reckless disregard for their truth', the case was sent back to the trial court for a hearing on the issue of actual damages.

Where the seller is aware of defects in a property (leaking swimming pool) and fails to disclose them to the buyer before signing of an agreement of sale, the failure to disclose the information constitutes constructive fraud, irrespective of any actual dishonesty of purpose or intent to deceive. *Snell v. Cornehl*, 81 N.M. 248, 466 P.2d 94 (1970).

Where the seller mistakenly misrepresents the square footage in a house, the misrepresentation constitutes constructive fraud, irrespective of the good faith of the seller, if the representation is justifiably relied on by the buyer. The statute of limitations does not begin to run against the buyer's cause of action for damages until the buyer actually discovers the error. *Gaston v. Hartzell*, 89 N.M. 217, 549 P.2d 632 (1976)

However, where a homebuilder and the buyer were equally aware that there was an unpaved street to the rear of the property, and the builder made no representations to the buyer, the builder had no duty to disclose the possibility that the city may levy a special paving assessment in the future, even though the builder, when he purchased the lots, had received a discount from the purchase price to offset any special assessments which may be

levied against the lots in the future. *Krupiak v. Payton*, 90 N.M. 252, 561 P.2d 1345 (1977)

Where a homeowner made no representations to a buyer (who was blind) other than information contained in a listing form containing the words "Large den with stone FP", the Court of Appeals held that the seller had a duty to disclose known defects in the fireplace to the buyer or his realtor. Failure to disclose the defects constituted constructive fraud, entitling the buyer to recover damages for smoke damage to the house. *Archuleta v. Kopp*, 90 N.M. 273, 562 P.2d 834 (1977)

A developer was liable in damages to a buyer when a shared water well went dry within 6 months after the sale. The developer had disclosed two favorable hydrology reports, and a negative report, as well as a H.U.D. report which warned of the divergent opinions as to the availability of water in the area. The developer had failed to disclose one adverse hydrology report. *Wirth v. Commercial Resources, Inc.*, 96 N.M. 340 (App.), 630 P.2d 292 (1981). "To reveal some information on a subject triggers the duty to reveal all known material facts".

Failure to provide title insurance

Where the seller is obligated by the contract to provide a policy of title insurance, and fails to produce the policy, the buyer may rescind the contract, subject to the requirement that the parties be restored to the status quo ante. See *Meech*, p. 62, CLA. The buyer may therefore have to pay the seller compensation for the use of the property, and also for any excessive deterioration in the condition of the property during the buyer's possession.

In the absence of a specific time deadline for delivery of the policy, or in the absence of a 'time is of the essence' clause, the seller will be allowed a reasonable time to perfect title. See *Loyd*, p. 61, CLA. However, in the *Meech* case, the contract required the policy to be furnished within one year after the date of the contract. The Court held that failure to meet the deadline entitled the buyer to rescind the contract.

Where the contract gave the buyer a six month period to conclude a quiet title suit regarding the property, and provided that if the buyer was unable to conclude the suit within the six month period, he could rescind the contract, recover his down payment, and the escrow agent would be instructed to deliver the special warranty deed to the seller, and the buyer continued to pursue the quiet title suit after the six month period expired, the Supreme Court held that the buyer had waived his right to rescind the contract. See *Lorentzen*, p. 62, CLA. The buyer had contracted to assume the burden of quieting title. When it later developed that the seller owned only a one-fourth interest in the property, the seller had no duty to perfect the title.

Where a REC required the seller to deliver a title policy at the time the warranty deed was

delivered from escrow, and the seller did not comply, it was held that the buyer did not waive his right to delivery of the policy by accepting and recording the warranty deed. The buyer was allowed to sue for damages after quieting title to the property. See *Chavez*, p. 63, CLA.

CASE LAW APPENDIX

About v. Adams et al.....	CLA-36
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EQUITABLE CONVERSION DOCTRINE

Mesich v. Board of County Com'rs of McKinley County, 46 N.M. 412, 129 P.2d 974 (1942)

Facts:

- Mesich entered into installment agreement with Ford to purchase lots adjacent to Highway 66 in Gallup.
- The Board guaranteed the Highway Commission that it would furnish the property in question to the Commission for highway widening purposes.
- Mesich, after negotiations, gave the Highway Commission a blank deed, with the understanding that it would be filled in later with the description of a ten-feet-wide strip of land. The description subsequently entered was for a much larger tract, contrary to the agreement.
- Ford executed and delivered to Mesich a deed for the property, less the appropriated right of way.
- Mesich filed suit to recover compensation for the taking of private property for public use.

Issue: Did Mesich have a cause of action, when he was not the fee simple owner of the property taken?

Holding: Yes. The applicable statute required compensation “to the owner of such property...”. The Court holds that the installment contract purchaser is the “owner”, and describes the respective interests of the vendee and vendor:

“In law the effect of a contract whereby the owner agrees to sell and another agrees to purchase a designated tract of land, the vendor remains the owner of the legal title to the land; he holds the legal title, 1 Pomeroy’s Equity Jurisprudence, sect 367. But, in equity the vendee is held to have acquired the property in the land and the vendor as having acquired the property in the price of it. The vendee is looked upon and treated as the owner of the land and the equitable estate thereof as having vested in him. He may convey it or encumber it, devise it by will and on his death it descends to his heirs and not to his administrators. The legal title is held by the vendor as a naked trust for the vendee and any conveyance by him to one not a bona fide purchaser for value is ineffective to pass title. The vendee must bear all accidental injuries or losses done to the soil or appurtenances, by the operations of nature or third parties, and is entitled to recover all damages for injury thereto. The vendor, before payment, holds the title as trustee for security only.”

The Court quotes from Pomeroy’s Equity Jurisprudence, section 368:

“Although the land should remain in the possession and in the legal ownership of the vendor, yet equity in administering his own property and assets looks not upon the land as land,-for that has gone to the vendee,-but looks upon the money which has taken the place of the land; that is, so far as the land is a representative of the vendor’s property, so far as it is an element in his total assets, equity treats it as money, as though the exchange had actually been made, and the vendor had received the money and transferred the land.”.

Trickey v. Zumwalt v. Albuquerque National Bank, 83 N.M. 278, 491 P.2d 166 (1971)

Facts:

- Zumwalt purchased land on REC from Trickey, payable in annual installments.
- State of New Mexico commenced condemnation proceedings against the entire property, and deposited \$27,000 into the registry of the court, and took immediate possession of the land.
- Trickey sent default notice to Zumwalt for delinquent payment in the amount of \$9,486.66. Trial court held that application of the condemnation deposit to the balance of the REC cured any past default. Appealed.
- State deposited an additional \$15,000 into the court registry, which was credited to the REC balance.

Issue: "...whether any part of the condemnation money deposited by the State could be applied to cure appellee's default without impairing the seller's security in the deposit."

Holding: "We think not....In Mesich..., we adopted the position that a vendor in a real estate sales contract holds the legal title as trustee for security only. When this security is condemned by one vested with the power of eminent domain, the award, in this instance the preliminary deposit prior to financial determination of the award, stands in place of the land and is security for performance of the contract and is subject to liens just as if it were the land....We do not decide the issue of the appellee's alleged default, only that the condemnation deposit cannot be used to cure any default under the real estate contract."

Hobbs Mun. School Dist. No. 16 v. Knowles Development Co. Inc., 94 N.M. 3, 606 P.2d 541 (1980)

Facts: School District sought to condemn a 40-acre tract of land being purchased by Knowles from the state under a contract of sale. The trial court found that the District had a reasonable necessity for only 15 acres of the land, and permitted condemnation of that part only.

Issue: The school district argued that the general rule, that a condemnor can take no greater interest than is reasonably necessary for the contemplated public use, should not apply here, because it was seeking to condemn the interest in the contract only.

Holding: "...we do not believe that any logical differentiation can be drawn between the condemnation of the land itself and the condemnation of the contract to purchase the land....The interest acquired by the purchaser under an executory contract for the sale of land is real estate. (citing *Marks*) This is an interest which is subject to condemnation proceedings. We hold that a court may approve the condemnation of a tract of land even though it is less than the entire tract held by third parties under contract with the State."

Gregg v. Gardner, 73 N.M. 347, 388 P.2d 68 (1963)

Facts:

- Irma Evans executed a will, in which she (1) devised all her real estate to a trust for her two minor children or their surviving children, or, if none, then to the surviving child. If both children predeceased her, then the real estate was devised to her niece, Marion Hogan; (2) gave and bequeathed all her personal property to her husband; if he predeceased her, then to the trust for the benefit of the two children. There was no contingent beneficiary named for the personal property in the event the two children predeceased Irma.
- The husband and both children predeceased Irma, leaving no surviving grandchildren.
- Before her death, Irma sold the real estate under installment contracts of sale.

Issue: Whether the contracts of sale are assets passing as real estate to Marion Hogan, or as personalty, in which case they would descend under the laws of intestate succession.

Holding: Irma's interest in the contracts of sale is personal property. "It is equally clear from our decisions that in equity a contract for sale of real estate results in the purchaser acquiring an equitable interest in the land which he may devise by will, and in case of intestacy the same passes to his heirs and not to his administrator. Whereas, legal title remains in the vendor, it is held in trust as security (citing *Mesich* and others). In *Treadwell v. Henderson*, 58 N.M. 230, 269 P.2d 1108, it was explained that this results through application of the doctrine of equitable conversion. It must follow that when testatrix entered into contracts to sell certain of her real estate, the equitable interest in the land passed to the purchasers although legal title remained in her. Through the doctrine of equitable conversion, her interest is considered as personalty.... The personal property not having been disposed of in the will, it descends under our statutes of descent and distribution."

Warren v. Rodgers, 82 N.M. 78, 475 P.2d 775 (1970) (overruled by *Mutual Building & Loan*)

Facts: Standard REC for purchase of land and service station. Buyer's judgment creditor recorded judgment liens; then buyer defaulted on REC & seller declared a forfeiture.

Issue: Do judgment liens attach to a purchaser's interest in land which is subject to a real estate contract, under sect. 21-9-6, N.M.S.A. 1953 Comp., which states: "Any money judgment...shall be a lien on the real estate of the judgment debtor from the date of the filing of a transcript of the docket of the judgment in the judgment record book in the office of the county clerk of the county in which the real estate is situate....."?

Holding: No. Legal interests only, as distinguished from equitable interests, are subject to judgment liens.

Mutual Building & Loan Association of Las Cruces v. Collins, 85 N.M. 706, 516 P.2d 677 (1973)

Facts:

- Mutual held a judgment against Collins, a transcript of which was recorded in the county clerk's office. Collins was the purchaser of land under an escrow contract.
- Mutual sued Collins to foreclose the lien of its judgment against Collins' interest in the land. The trial court held that Mutual had failed to state a claim upon which relief could be granted, and Mutual appealed.

Issue: Does a judgment lien attach to the equitable interest of a conditional vendee of real estate?

Holding: Yes. (Overruling *Warren v. Rodgers*).

"Ordinarily an equitable interest in real estate is not subject to execution or judgment lien,...unless there exists a statute broad enough to include equitable interests....This Court, in *Warren v. Rodgers*, supra, stated that only legal interests, unlike equitable interests, were subject to judgment liens. In declaring its position, the Court in *Warren*, supra, recognized a substantial split of authority on this question,...and adopted the limiting California rule. We, however, prefer and adopt the more liberal rule...and declare that both legal and equitable interests in real estate are subject to judgment liens. Therefore, *Warren v. Rodgers*, supra, is overruled insofar as it held that judgment liens cannot attach to equitable interests."

"A judgment lien on real property did not exist at common law, but is a right established by statute...Section 24-1-22, N.M.S.A. 1953 Comp. establishes such a right and together with sect. 21-9-6, N.M.S.A. 1953 Comp...make no distinction between legal and equitable interests in real estate."

The Court went on to discuss the homestead exemption statute, sect. 24-6-1, N.M.S.A. 1953 Comp., which allowed a \$10,000 exemption from foreclosure by a judgment creditor in a dwelling-house occupied by the debtor, "...although the dwelling is on land owned by another, provided that the dwelling is owned, leased or being purchased by the person claiming the exemption.". The Court noted that if the *Warren* rule governed, then the equitable interest of the purchaser would be completely exempt, and the homestead exemption provision effectively contravened, a result not intended by the Legislature in enacting sect. 24-6-1.

The Court also stated that its new rule "...prevents a debtor from placing his assets beyond his creditor's reach and precludes the possibility of fraud being perpetrated upon the commercial community".

Marks v. City of Tucumcari, 93 N.M. 4, 595 P.2d 1199 (1979)

Facts:

- Marks purchased property from Goldenstein by REC, which was recorded.
- The City filed a transcript of its judgment against Goldenstein in the county clerk's office.
- The deed to the property, running from Goldenstein to Marks, was released from escrow and filed with the county clerk.
- Marks sued the City, seeking a declaration of his rights to the real estate.

Issue: Does a judgment lien attach to the interests of a vendor of land under a conditional sales contract?

Holding: No. "In New Mexico, the rule is that a *vendee*, under an executory contract for the sale of realty, acquires an equitable interest in the property. By application of the doctrine of equitable conversion, the *vendee* is treated as the owner of the land and holds an interest in real estate. On the other hand, the *vendor* holds the bare legal title as a trustee for the vendee. The *vendor's* interest is considered personalty." (citing *Gregg* and *Mesich*)

The Court cites sect. 39-1-6, N.M.S.A. 1978 (formerly sect. 21-9-6, N.M.S.A. 1953) and sect. 39-4-13, N.M.S.A. 1978 (formerly sect. 24-1-22, N.M.S.A. 1953) and reviews the *Mutual Building & Loan* discussion of those statutes: “We note that in *Mutual Building & Loan* the Court held that both *legal and equitable interests* in real estate were subject to judgment liens. If the Court, by that statement, intended to include within the term “*real estate*” the interest of a *vendor* in an executory contract for the sale of realty, then that specific language is hereby expressly overruled.”.

“We are committed to the rule expressed in *Gregg* and *Mesich* that the interest retained by a vendor under an executory contract of sale is personalty and not real estate. Since section 39-1-6 permits a judgment lien only upon real estate and since the judgment debtor’s interest in the property was converted to personalty, the City’s judgment did not ripen into a lien on the real estate involved.”.

Bank of Santa Fe v. Garcia, 102 N.M. 588, 698 P.2d 458 (1985)

Facts:

- Witt purchased land on REC from Smith.
- Bank of Santa Fe obtained judgment lien against Witt’s interest in REC.
- Witt deeded property to Espinoza, who accepted the deed with knowledge of the judgment lien, and made improvements on the property.
- Bank of Santa Fe foreclosed.

Issue: Whether a judgment lien attaches to the full value of the REC purchaser’s estate in the property, or only to the value of payments and improvements made by purchaser.

Holding:

- “When the vendor has not exercised his contractual rights to declare a forfeiture, our cases support recognizing that the debtor’s estate in the property is an equitable fee simple, subject to the vendor’s lien for the unpaid purchase price.”. (citing *Mutual Building & Loan*, *Marks* and *MGIC Mortgage Corporation* cases)
- “...because a judgment lien is a lien on the real estate of the debtor from the date of filing of the transcript of judgment, Section 39-1-6, and a purchaser under a real estate contract is treated as the owner of the property, the debtor’s interest in the property to which the lien attaches, when he holds equitable title under a real estate contract, is the full value of his estate in the property, not just the amount of his payments and the value of improvements as defendants here contend.”.
- “Mrs. Espinoza made the improvements with actual and constructive knowledge of the prior liens on the property and, therefore, contributed to the equity at her peril.”.

MGIC Mortgage Corp v. Bowen, 91 N.M. 200, 572 P.2d 547 (1977)

Facts:

- Bowen sold property to Lovato by REC, subject to MGIC mortgage, which Lovato assumed.
- ACRA Inc. became a judgment lien creditor of Bowen.
- The U.S. filed a tax lien against the property based on tax assessments against Lovato.
- Lovato defaulted on the REC, MGIC foreclosed on its mortgage. No notice of default was ever sent by Bowen to Lovato, as required by the REC.
- After the foreclosure sale, a surplus refund was deposited with the Court, and suit followed to establish whether ACRA or the U.S. was entitled to the refund.

Issue: Whether the contract purchasers (Lovato) retained a property right under the REC that could be attached by the U.S.

Holding: “Tax liens attach to the interest of the vendee in a conditional sales contract (citation). They are co-extensive with the taxpayer’s interest in the property. (citations) However, a tax lien cannot endure after the expiration of the interest of the party against whom the lien was filed. If the interest of Lovatos, the vendees, terminated through forfeiture or otherwise, the tax lien attached to that interest must have also terminated...”

“This Court has held that if the vendor fails to give notice of his intent to forfeit the contract, it remains in effect. *Nelms v. Miller*, 56 N.M. 132, 241 P.2d 333 (1952). Although the Lovatos were in default, since their interest had not been forfeited by receiving notice, they still had an equitable interest that could have been redeemed prior to the foreclosure sale. The United States’ tax lien attached to the equitable interest of the Lovatos which was still in existence at the time the mortgage was foreclosed.” The Court awarded the refund to the U.S., based on its lien.

Comment: The Court’s observation that a federal tax lien against the buyer’s equitable interest would not survive forfeiture of the REC was correct at the time. The Tax Reform Act of 1986 completely changed the law. See “**Who is entitled to notice?**”, Chapter 12.

Shindledecker v. Savage, 96 N.M. 42, 627 P.2d 1241 (1981)

Facts:

- Taylor sold land on REC to Savage.
- Savage executed a “second mortgage” to Shindledecker, to secure a personal loan.
- Savage, while not in default, instructed the escrow agent to release the special warranty deed to Taylor, and left the state.
- Taylor sold the property to Villasenor, who then sold it to Jacquez.

Issues:

- (1) Whether the vendee under an executory land sales contract has a mortgageable interest, and
- (2) If so, whether vendee can terminate that interest by agreement with the vendor to relinquish the property to the vendor.

Holding:

- (1) Following a line of cases from the state of Washington, the Court holds that the vendee under a real estate contract has a mortgageable interest, subject to the prior interest of the vendor and, in this case, Shindledecker "...had a valid lien on that interest."
- (2) The Court recognized that, although the vendor can, upon default by the vendee, retake the property and retain all sums paid under the contract, where there is no default, the "...mortgagee cannot have his lien eclipsed by the agreement of the parties to the real estate contract to rescind it.... the mortgagee assumes the rights of the vendee under the real estate contract."
- (3) Nevertheless, the Court held that the rights of Shindledecker must yield to the rights of the subsequent purchasers of the property, because Shindledecker failed to protect his lien by giving notice to Taylor of his mortgage interest. Citing a Washington case, the Court reasoned: "The mortgagee of an equitable interest must protect his lien by giving notice to the vendor of his equitable interest so that he can arrange an assumption of the contract in case the vendee defaults or otherwise rescinds the contract. Recording the mortgage does not give the vendor constructive notice such as to require the vendor to notify the mortgagee of his intent to retake the property.... Instead, the mortgagee must use one of several available contractual devices to insure that he receives both notice of a breach by the vendee and the opportunity to protect his interests." (emphasis added)

First National Bank of Belen v. Luce, 87 N.M. 94, 529 P.2d 760 (1974)

Facts:

- In 1963, Tucker sold land to Newton on a REC, which was not recorded. Newton took possession.
- In 1965, Newton assigned his interest to Levacy, who took possession and made substantial improvements on the property. The assignment was not recorded.
- In 1969, Tucker mortgaged the property to FNB. Tucker then assigned his interest in the REC to Luce.
- FNB filed a foreclosure suit. The trial court concluded that FNB, prior to advancing any funds on the mortgage, had actual knowledge of the existence of the REC. The trial court ruled that FNB had no lien on the balance of the money due under the REC.

Issues:

- (1) Whether FNB should be charged with notice of the existence and priority of the REC;
- (2) Whether FNB's mortgage attached to the property.

Holding:

- (1) A person who purchases real estate in the possession of another is, in equity, bound to inquire of such possessor what right he has in the real estate. If he fails to make such inquiry, which ordinary good faith requires of him, equity charges him with notice of all the facts that such inquiry would disclose. The Court cites *McBee* and *Nelms*. Therefore, the mortgage is junior and subject to the unrecorded REC and the assignment.
- (2) At the time of execution of the mortgage to FNB, the only interest in the real estate owned by Tucker was a possibility of reverter to him in the event of a default by Levacy in payment of the REC. Since Tucker never assigned to FNB any interest in the unpaid balance of the REC, the only lien acquired by FNB was on the possible reversionary interest of Tucker.
- (3) The Court also stated its opinion that FNB's case should fail because FNB failed to comply with the UCC provisions on secured transactions.

In Re Finch, 120 N.M. 658, 905 P.2d 198 (1995)

Facts:

- Finch borrowed \$12,000 from Beneficial Mortgage Company. As security, Beneficial obtained and recorded a mortgage on real property that Finch had sold under REC to Rasmussen.
- Finch defaulted on loan with Beneficial & declared bankruptcy; Rasmussen paid off the REC.
- Beneficial claimed the proceeds from the REC being held in escrow in the bankruptcy proceeding. Finch argued that Beneficial lost its secured status & no longer held a forecloseable mortgage when legal title passed to Rasmussen. Beneficial argued that the mortgage attached to any interest Finch had in the property, including the right to the contract proceeds, and that it should be recognized as a “secured creditor”.

Issue: The U.S. District Court certified a single question of law to the New Mexico Supreme Court for determination under state law: whether a mortgage granted by the seller under a REC attaches to the proceeds of that contract as a matter of law.

Holding: A mortgage lien does not automatically attach to the proceeds of a real estate contract. A mortgage is not an assignment. An assignment immediately transfers legal title, while a mortgage only establishes a lien on legal title. “Once full legal title passed to Rasmussen, Beneficial lost all its rights associated with ownership of that property *in relation to Rasmussen*.”

However, “...the mortgage served as a written security agreement attaching to the proceeds of the contract, and that the filing of the mortgage in the county records perfected that interest *as to the Finches*.”. Because the Finches admittedly intended to give their whole interest in the property to secure the loan, the description of the real estate subject to the real estate contract “...adequately described the contract proceeds...” *as to the Finches*. The REC met the requirements of the UCC as a security agreement creating a security interest in personal property, and it was perfected upon recording in the county clerk’s office.

Comment: The Court distinguishes *Marks*, because that decision held that a judgment lien did not attach to the *buyer’s* interest in a REC. In this case, “...the Finches are the sellers, not a bona fide purchaser, and the Finches offered their interest as security for their loan.”.

C & L Lumber and Supply v. Texas American Bank, 110 N.M. 291, 795 P.2d 502 (1990)

Facts:

- Joe McDermott, while married to Dixie, purchased a 1.7 acre tract of land from West on an REC. He then purchased from West a 6.4 acre tract, using cash from a loan & mortgage from Ruidoso State Bank, and by giving a 2nd mortgage to West. Each of the instruments stated that the property was the sole & separate property of Joe McDermott, a married man, but Dixie did not join in any of the instruments.
- Joe borrowed \$200,000 from Texas American Bank, and paid off the loan to Ruidoso State Bank. Texas American obtained a mortgage from Joe, & entered into a subordination agreement with West, thereby placing Texas American in first position as to the 6.4 acre tract.
- Joe then borrowed another \$120,000 from Texas American, and used \$60,000 of the loan to pay off the REC debt to West. Texas American obtained a mortgage from Joe on the 1.7 acre tract, and entered into a subordination agreement with West, thereby placing Texas American in first position as to the 1.7 acre tract.
- Joe & Dixie divorced; she conveyed her community interest in both tracts to Joe by special warranty deed.
- Construction began on both tracts. C & L Lumber, a materials supplier, filed suit to foreclose its materialmen’s lien on the property.
- Trial court, in determining lien priorities, placed Texas American in last position on both properties, ruling that the mortgages granted by Joe to Texas American were void, because they were not signed by his wife. Under sect. 40-3-13(A) NMSA 1978, any attempt to mortgage community real property by either spouse alone is void, except in the case of purchase-money mortgages. Texas American appealed.

Issues:

1. Do mortgages securing loans to refinance purchase money mortgages constitute purchase money mortgages themselves?
2. Does a mortgage securing a loan to refinance a REC constitute a purchase money mortgage?

Holding:

1. “A purchase-money mortgage is a mortgage executed at the same time as the deed of the purchase of land, or in pursuance of agreement as part of one continuous transaction, in favor of the vendor, or third-party lender of the purchase price paid to the vendor, provided the money was loaned for this purpose.”. Although the Ruidoso State Bank mortgage was a purchase-money mortgage, the refinancing of that obligation did not create a purchase-money mortgage. “Title had already passed to McDermott as part of the original financing transaction. McDermott was already indebted for the purchase price. The subsequent borrowing was for the purpose of discharging this debt, not for the acquisition of title.”.
2. Notwithstanding that McDermott first acquired legal title to the 1.7-acre tract when the REC was paid off, the Texas American mortgage securing the loan to pay off the REC is nevertheless not a purchase-money mortgage. “...the basis usually given for the priority of a purchase-money mortgage...is that ‘there is no moment at which the judgment lien can attach to the property before the mortgage of one who advances purchase money.’” (citing an Indiana case) “In New Mexico, the purchaser’s equitable estate under a land sales contract is an estate in property. (citing *Hobbs*) He is treated as the owner and his interest in the property is subject to a judgment lien. (citing *Mutual Building & Loan* and *Marks*) Thus, various liens in fact may attach themselves to property under a land sales contract prior to the execution of a refinancing loan and mortgage.... We conclude that under New Mexico law a mortgage executed for the purpose of paying off a land sales contract is itself not a purchase-money mortgage.

Comment: The Court also rejected Texas American’s argument that it should be subrogated to the purchase-money mortgage position of the original vendors by virtue of the refinancing transactions. Even if the REC was a purchase-money mortgage, the Court observed that “...subrogation is generally not allowed when a third party, in the absence of some compulsion or duty, pays the debt of another.”. Since Texas American did not pay under a legal duty to do so, and was not acting to protect its interests, and because it received no assignment of rights from either Ruidoso State Bank or the Wests, the subrogation argument fails.

Withers v. Board of County Com’rs of San Juan County, 96 N.M. 71 (App.), 628 P.2d 316 (1981)

Facts:

- Douglass bought land in 1968 on a REC.
- In 1979, the County published a bid invitation for property adjacent to Douglass’ land. The invitation provided that if the successful bidder did not own any property adjacent to the subject property, then any adjacent landowner would be allowed to meet the successful bid.
- Withers, a non-adjacent landowner, was the successful bidder. Douglass was allowed to meet the bid.
- Withers sued for an injunction and damages. Trial court granted summary judgment to defendants.

Issue: Is the purchaser under a REC an “owner” of real property, and entitled to meet the successful bid?

Holding: Citing *Marks* and *Mesich*, the Court applied the doctrine of equitable conversion and concluded that “...the vendee is treated as the owner of the land and holds an interest in real estate.”.

Connelly v. Wertz, 115 N.M. 803 (App.), 858 P.2d 1282 (1993) (overruled by *Southwest Land*)

Facts: REC purchasers failed to pay taxes; property was sold pursuant to tax sale statute; seller then declared forfeiture for nonpayment of installments; suit to quiet title followed.

Issues: Under NMSA 1978, sect. 7-38-70(B), which provides that the deed from the state to the buyer

“conveys all of the former property owner’s interest in the real property as of the date the state’s lien for real property taxes arose...subject only to perfected interests in the real property existing before the date the property tax lien arose.”,

- (1) whether a seller under a REC is a “former real property owner”, and
- (2) whether a seller under a REC holds a “perfected interest”.

Holding:

- (1) The purchaser, and not the seller, is a “former real property owner”, because the seller holds legal title only as trustee for the purchaser, and the seller’s interest is personalty, not realty. (citing *Marks*)
- (2) The seller’s interest in the real estate contract is personalty. The REC is a writing concerning the sale of land and thus falls under the recording act, and becomes a perfected interest when duly recorded. The Court also noted that it was the long-standing policy of the Taxation and Revenue Department to treat recorded real estate contracts as perfected interests. The tax sale deed did not convey the seller’s interest in the land, and the tax sale purchaser took his deed subject to the perfected security interest of the seller.

Southwest Land Investment, Inc. v. Hubbard, 116 N.M. 742, 867 P.2d 412 (1993)

Facts & Issues: Same as Connelly.

Holding:

- (1) The Supreme Court faults the Court of Appeals for failing to take into account that the Property Tax Code defines “owner” as “the person in whom is vested *any title* to property”. Section 7-35-2(F). (Emphasis added by the Court). “Because a vendor holds legal title and because the Property Tax Code defines “owner” as the holder of *any title*, the vendor under a real estate contract is an “owner” under the Code. To the extent that *Connelly v. Wertz* is inconsistent with this holding, it is hereby overruled.”
- (2) A vendor in a real estate contract holds several interests in the property:
 - a legal interest in the title to the land;
 - a reversionary interest in the property; and
 - an equitable personalty interest in the contract secured against third parties by a lien on the real estate.

The legal title was conveyed by the tax deed, because “legal title is clearly an interest in real property”. The reversionary interest was also lost because the legal title was lost.

The personalty interest was also conveyed by the tax deed. The Property Tax Code states that “*all* of the former property owner’s *interest in the real property*” is conveyed. The legislature did not limit the word “all”. “Southwest was an owner under the Code and its perfected security interest was an interest “in the real property”, and the interest was conveyed along with all of Southwest’s other interests in the property.

The Court notes that the 1973 amendment to the tax sale statute established stricter requirements regarding the state's duty to give notice to interested parties of an impending tax sale, and provided that owners can protect their interests, once they receive notice of the pending tax sale, only by paying their taxes or by challenging the validity of the tax sale pursuant to section 7-38-70(D) after the sale has actually taken place.

Comment: Without expressly saying so, the Court also overruled the Court of Appeals on its holding that the seller's perfected security interest is not conveyed by the tax deed. The Court agrees that the seller does hold a perfected security interest, but because that interest is held by a former 'owner', it is conveyed by the tax deed. Implicitly, then, perfected security interests held by persons who are not former owners, would not be conveyed by the tax deed, and title acquired by the tax sale purchaser would be subject to those perfected security interests.

Hertzmark-Parnegg Realty, Inc. v. Hunt v. Wilson et al, 99 N.M. 184, 656 P.2d 234 (1982)

Facts:

- Hertzmark, a real estate broker, introduced Hoffman to Hunt, his client, as a prospective purchaser. No sale was made.
- Hunt later sold the property to Wilson, who then assigned his interest in the property to Hoffman. At the closing, Hunt signed a deed that conveyed the property to Hoffman's limited partnership.
- At all material times, Hertzmark had a listing agreement with Hunt, which provided that Hertzmark would receive a commission if the property was "sold, exchanged or conveyed" to any purchaser introduced by Hertzmark to his client.
- Hertzmark sued Hunt to recover a commission. Hunt impleaded Wilson and Hoffman. Trial Court dismissed Hertzmark's complaint. Appealed.

Issue: Was the property "sold, exchanged or conveyed" within the meaning of the listing agreement when Hunt signed a purchase agreement with Wilson, or when Hunt deeded the property to Hoffman?

Holding: Affirmed. Citing *Mesich*, *Gregg*, *Hobbs* and *Marks*, the Court invokes the equitable conversion doctrine to hold that "...Wilson acquired the property once Hunt signed the purchase agreement with him.". The signing of the purchase agreement made Wilson the equitable owner of the property. "The legal title is held by the vendor as a naked trust for the vendee and any conveyance by him to one not a bona fide purchaser for value is ineffective to pass title." (quoting from *Mesich*). Therefore, the sale occurred when the purchase agreement was signed, not at the later date when Hunt conveyed to Hoffman, and Hertzmark may not recover a commission.

COMPLEX CONTRACTS: ASSUMPTION AGREEMENTS

Kuzemchak v. Pitchford, 78 N.M. 378, 431 P. 2d 756 (1967)

Facts:

- REC with escrowed deeds provided that buyer would assume a first mortgage. The warranty deed was "subject to..." the mortgage.
- The seller's equity was paid off and the warranty deed was delivered from escrow and recorded.
- The buyer defaulted on the mortgage, which was foreclosed. Deficiency judgment was entered against the sellers, who sued the buyers for reimbursement under the "assumption clause" in the REC. Trial court ruled for the buyers, on the basis that the REC was merged into the warranty deed.

Issue: Does the buyer's REC obligation to assume and pay a senior obligation merge into the warranty deed delivered from escrow and recorded, so that buyer has no further liability to seller upon default on the mortgage?

Holding:

1. Generally, delivery and acceptance of a deed in pursuance of a contract for the sale of land merges the covenants of the prior contract in the deed, and the rights of the parties are governed solely by the deed.
2. The rule does not apply to collateral obligations in the contract of sale for which delivery of the deed is not a performance.
3. If the obligation has reference to title, possession, quantity, or emblements of the land, it is generally held to inhere in the very subject matter with which the deed deals and is merged therein.
4. A covenant to assume a mortgage debt is a collateral and independent obligation that is not merged in the deed.

HUD Rule, 24 C.F.R. Chapter II Sect. 203.510 Release of personal liability.

- (a) *Procedures.* The mortgagee shall release a selling mortgagor from any personal liability for payment of the mortgage debt, if release is permitted by sect. 203.258 of this part, in accordance with the following procedures:
 - (1) The mortgagee receives a request for a creditworthiness determination for a prospective purchaser of all or part of the mortgaged property;
 - (2) The mortgagee or servicer performs a creditworthiness determination under sect. 203.512(b)(1) of this part if the mortgagee or servicer is approved for participation in the Direct Endorsement program, or the mortgagee requests a creditworthiness determination by the Secretary;
 - (3) The prospective purchaser is determined to be creditworthy under the standards applicable when a release of the selling mortgagor is intended;
 - (4) The prospective purchaser assumes personal liability by agreeing to pay the mortgage debt; and
 - (5) The mortgagee provides the selling mortgagor with a release of personal liability on a form approved by the Secretary.
- (b) *Release after 5 years.*

- (1) If a selling mortgagor is not released under the procedures described in paragraph (a) of this section, either because no request for a creditworthiness determination is submitted under paragraph (a)(1) of this section, or because there is no affirmative determination of creditworthiness under paragraph (a)(3) of this section, then the selling mortgagor is automatically released from any personal liability for payment of the mortgage debt because of section 203® of the National Housing Act if:
 - (i) The purchasing mortgagor has assumed personal liability by agreeing to pay the mortgage debt;
 - (ii) Five years have elapsed after the assumption; and
 - (iii) The purchasing mortgagor is not in default under the mortgage at the end of the five-year period.
- (2) If the conditions of this paragraph (b) for a release are satisfied, the mortgagee shall provide a written release upon request to the selling mortgagor.
- (3) This paragraph (b) only applies to a mortgage originated pursuant to an application by the mortgagor on or after December 1, 1986 on a form approved by the Secretary.

(c) *Mortgagee to provide notice.* A mortgagee shall inform mortgagors (including prospective mortgagors seeking information) about the procedures for release of personal liability by providing a notice approved by the Secretary when required by the Secretary.

[58 FR 42649, Aug. 11, 1993]

PRINCIPAL and INTEREST

Edward H. Snow Development Company, Inc. v. Oxsheer, 62 N.M. 113, 305 P.2d 727 (1957)

Facts:

- Oxsheer entered into a binder agreement to sell vacant lots to Snow for purchase price of \$60,000 with \$10,000 down payment and “Bal. of 50,000 to be paid as lots are released at purchaser’s convenience. This is on an equal amount per lot basis”.
- The parties dickered for months over a payment schedule, but never arrived at an agreement as to payment of the deferred balance.
- Oxsheer declared the binder void and started selling lots to other parties.
- Snow sued for specific performance. Trial court ruled for Oxsheer, holding that the binder was so uncertain and indefinite as to the maturity of the deferred balance that it was incapable of specific performance. Appealed.

Issue:

Where the contract does not include a ‘time is of the essence’ clause, will a court of equity imply a reasonable time for performance, set a time for performance, and grant specific performance?

Holding:

Affirmed. Quoting the Supreme Court:

“The rule that performance must be made within a reasonable time...will not be applied by a court of equity where the contract contains a provision for deferred payment of the balance of the consideration, and thus a court of equity will not decree specific performance of a contract which does not itself set a time for payment of a deferred balance”.

The Court quoted the following language from 81 C.J.S., Specific Performance, sect. 34, p. 493 in support of its holding:

“‘Where it is the intention of the parties to defer payment, but no provision is made as to the time of payment, the uncertainty is fatal; but mere failure to fix a time for payment will not prevent specific performance where *deferred* payment was not contemplated.’ (Emphasis ours.)”

TAXES and INSURANCE

Boatwright v. Howard, 102 N.M. 262, 694 P.2d 518 (1985)

Facts:

- Boatwright sold improved land on REC to Howard. The contract contained provisions requiring the purchaser to maintain insurance on the property. That provision and the default and forfeiture clause were essentially identical to the form 103 clauses.
- Boatwright sued Howard, alleging a failure to maintain insurance on the property as required by the contract, and seeking restitution of the property and other relief. Howard filed a motion for summary judgment; trial court granted the motion & Boatwright appealed.

Issue:

Whether the cost of insurance is a charge within the meaning of the phrase, “other charges against the Real Estate” contained in the contract.

Holding:

Affirmed.

- The default provision of the REC did not list failure to maintain insurance as one of the events for which a default could be declared, although it did provide that the seller could insure the property, then demand reimbursement for the amount of premium paid. Thus, seller’s demand that purchaser obtain insurance on the property could be sustained only if the cost of insurance fell within the meaning of the phrase, “*or other charges against said Real Estate*”.
- The Court concluded that “charges against the Real Estate” means “...those costs which, if not paid, could become liens or affect the title to the real estate by casting a cloud upon it. Insurance is not such a cost. It is not a cost *against the real estate* that could be satisfied out of the real estate.”
- The Court noted that the Boatwrights had other adequate remedies under the agreement. “They could have sued to enforce the insurance provision or, in the alternative, they could have paid the insurance premiums and then sought reimbursement from the Howards.”

RESTRAINTS on ALIENATION

DeBaca v. Fidel, 61 N.M. 181, 297 P.2d 322 (1956)

Facts:

- DeBaca leased real property to Fidel for 25 years.
- Fidel sublet the property to another party on a month-to-month basis.
- The lease stated that “tenant shall not...assign or transfer this lease without the written consent of the landlord”.
- DeBaca sued for restoration of the property and damages. Trial court awarded summary judgment to Fidel.

Issue:

Whether or not the sublease constituted an assignment or transfer of the leasehold in violation of the lease.

Holding:

Affirmed.

- A sublease for a shorter period than the term of the original lease does not violate the prohibition against assignment.
- The Court recognizes a clear distinction between an assignment and a sublease:

‘An assignment transfers the entire interest in the leasehold...A subletting is a grant of a portion of the term, with some reversionary interest in the sublessor’.

- The Court cited the general rule that a sublease does not violate a covenant against assignment, and an assignment does not violate a limitation on the right to sublease.
- As to restraints generally, the Court follows the rule that ‘Reasonable restrictions upon the alienation of property are enforced, but they are rigidly construed so as to confine their operation within the exact limits defined by the precise terms of restraint’.

State ex rel. Bingaman v. Valley Savings & Loan Association, 97 N.M.8, 636 P.2d 279 (1981)

Facts:

- NMSA 1978, sections 48-7-11 & 48-7-12, became effective March 15, 1979, and provided that clauses in mortgages or deeds of trust, securing an interest in residential property consisting of not more than four housing units, which either allow accelerated payments or increased interest rates upon a transfer of the mortgaged property may constitute an unreasonable restraint upon alienation and therefore are unenforceable, except where a mortgagee’s security interest is proven to be substantially impaired.
- Valley and other defendants had adopted due-on-sale clauses in their uniform mortgage instruments, approved by FNMA and FHLMC, which provided that upon a sale or transfer of the property without the lender’s prior written consent, the lender may, at its option, declare the unpaid balance of the loan to be immediately due and payable.
- The N.M. Attorney General sued for a declaratory judgment that the clauses were unenforceable under the statute, for restitutionary relief and for civil penalties. The district court ruled for the Attorney General, and held the statute to be applicable to mortgages executed prior to March 15, 1979. Appealed.

Issues:

1. Whether a due-on-sale clause is a reasonable restraint on alienation;
2. Other issues involving the standing of the A.G. to bring the suit, and the granting of restitutionary relief, are not discussed here.

Holding: Affirmed.

1. At common law, restraints on alienation were prohibited. New Mexico has interpreted the common law rule to mean that reasonable restraints upon the alienation of property are enforceable, but will be construed to operate within their exact limits (citing *DeBaca*). The New Mexico Legislature "...has adopted this view by adopting the common law in Section 38-1-3, N.M.S.A. 1978".
2. The Court observed that whether a due-on-sale clause is a reasonable restraint upon alienation is a matter of first impression in New Mexico, and it stated two views from other jurisdictions on the subject:
 - (a) Due-on-sale clauses are not per se invalid; their validity depends upon the reasonableness of the underlying purpose of the restraint;
 - (b) Due-on-sale clauses may be validly exercised only if a legitimate interest of the lender is threatened. The protection of the lender's security is a recognized legitimate interest.

Without discussion or explanation, the Court stated its preference for the second view, and held: "...based upon common law principles, that due-on-sale clauses which either permit acceleration of payment or increased interest rates upon transfer of the property or assumption of mortgages without a showing of substantial impairment to the lender's security interest are unenforceable as unreasonable restraints upon alienation."

3. Without discussion, the Court held the statute to be applicable to mortgages executed prior to the effective date of the statute, March 15, 1979. Two justices dissented from this holding, on the basis that it "...impermissively infringes on the right to contract".

Comment: Sections 48-7-11 through 48-7-14 were repealed effective April 7, 1983, due to preemption by *Garn*. That Act preempted New Mexico law restricting enforcement of due-on-sale clauses, except as to loans made or assumed during the period March 15, 1979 through October 15, 1982. To regulate due-on-sale clauses in loans made or assumed during that "window period", the Legislature in 1983 enacted sections 48-7-15 through 48-7-24.

Brummond v. First National Bank of Clovis, 99 N.M. 221, 656 P.2d 884 (1983)

Facts:

- Defendant held a \$150,000.00 promissory note from Plaintiff, secured by certain personal property located in a motel and secured also by a commercial mortgage covering real estate. Plaintiff sold the personal property and the real estate without seeking the consent of the Defendant. Defendant thereupon declared a default on the note and accelerated the balance. The security agreement contained a due-on-sale clause.
- The trial court held the due-on-sale clause to be an unreasonable restraint on alienation at common law, and therefore unenforceable.

Issue:

The Court was called upon to determine the impact on the subject due-on-sale clause of Section 55-9-311 of the New Mexico Uniform Commercial Code-Secured Transactions, which is quoted as follows:

"The debtor's rights in collateral may be voluntarily or involuntarily transferred (by way of sale, creation of a security interest, attachment, levy, garnishment or other judicial process) notwithstanding a provision in the security agreement prohibiting any transfer or making the transfer constitute a default."

Holding:

The Court held that the effect of Section 55-9-311 was to validate the transfer of the debtor's interest in the collateral to his purchaser. It does not destroy or limit the seller's prior perfected security interest. Therefore, although the sale does effectively transfer the debtor's interest in the collateral, the sale can still be an event of default entitling the seller to accelerate the balance, pursuant to the due-on-sale clause.

The Court also overruled the holding that the due-on-sale clause in the security agreement constituted an unreasonable restraint on alienation of property at Common Law. The Court stated that "...nothing in ... the security agreement serves to restrain the Plaintiff's right to transfer the collateral." It merely makes such transfer an event of default which triggers the due-on-sale clause. The Court also held that "the Common Law was displaced by the Uniform Commercial Code as adopted in New Mexico." Finally, the Court ruled that its prior decision in *Bingaman* did not apply to the facts of this case, because that case and the statute upon which it was decided (Section 48-7-1 1, NMSA 1978) were concerned only with transfer of residential property.

Comment:

This case did not involve a real estate contract. However, the decision is very important in its predictable application to REC's in several critical aspects:

- The Court reaffirmed its prior holding in *Foreman v. Myers*, 79 N.M. 404, 444 P.2d 589 (1968) that "an acceleration clause will be enforced in both law and equity." Such a clause does not constitute an unreasonable restraint on alienation of property at Common Law.
- Some parts of this decision must be carefully limited to acceleration based on sales of personal property as contrasted to real estate. For example, the U.C.C. article on secured transactions does not apply to transfers of real estate. Section 55-9-104(J). Therefore, the Court's statement that the U.C.C. had displaced the Common Law on restraints on alienation must be understood to apply only to restraints on alienation of personal property. The Common Law rule regarding restraints on alienation of real estate is still applicable to real estate contracts, mortgages and other conveyances of real estate.
- Nevertheless, it is clear that the Court in this case was also ruling on the validity of a due-on-sale clause in a real estate mortgage, and found that the clause does not violate the Common Law rule against restraints on alienation. This point is made in only one section in the entire written opinion, but that sentence is clear:
"We conclude that a provision in a security agreement and in a commercial mortgage making an unconsented transfer of commercial personalty **and realty** an event of default, and giving rise to an option to accelerate the balance due, is not a restraint on alienation in violation of the Common Law."

Paperchase v. Bruckner, 102 N.M. 221, 683 P.2d 587 (1985)

Facts:

- Paperchase sold to Bruckner on a form 103 REC which contained this clause: "It is further understood and agreed that no assignment of this contract shall be valid unless the same be endorsed hereon and countersigned by the owner."
- Bruckner re-sold to A & O Investments on a new REC, the buyer assuming the existing REC.
- Paperchase sued for a declaratory judgment that it could either accelerate the balance or, alternatively, forfeit the buyer's interest in the property. Trial court granted summary judgment to Bruckner; appealed.

Issue:

Does the re-sale on an assumption REC violate a provision prohibiting assignment?

Holding:

The junior contract did not operate as a true assignment and does not violate the clause:

"According to the Restatement (Second) of Contracts, Section 328 (1979) ... an assignment of the contract is both an assignment of the assignor's rights and a delegation of his duties. But a provision prohibiting assignment of the contract bars only the delegation of duties... Consequently, in most cases, if there is no delegation of duties, there is no violation of the prohibition on assignment."

"Since the Bruckner/A & O contract was not designed to relieve the Bruckners of their liabilities to Paperchase, we agree that that contract does not operate as a true assignment....".

"Since neither the Bruckner/A & O or the A & O/Yu contracts attempted to relieve Bruckners of their responsibilities to Paperchase, the clause was not violated. The particular individuals on whom Paperchase chose to rely for payment of the purchase price, Bruckners, have remained in contact with the land and in privity of contract with Paperchase."

Comment:

While the Court's holding is agreeable, its reasoning is troublesome. A 'true' assignment does not purport to relieve the assignor of his contract obligations. It may delegate or transfer them to an assignee, but it cannot discharge the assignor's liability unless the seller releases him and agrees to substitute the assignee, in which case a 'novation' occurs.

It would have been enough to say that a re-sale contract does not involve an attempt to place the junior buyer in *privity of contract* with the seller. An "assumption" REC, as opposed to a "wrap", does involve a delegation of duties, but it does not attempt to place the junior buyer in privity with the seller. It would seem that since the buyer can do nothing unilaterally to extinguish his liabilities, the real objection to an assignment would be the attempt to transfer the buyer's RIGHTS to another party. The bar prevents seller from involuntarily being burdened with obligations to a party with whom he did not enter into a contract.

Oddly, the Court does not cite the *DeBaca* decision. Although that case dealt with a lease rather than a sale, the common law distinction between *alienation by substitution* and *alienation by subinfeudation*, which is implicit in the *DeBaca* Court's reasoning, would seem to be applicable to the distinction between sale by assignment and sale by assumption. Prior to adoption of the statute of Quia Emptores, which abolished common law subinfeudations, feudal restraints against alienation were avoided by use of the subinfeudation, which created a subordinate feud while leaving the existing feud undisturbed. See *61 Am Jur 2d Perpetuities, Etc. sect.101*.

Gartley v. Ricketts, 107 N.M. 451, 760 P.2d 143 (1988)

Facts:

- Cunningham gave a warranty deed to her sister, Gartley, for a tract of farm land, pursuant to an agreement which contemplated that Gartley would build a house on the property for her own use. The agreement and deed contained this condition, among others:

'So long as Grantor lives, Grantee nor her heirs or assigns may sell the tract of land, and the home which Grantee will build thereon, to any person or firm, nor shall she or her heirs rent the same to any person or firm; provided, however, each of the same may be done with the written consent of the Grantor.'

- Shortly thereafter, Gartley, without notice or consent of Cunningham, conveyed the property for consideration to herself and her daughter, Schriber. The house was partially constructed, but never completed, and remained occupied.

- Thirteen years later Gartley & Schriber filed a complaint to reform the deed to void the condition as being a cloud on their title. They alleged the condition was void as a restraint on alienation. Ricketts, the daughter of the then-deceased Cunningham, was named as defendant.
- The trial court held that the condition was an unreasonable restraint upon alienation, and reformed the deed to convey a fee simple title to Gartley. Ricketts appealed.

Issues:

1. An issue as to whether another condition on the deed, giving Ricketts a right of first refusal to purchase the property, constituted a violation of the rule against perpetuities, was decided against Ricketts, but is not discussed here.
2. Whether the condition subsequent constituted an unreasonable restraint on alienation.

Holding:

Affirmed.

1. “New Mexico has adopted and interpreted the common law rule against restrictions on alienation to mean that ‘reasonable restraints upon the alienation of property are enforceable, but will be construed to operate within their exact limits.’” (The Court quoting from *Bingaman*).
2. In determining whether a particular restraint is reasonable, the Court adopts the factors listed by the Restatement of Property (2d), sect. 4.2:
 - (a) The restraint is limited in duration;
 - (b) The restraint is limited to allow a substantial variety of types of transfers to be employed;
 - (c) The restraint is limited to the number of persons to whom transfer is prohibited;
 - (d) The restraint is such that it tends to increase the value of the property involved;
 - (e) The restraint is imposed upon an interest that is not otherwise readily marketable; or
 - (f) The restraint is imposed upon property that is not readily marketable.

Here, the restraint offended factors (a) and (c), and is held to be an unreasonable restraint on alienation.

State ex rel. Bardacke v. New Mexico Fed. Savings & Loan, 102 N.M. 673, 699 P.2d 604 (1985)

Facts:

- Effective March 15, 1979, sect. 48-7-11 to –14 NMSA 1978 declared due-on-sale clauses in mortgages to be unenforceable. After that date, N.M. Federal made various mortgages which contained due-on-sale clauses (the clauses were identical to the clauses considered in *Bingaman*, and would therefore be in violation of the statute).
- On June 22, 1981, N.M. Federal converted from a state-chartered association to a federal association, and thereafter continued to enforce its due-on-sale clauses contained in mortgages made before the conversion date.
- In 1982, the *Garn* Act made due-on-sale clauses enforceable by federal associations. However, the Act also provided that in the case of loans made or assumed after the date any state adopted a statute prohibiting the exercise of due-on-sale clauses, and ending on October 15, 1982, the provisions of the Act making due-on-sale clauses enforceable would apply only in the case when a transfer occurs on or after October 15, 1985.
- In 1983, the N.M. Legislature repealed sect. 48-7-11 to –14, to conform to *Garn*. However, the unenforceability of due-on-sale clauses made or assumed during the period March 15, 1979 through October 15, 1982 was continued in effect except that a limited increase in interest was allowed. Sect. 48-7-15 to –20, NMSA 1978.
- The Attorney General filed suit for declaratory and injunctive relief to prevent enforcement of due-on-sale clauses by N.M. Federal as to mortgages made or assumed after March 15, 1979. Trial court granted partial summary judgment to the State. Appealed.

Issues:

1. Procedural issues are not discussed here.
2. Whether *Garn* made due-on-sale clauses enforceable by federal associations under the facts of this case.

Holding:

Affirmed.

1. The exception specified in sect. 1701j-3©(1)(A) of *Garn* causes the result that "...due-on-sale clauses in mortgages originated by state-chartered associations during the statutory period are not enforceable...where state law has made due-on-sale clauses unenforceable."
2. The Court further stated that it "...will not extend federal regulation of due-on-sale clauses to mortgages which were made by savings and loan associations chartered under state law prior to their conversion to federally chartered associations".
3. Because the district court's ruling included mortgages made or assumed after June 22, 1981, the date N.M. Federal converted to a federal association, the Court remanded the case to correct the decree to limit the order to the period ending June 22, 1981.

Cowan v. Chalamidas, 88 N.M. 14, 644 P.2d 528 (1982)

Facts:

- Commercial lease, which was not assignable by lessees without lessor's consent, "which shall not be unreasonably withheld".
- Lessor refused to consent to assignment on grounds that assignees were financially unstable.
- Lessees abandoned the property.
- Within a week after the lessees abandoned the property, lessor leased the property directly to the rejected assignees.

Holding:

Withholding of consent was unreasonable where lessor leased to same prospective tenants within a week after refusing to consent to assignment.

Boss Barbara, Inc. et al v. Newbill, 97 N.M. 239, 638 P.2d 1084 (1982)

Facts:

Commercial lease agreement prohibited sublease or assignment of the lease without first obtaining the lessor's written consent. Sub-lessee requested approval for a second sub-lease; lessor refused. Sub-lessee sued for a declaration that lessor could not unreasonably withhold consent. Trial court ruled for sub-lessee; Court of Appeals reversed; Supreme Court granted certiorari.

Issue:

Whether a landlord may unreasonably and arbitrarily withhold consent to a subleasing agreement when the lease agreement provides that the tenant must obtain the written consent of the landlord before subleasing.

Holding:

Reversed.

- The Court noted that the issue was one of first impression in New Mexico, and that the majority of jurisdictions had adopted the rule that a landlord may withhold his consent without justification. It also observed that the trend in recent years had been to require the landlord to act reasonably when withholding consent to sublease.

- The Court adopted the latter view, reasoning that 'a lease, being a contract, should be governed by general contract principles of good faith and commercial reasonableness'. Therefore, a landlord must act reasonably when withholding consent to sublease, and cannot arbitrarily withhold consent. Consent is not to be withheld unless the prospective tenant is unacceptable, using the same standards applied in the acceptance of the original tenant.
- Citing *DeBaca* and *Bingaman*, the Court restated the rule that 'reasonable restraints upon the alienation of property are to be strictly construed so as to operate within their exact limits'. In this case, because the language in the lease was silent as to whether the lessor could arbitrarily withhold consent or must withhold only on reasonable cause, the Court construed the language to require reasonableness.

Comment:

The Court's opinion left open the possibility, even if slight, that it may hold otherwise if the language of the lease clearly stated that the lessor would be under no obligation to give consent.

Economy Rentals, Inc. v. Garcia, 112 N.M. 748, 819 P.2d 1306 (1991)

Facts:

- Car dealer leased lot from Economy, attempted to transfer lease to another dealer.
- The lease provided that written consent would not be unreasonably withheld.
- Original lease had rent payments of \$3,000/month, sub-lease rent would have been \$10,500 per month.

Issue: Can lessor withhold consent to a lease assignment for purpose of improving the terms of his lease?

Holding:

Withholding of consent was unreasonable. The Court adopts a test of reasonableness:

"A lessor may refuse consent when the proposed assignment or sublease would injure or impair the lessor's interest in the leased property, such as by devaluing it (and thereby reducing the benefits bargained for in the original lease), but not when the lessor seeks to improve its economic position, such as by sharing in the sublease rent or by securing a benefit not bargained for in the original lease.... the lessor's interest to be protected by refusing consent must relate to the ownership and operation of the leased property, not the lessor's general economic interest."

The Court agreed with the trial court's conclusion that the lessor's primary motivation was 'the forbidden one of increasing the economic benefit of the lease. As such, it was unreasonable'.

Comment:

The Court modifies the test stated in two previous cases: "The statement in *Boss Barbara*, reiterated in *Cowan*, that a tenant's acceptability must be gauged by the same standards as were applied when the original lease was entered into was not meant to limit all bases for refusing consent to those expressed or implied in the original lease. Many circumstances may change;..".

Naumburg v. Pattison, 103 N.M. 649, 711 P.2d 1387 (1985)

Facts:

- This case focused on interpretation of portions of the New Mexico Residential Home Loan Act, 56-8-22 to 56-8-30 NMSA 1978. Sections 56-8-25 to 56-8-28, relating to rates of interest on home loans, had been repealed in 1981. The remaining provisions related to prepayment penalties on home loans. Section 56-8-30 provided:

“No provision in a home loan, the evidence of indebtedness of a home loan, a real estate contract or an obligation secured by a real estate mortgage requiring a penalty or premium for prepayment of the balance of the indebtedness is enforceable”.

The statute defined “home loan” to mean, among other things, in section 56-8-24 B(2), “the deferred balance due under a real estate contract made for the purchase or sale of a residence;”. Finally, section 56-8-24 A. defined “residence” to mean “...a dwelling and the underlying real property designed for occupancy by one to four families; and includes mobile homes and condominiums;”.

- In 1982, Naumburg entered into a REC with Pattison to purchase a tract of land and house (log cabin) in Taos County. The contract had an unpaid balance of \$100,000, and required annual payments of interest at 20% per annum, or \$20,000, for a period of ten years, when the principal would be due in one lump sum. The REC also contained the provision, “buyer shall *not* have the right of prepayment during the pendency of the contract”.
- In 1983, Naumburg’s attorney notified Pattison’s attorney that Naumburg intended to ‘shortly pay the outstanding balance on the Real Estate Contract between the parties’. Pattison’s attorney responded that he considered the prohibition against prepayment to be enforceable.
- Naumburg filed a Complaint seeking a declaratory judgment, an injunction and damages for Pattison’s refusal to accept prepayment. Trial Court ruled that the RHLA did not apply because the property was not purchased as a principal residence, is not a residence within the definitions of the Act, and the REC is not a home loan as defined in the Act.

Issues:

1. Does the RHLA apply to a log cabin vacation home?
2. Does a contractual provision that completely prohibits prepayment constitute a penalty within the meaning of the Act?

Holding:

1. The log cabin was a structure designed for single-family use, notwithstanding its location in a commercial area. It therefore fits the statutory definition of residence. The RHLA makes no distinctions based on the locale of the property, and the statute contains no requirement that the dwelling be the primary family residence.
2. Although under common law principles, a purchaser had no right to prepay in the absence of a contract provision allowing him to do so, in this case the RHLA applies, so there is no need to resort to common law principles. The RHLA confers the statutory right to prepay. “It is self-evident that a complete prohibition against prepayment is a penalty of the most extreme kind and, thus, is forbidden by the Act”.

Los Quatros, Inc. v. State Farm Life Insurance Company, 110 N.M. 750, 800 P. 2d 184 (1990)

Facts:

- Mortgage loan for the purchase of commercial, nonresidential property was made in 1980 by American Bank of Commerce to Pickard. ABC sold the note & mortgage to State Farm. In 1982, Pickard sold the property to Los Quatros, who assumed the mortgage.
- The Note provided that it could not be prepaid during the first twelve years, and provided for gradually reducing penalties for prepayment after the first twelve years.
- In 1988, Los Quatros attempted to prepay the note, State Farm refused the prepayment. Los Quatros filed suit for a declaratory judgment that it had a right to prepay. District Court ruled for Los Quatros; State Farm appealed.

Issues:

1. Whether section 48-7-19(A), NMSA 1978 (enacted in 1983), which prohibits enforcement of prepayment penalties in mortgages made or assumed between March 15, 1979 and October 15, 1982, is applicable only when there is a sale and the lender is exercising an option under the due-on-sale clause.
2. Whether the prepayment penalty prohibition provision of the 1983 enactment of 48-7-19(A) is applicable only to loans secured by residential real estate consisting of not more than four housing units, as provided in the 1979 Act, due to federal preemption provisions of the Garn-St. Germain Act.
3. Whether retroactive application of 48-7-19 to a mortgage made or assumed prior to the effective date of the statute unconstitutionally impairs the obligations of the mortgage contract.

Holding:

Affirmed.

1. Notwithstanding the apparent meaning of the statutory language when considered in context, the Court HOLDS that the last sentence of the section "...applies whether or not there has been a sale and whether or not the lender has sought to exercise its options under a due-on-sale clause.". The 1983 Legislature declared its intention to carry forward the 1979 Act's prohibition on enforcement of due-on-sale clauses in a window-period loan. The policy was to protect the borrower during periods of rising interest rates against enforcement of due-on-sale clauses, which would impair marketability of property, with a resultant burden on the state's economy. During periods of falling interest rates, lenders who prohibit or penalize prepayment effectively prevent or retard the borrower from refinancing at a lower rate, and effectively impair marketability of the property. The Court finds that "The statute's objective is to promote the alienability of land, whether interest rates are rising or falling. When they are rising, enforcement of due-on-sale clauses is prohibited (for window-period loans only); when they are falling, clauses (in window-period loans) preventing or restricting prepayment are not to be enforced.".
2. The Garn-St. Germain Act "preempts state regulation of enforcement of due-on-sale clauses, not enforcement or restriction of clauses barring or penalizing prepayment of loans.". Also, "...even if a prohibition on prepayment penalties is governed by the restriction on window-period loans in the Garn-St. Germain Act, that Act does not prevent a state from enlarging the class of loans subject to the prohibition, so long as they are 'real property loans' made or assumed during the window period.". The Court noted that although a Senate Report constituting a portion of the legislative history of Garn-St. Germain declared that state legislatures may not expand the types of loans to which the window-period applies, the limitation on state authority was not found in the statute itself. Indeed, "The exception to preemption in 12 U.S.C. sect. 1701j-3©(1)(A) permits a state to 'otherwise regulate such contracts,' 'such contracts' being real property loans originated in the state by lenders other than national banks, federal savings and loan associations and savings banks, and federal credit unions. There is no prohibition in the federal act on a state's 'expansion' of the preexisting limitations on enforcement of due-on-sale clauses from those applicable to loans secured by another, broader type.".

3. Even though there is a significant, and perhaps a substantial impairment of a contractual relationship (that being the contractual right of the lender to refuse prepayment and thereby to maintain the return on its loan portfolio at or above current market interest-rate levels), nevertheless, the prohibition on enforcement of a prepayment penalty "...is sufficiently justified by the significant and legitimate public purpose of promoting the alienability of land to withstand challenge under...our Constitution.". Even though the statute might be said to advance the interest of a particular group-borrowers versus lenders- the Court had "...no difficulty finding that promoting the alienability of land is a basic societal interest – even though the same 1983 Act which furthers this interest in window-period loans also promotes the countervailing interest [as to non window-period loans] of enhancing the secondary loan market by enforcing due-on-sale restrictions.".

ASSIGNMENTS

In Re Anthony, 114 N.M. 95, 835 P.2d 811 (1992)

Facts:

- Anthony sold real property under standard REC to Sanchez.
- Anthony borrowed \$10,000 from Alsup, gave Alsup a Note and secured it with a collateral assignment of seller's interest in the REC. Alsup recorded the assignment in the county clerk's office, but did not file a financing statement under Article 9 of the New Mexico UCC.
- Anthony filed bankruptcy; the trustee filed an action claiming priority to the contract payments. Bankruptcy Court held that because the Alsups failed to perfect their security interest by filing a financing statement in accordance with the UCC, their interest was subordinate to the trustee's interest. U.S. District Court affirmed.

Issue:

The U.S. Tenth Circuit Court of Appeals certified a question of state law to the state Supreme Court: Does a security assignment of a real estate contract fall within the provisions of Article 9 of the New Mexico UCC, thereby requiring the filing of a financing statement in the Office of the Secretary of State in order to perfect the secured interest against the claims of third parties; or, if such a security agreement falls within the Code, is it then excluded by Section 55-9-104(j) as a "transfer of an interest in or lien on real estate?"

Holding:

A vendor's interest in a real estate contract is personalty, and not real property (citing *Marks*). That does not alter the fact that this interest is also "an interest in or lien on real estate". Because the Anthonys held legal title when they assigned all their interest in the REC, and because the vendee's equitable interest is subject to divestment, "...we hold that this transaction involved the 'transfer of an interest in or lien on real estate' within the meaning of 55-9-104(j)". Accordingly, the perfection requirements of Article 9 do not apply.

Comment: The Court was also impressed by the history of the Official Comment 4. The amended version deleted the words "and mortgage" from the comment, and replaced them with "instrument", in the following statement:

'However, when the mortgagee in turn pledges this note *and mortgage* to secure his own obligation to X, this Article is applicable to the security interest thus created in the *note and the mortgage*'.

According to the Court, "The omission of the word 'mortgage' suggests that while the security interest in the note is subject to the Code, the question of whether the security interest is perfected in mortgage and similar security interests (including real estate contracts) is left to local real estate law."

MORTGAGES and DEEDS OF TRUST

McBee v. O'Connell, 19 N.M. 565 (1914) (no parallel cite avail.)

Facts:

- In June 1907, Santa Fe Land & Improvement Company sold a house and lot in Clovis to Ray, on an executory land sale contract.
- In October 1907, Ray assigned the contract to McBee, who paid the debt in full. McBee took possession and thereafter leased the property to Leeper. The property was occupied by Leeper until March of 1908, when O'Connell took possession, claiming to be a purchaser from Ray, without knowledge of any right or interest of McBee.
- At first trial, the trial court ruled for McBee. The Territorial Supreme Court reversed & remanded, on the basis that the acknowledgment of the assignment to McBee was defective, and rendered the contract unrecordable, and therefore ineffective to give constructive notice to a subsequent purchaser without actual knowledge of it.
- On the 2nd trial, a directed verdict was given to O'Connell, because McBee's evidence of title was not constructive notice under the laws of New Mexico. Appealed.

Issue:

Whether the occupancy and possession of McBee's tenant was such as would put a subsequent purchaser on notice of McBee's rights, or be such constructive notice of those rights as would negate the subsequent purchaser's claim of good faith as a bona fide purchaser.

Holding:

This being an issue of first impression in the new State of New Mexico, the Court adopts the rule and rationale of the Supreme Court of Oregon:

“A person who purchases an estate in the possession of another than his vendor is in equity, that is, in good faith, bound to inquire of such possessor what right he has in the estate. If he fails to make such inquiry, which ordinary good faith requires of him, equity charges him with notice of all the facts that such inquiry would disclose”.

The Oregon Court had further held that the possession of the tenant is sufficient to put the subsequent purchaser “upon inquiry” as to the landlord's rights, and to charge him with constructive notice of those rights if he fails to make such inquiry.

The Court stated an exception to the rule, not pertinent in this case, “...where the subsequent purchaser shows that he pursued an inquiry, with proper diligence, and failed to obtain the knowledge of the unrecorded instrument, or of the right of the parties claiming under it”.

Nelms v. Miller, 56 N.M. 132, 241 P.2d 333 (1952)

Facts:

- In 1937, Nelms contracted to sell farm land in Rio Arriba County to Miller. The REC required eight annual payments of interest only, and a balloon payment of principal at the end of eight years. Miller was also required to pay the property taxes. The documents were placed in escrow in Grand Junction, Colorado.
- Miller made few payments during the term of the contract; the parties carried on extensive written correspondence; annual due dates were extended twice. The principal was never paid.
- During his period of possession, Miller paid the taxes partly in cash & partly by use of his Soldier's exemption.
- In January, 1947, Nelms obtained the documents from the escrow agent, without the knowledge of Miller. Miller remained in possession and farmed the property. Correspondence between the parties continued, but Nelms never advised Miller that the documents had been retrieved from escrow.
- In February, 1947, Nelms leased the oil, gas & mineral rights to Cornell, who then assigned those rights to Magnolia Petroleum Co., who then assigned a ½ interest to Delhi Oil Corp.
- In 1949, Nelms deeded a ¾ interest in the minerals, oil & gas in & under the property to Cornell, subject to the lease. Cornell in turn deeded this interest to Curtis.
- Nelms sued to quiet title. Trial court ruled for Nelms, holding that Miller had forfeited his interest in the property, that the extended correspondence did not create a new contract and did not constitute an estoppel or an extension of the original purchase agreement, and that Curtis, Magnolia & Delhi were bona fide purchasers of the oil & mineral rights, without notice of any claim of Miller.

Issues:

1. Whether there was a valid forfeiture of purchaser's interests in the property;
2. Whether the subsequent purchasers were charged with notice of Miller's interest, if any, in the property.

Holding:

Reversed & remanded, with order that title be quieted in Miller, subject to the lien of Nelms for the purchase price and interest.

1. Nelms could not declare a forfeiture, for two reasons:

(a). "The mere failure to make stipulated payments does not make the contract void or work a forfeiture of it.". The Court quoted 3 *Black on Rescission and Cancellation*, sect. 569:

'Where a contract for the sale of real estate reserves to the seller the right to declare the contract void in case the purchaser shall make default in the payment of the price, failure to make the stipulated payments does not of itself make the contract void or effect a forfeiture, of it, but the vendor must give notice of his election and intention to forfeit the contract,...'.

(b). Citing various authorities, including *Black*, 107 A.L.R. 385, and 55 Am.Jur. 628,630, the Court ruled that

"A vendor cannot acquiesce in delay and then rescind, without giving notice of his intention to insist on strict compliance....Also, the right of forfeiture is waived by continuing negotiations, or, where an indefinite extension of time has been granted.".

2. "It is a general rule that open, notorious and exclusive possession of real estate under claim of ownership, is constructive notice to the world of whatever claim the possessor asserts, whether such claim is legal or equitable in its nature." (citing *McBee*). The Court then quoted from 8 *Thompson on Real Property*, section 4514, as support for the Oregon rule adopted in *McBee* which states that possession puts the purchaser upon inquiry as to the possessor's rights, and that one who fails to make such inquiry is affected with notice of such title or interest as the possessor actually has. Accordingly, Curtis, Magnolia & Delhi all were charged with a duty to inquire as to Miller's rights.

Citizens Bank of Clovis v. Hodges et. al., 107 N.M. 329 (App.), 757 P.2d 799 (1988)

Facts:

- Rutledge sold residence to Hodges on a REC, which was not recorded. Hodges took possession and continuously occupied the property as their residence.
- Citizens Bank obtained a judgment against Rutledge, and recorded a transcript of judgment in the county clerk's office. Citizens conceded that no inquiry was made as to whether the property was occupied.
- Two years later, Hodges notified Citizens Bank that its judgment lien was interfering with a pending sale of the property. Citizens sued to foreclose its judgment lien; Hodges counterclaimed for cancellation of the transcript of judgment. Trial court granted Citizens' motion for summary judgment.

Issues:

1. Whether a judgment lien on real estate has priority over the interest of the purchasers under an earlier executed but unrecorded contract.
2. Whether a judgment lien can attach to the ownership interest of a conditional sales vendor of real estate.

Holding:

1. The applicable statute, sect. 14-9-3 NMSA 1978 states:

“No deed, mortgage or other instrument in writing, not recorded in accordance with Section 14-9-1 NMSA 1978, shall affect the title or rights to, in any real estate, of any purchaser, mortgagee in good faith or judgment lien creditor, *without knowledge of the existence of such unrecorded instruments.*” (emphasis added by the Court).

Citing *McBee, Nelms* and *First National Bank of Belen v. Luce*, the Court quoted with favor from 8 *Thompson on Real Property* Section 4514, also quoted by *Nelms*:

“...Possession does not amount to constructive notice of the nature and extent of the rights of the person in possession, but it puts the purchaser upon inquiry as to such rights. He is bound to pursue the inquiry with diligence, and to ascertain what those rights are....A purchaser who negligently or intentionally fails to inquire as to the fact of possession, or as to the title or interests of the person in possession, is affected with notice of such title or interest as the possessor actually has....”.

An exception to the rule is made where the subsequent purchaser, mortgagee or judgment lien creditor shows he pursued an inquiry, with proper diligence, but failed to obtain the knowledge of the unrecorded instrument, or of the right of the parties claiming under it. *McBee*. The Court stated it would normally remand for a factual determination as to the exception; however, because Citizens conceded that it made no inquiry, reversal is proper.

2. Because the Court ruled that Citizens Bank had constructive notice of the Hodges' interest through Hodges' actual possession of the property, and the Bank's judgment lien therefore cannot attach to the property, the Court found no need to decide whether the doctrine of equitable conversion applies.

Comment: Due to other prior decisions of the Supreme Court, it is apparent that the Bank would have lost on the issue of equitable conversion, also.

Kuntsman v. Guaranteed Equities, Inc., 105 N.M. 49, 728 P.2d 459 (1986)

Facts:

- Equities, Inc. loaned \$14,435 to two joint borrowers (Conkling & Wilson) for purchase of real property. Equities funded the loan by raising money from two investors, Kuntsman & Holzapfel. Each investor contributed \$14,435 to the loan. Wilson executed a note and deed of trust to Equities as trustee for Kuntsman, which was recorded. Holzapfel's investment agreement with Equities also provided that he was to receive a note & deed of trust, but he received neither, and had no recorded title security interest.
- A court-appointed receiver for Equities received \$16,321.54 by a title company check payable to Equities, as trustee for Holzapfel. (The Court didn't elaborate, but presumably the funds represented the proceeds from either a sale of the Conkling-Wilson receivable, or from a payoff of the loan.)
- The receiver filed a motion to determine the priorities of the claims of Kuntsman & Holzapfel to the proceeds. The District Court concluded that both Kuntsman & Holzapfel were investors, and apportioned the proceeds between them. Kuntsman appealed.

Issue:

Whether Kuntsman & Holzapfel were equal creditors of Equities, Inc. or whether Kuntsman's claim is in the nature of a mortgage interest, and therefore entitled to priority under the recording statutes.

Holding:

Reversed. "...the deed of trust is, in essence, a mortgage and should be enforced as a mortgage." It therefore follows that the deed of trust is governed by the recording provisions of sections 14-9-1 to -2 NMSA 1978. Since Kuntsman's deed of trust was recorded, Holzapfel had constructive notice of Kuntsman's interest prior to the time Holzapfel invested in the property, and Kuntsman's claim has priority over Holzapfel's claim.

McInerny v. Guaranteed Equities, Inc. et al., 105 N.M. 207, 730 P.2d 1189 (1986)

Facts:

This case, essentially parallel to the *Kuntsman* case, was decided six weeks after that case. The fact pattern was basically the same, except that the junior investors had recorded security instruments:

- King obtained three separate loans of \$30,000 each from Equities, Inc., all secured by the same property. The investors, who contributed a total of \$90,000, were distributed in three separate investor "groups": Group I, Group II, and Group III. In October of 1981, King executed a note and "master" deed of trust to Equities, as trustee for the Group I investors, securing the first loan of \$30,000. This deed of trust was recorded. In December, King executed a \$60,000 note and "master" deed of trust to Equities, Inc. as trustee for the Group II investors. This deed of trust was also recorded. In March, 1982 King executed individual notes and deeds of trust to Equities, Inc. as trustee for the individually named Group III investors; these deeds of trust were also recorded.
 - King defaulted in July 1982 and quitclaimed the property to the trustee, as trustee for all the investors in the three groups.
 - In 1983, the court-appointed receiver sold the property for \$45,000. After a hearing to determine the distribution of the proceeds, the trial court apportioned the proceeds to all the investors on a pro rata basis. Group I investors appealed.

Issue: Same as *Kuntsman*, above.

Holding: The deeds of trust are essentially mortgages, and their relative priority is determined by the real estate recording statute. The investors in Groups II and III all had constructive notice of the existence of the first deed of trust, and therefore their claims are junior to the claims of the Group I investors. Any remaining proceeds after Group I is paid goes to Group II investors, in proportion to their contributions.

ESCROW AGENTS

Val Verde Hotel Co. v. Ross, 30 N.M. 270, 231 P.702 (1924)

Facts:

- Deed delivered in escrow, subject to conditions.
- The conditions were all satisfied but, through oversight, buyer did not claim the deed from escrow for several months.

Issue:

Whether title passed upon manual delivery or upon fulfillment of condition.

Decision:

"...Plaintiff was entitled to the delivery of the deed by the escrow holder. The deed belonged to the Plaintiff, and the grantor no longer had any power or control over the same. Under such circumstances, the delivery of the deed was complete, and title vested in the grantee, notwithstanding the manual delivery of the paper had not been made."

Albarado v. Chavez et al., 36 N.M. 186, 10 P.2d 1102 (1932)

Facts:

- In 1925, Albarado contracted to sell two lots to Chavez.
- In 1929, while this contract was still in force, Albarado & Chavez contracted to sell the property to Green, subject to the first contract. The intent was that Green was advancing to Chavez money to complete the purchase, and Green was taking title in his name as security for the money advanced to Chavez. Deeds were to be escrowed in the bank. However, the deed from Albarado to Green was never escrowed. Instead, Green placed it in his private box in the bank.
- Green paid the balance of the purchase price to Albarado's attorney in fact (Luskin). Green took the deed from his private box & recorded it.
- Luskin never accounted to Albarado for the moneys received. Albarado sued to quiet title; trial court ruled for Chavez & Green.

Issue:

Whether proof of delivery of the escrow deed is essential to contract purchaser's defense against quiet title action.

Holding:

Payment of the purchase price, to either vendor or vendor's attorney in fact, vests the equitable estate and title in the purchaser, sufficient to defeat vendor's claim to quiet title. "Manual delivery of the deed was not necessary to vest a title in the grantee named in it, sufficient to withstand application for the relief sought, if the conditions warranting its delivery had been duly performed." (citing *Val Verde Hotel Co.*)

Garcia v. Garcia, 111 N.M. 581, 808 P.2d 31 (1991)

Facts:

- In 1967, Annie Garcia contracted to buy a tract of land from son Julian & his spouse, Sheilah. Annie leased-back the property to a corporation owned by Julian & Sheilah. No deeds were placed in escrow. After making 30 payments, Annie was told by Julian that the REC was “all paid”, and that she should discontinue making payments.
- Julian died in 1984; Annie filed quiet title suit in 1987. Trial court ruled against Annie.
Note: This statement of facts is simplified to frame the issues. See the Opinion for full statement of facts.

Issues:

1. Whether the six-year statute of limitations on written contracts bars purchaser’s action to quiet title;
2. Whether the equitable defense of laches is available to vendor as a defense against purchaser’s action to quiet title after full performance of REC.

Holding: Affirmed.

1. After a contract purchaser has fully performed the contract, but has not received the deed of conveyance, the statute of limitations on claims to enforce written contracts cannot be asserted as a defense to a suit to quiet title, even though the statute would have barred an action on the contract for delivery of the deed. The Court held “...that a contract vendee’s claim of title, where the vendee has fully performed and whether or not he or she is in possession, is not cut off by the running of a statute of limitations.”. The Court cites *Albarado* (entire equitable ownership was in purchaser, even though deed was undelivered), *Conway v. San Miguel County Bd. Of Educ.*, 59 N.M. 242, 254, 282 P.2d 719, 727 (1955) (contract vendee had equitable title even though promise to convey never fulfilled), and *Mesich* and *Val Verde* cases. The Court noted that it had previously adopted the rule “...that an equitable owner in possession, whose possession is undisturbed, does not have to sue to convert his or her equitable title into legal title.”. (citing *Wooley v. Shell Petroleum Corp.*, 39 N.M. 256, 268, 45 P.2d 927, 934 (1935))
2. The equitable defense of laches, however, may be available despite the fact that a statute of limitations defense is not. The doctrine of laches “prevents litigation of a stale claim where the claim should have been brought at an earlier time and the delay has worked to the prejudice of the party resisting the claim.”. (For a full description of the elements required to establish the defense of laches, see the Opinion at p. 588.) In this case, the elements were all met to establish the defense. The injury or prejudice to Sheilah resulting from the delay in bringing the action (13 years from the accrual of the cause of action until Julian’s death) was that Julian was such a key witness that his death prejudiced Sheilah’s ability to conduct her defense.

Otero v. Albuquerque, 22 N.M. 128, 158 P.799 (1916)

Facts:

A deed placed in escrow was obtained by the buyer by false representations made to the escrow holder, and recorded. Thereafter, the city, which had been a lessee of the property from the grantor, entered into a new lease with the grantee.

Issue:

Whether title passed to the buyer, enabling the city to rely upon the second lease rather than the original lease.

Holding:

Delivery of a deed procured by fraud practiced upon the escrow holder was void, and transferred no title, even to a subsequent Purchaser without notice.

Roberts v. Humphreys et al., 27 N.M. 277 (1921)

Holding:

"Where a lease is put in escrow to be recorded upon the happening of certain events or the fulfillment of certain conditions, and such events do not happen and the conditions are not fulfilled, the recording of such lease without the consent of the lessor entitles him to have the lease declared null and void and the record thereof cancelled."

Mosley v. Magnolia Petroleum Co., 45 N.M. 230, 114 P.2d 740 (1941)

Facts:

- Mosley sold mineral rights to Asbury, by agreement the parties delivered deeds to mineral rights to a bank as escrow agent for 30 days. Asbury could pay the price within the 30 days and take the deeds; failing which, the escrow agent was instructed to return the deeds to Mosley.
- Asbury fraudulently obtained the deeds from the escrow agent without complying with the escrow agreement. He then altered the deeds & sold the rights to another party, who then sold them to Magnolia, who bought them without knowledge of the fraud or alterations.
- Magnolia struck oil, Mosley sued.
- Trial court held that Magnolia was an innocent purchaser, and that delivery of the deeds 'related back' to the deposit of the deeds in escrow.

Issue:

Whether a deed procured by fraud from the escrow agent conveys title to a subsequent bona fide purchaser for value, without knowledge of the fraud.

Holding:

Reversed. Generally, a deed delivered from escrow is effective upon the final date of delivery. The relation-back doctrine is invoked only when necessary to prevent an injustice, or to effectuate the intent of the parties. The doctrine cannot be applied to the facts of this case, because the deeds procured by fraud from the escrow holder were void, and transferred no title. Even a subsequent purchaser for value, without notice of the fraud, is not protected and acquires no title.

Martinez v. Martinez, 101 N.M. 88, 678 P.2d 1163 (1984)

Facts:

- Sale on REC, buyers assumed 1st mortgage (sale was from parents to son and daughter-in-law). REC was silent as to requirement for notice of default before exercising right of termination. REC did not contain a 'time is of the essence' clause.
- Sellers gave warranty deed to buyers, and instructed them to give it to the mortgagee, to hold in escrow until mortgage was paid off.
- Buyers recorded the deed before delivering it into escrow.
- Buyers defaulted on mortgage payments. Sellers cured the mortgage default, & sent letter to buyer notifying her that they were exercising their option under the REC to order buyer to reconvey the property to them.
- Buyer refused to reconvey; sellers sued to recover possession & title to the property. Trial court ruled for sellers.

Issues:

1. Whether delivery of the warranty deed was unconditional and, if so, whether the default provision in the REC was merged into the warranty deed.
2. Whether buyer received proper notice of sellers' intent to exercise the option to repossess the property.

Holding:

Reversed.

1. Delivery of the deed to buyers and recordation of deed did not convey title. Intent to transfer title is an essential element of delivery and the intent may be determined from the surrounding circumstances. The delivery was conditional, and failure of the condition prevented merger of the REC into the warranty deed. The default and reconveyance provisions of the REC remained in effect.
2. Because the REC did not contain a 'time is of the essence' clause and was silent regarding notice of default, the Court implied a stipulation to give reasonable notice and set not less than 30 days as a reasonable time to cure the default. "Time for compliance ordinarily is not of the essence of an agreement for the purchase and sale of land, and a reasonable time is generally implied unless the parties expressly make time of the essence in the contract." Where a contract contains an option to declare a forfeiture, the forfeiture is not self-executing. The right to declare a forfeiture "may be exercised only when (1) the vendor first gives notice for a reasonable period of time, and (2) the purchaser fails to pay during the time fixed by such notice".

Allen v. Allen Title Company, 77 N.M. 796, 427 P.2d 673 (1967)

Facts:

Purchasers delivered a personal check to escrow agent to pay off the contract balance. The escrow agent, without waiting for the check to clear, recorded the Warranty Deed. The check was subsequently dishonored. The NSF check was never paid. Seller sued the escrow agent for damages.

Issue:

It was conceded that the escrow agent negligently delivered and recorded the deed. The issue was the correct measure of damages for negligent recording of a deed by an escrow agent.

Holding:

- Although record title passed to the buyer, he acquired nothing thereby, and the seller can regain the title and clear the record in a proper action.
- Seller may recover an amount of money that will place him in as good a position as he would have occupied if the escrow holder had not breached its contract. "It would be no more than would be required to quiet the title-that is, to cancel the deed and place the record title back in [Seller]."
- Since no title passed, the escrow holder is not liable in damages for the value of the property, and its liability is limited to the costs and expenses which the seller would have to incur in recovering title.
- The Court added that had title been lost, the escrow holder would have been liable for the unpaid balance of the purchase price.

Dunlap v. Albuquerque National Bank, 56 N.M. 638, 247 P.2d 981 (1952)

Facts:

- Construction contract; separate escrow letter to bank instructed bank to pay over money to the contractor upon receiving an architect's certificate of completion.
- The contractor defaulted and the surety company arranged for a new contractor to finish the job. Upon completion, bank received the certificate of completion and released the escrowed money to the original contractor.

Issue:

Is the bank escrow agent liable for negligence in delivering the escrowed money to the original defaulted contractor, rather than the new contractor?

Holding:

Bank is not liable. It followed its instructions as stated. The bank was not a party to the separate construction contract, and is not bound by it.

Buhler v. Marrujo, 86 N.M. 399, 524 P.2d 1015 (1974)

Facts:

REC and deeds placed in escrow at bank, which wrongfully released deeds to the seller.

Issue:

Measure of damages.

Holding:

"The measure of damages is the amount of money that would place the Plaintiffs in as good a position as they would have occupied if Defendants had not breached their contract Plaintiffs are entitled to have the Warranty Deed placed once more in the possession of the bank subject to the terms of the escrow agreement." (Citing *Allen*)

Lynch v. Santa Fe National Bank, 97 N.M. 554 (App.), 627 P.2d 1247 (1981)

Facts:

- Lynch was purchaser on a REC, and also a seller on a junior REC, both of which were escrowed at Santa Fe National Bank (the "bank"). The owner of the senior contract declared a default, and obtained all the deeds from the bank.
- In subsequent litigation, trial court ordered specific performance of the senior contract, and was affirmed on appeal. Lynch then sued the bank for damages; the bank admitted it was negligent, but denied liability because of an exculpatory clause contained in the escrow agreements which purported to relieve it from liability except for willful or gross negligence. Trial court ruled for the bank.

Issues:

1. Whether an exculpatory clause should be given effect when a bank serves as escrow agent, on the ground that the bank enjoys superior bargaining power;
2. Whether the public interest requires that such a clause not be enforced.

Holding: Affirmed.

1. The Court states the general rule from *Tyler v. McDowell, Inc.*, 274 F.2d 890 (10th Cir. 1960): *“Exculpatory clauses in contracts of this kind are not favorites of the law. They are strictly construed against the promisee and will not be enforced if the promisee enjoys a bargaining power superior to the promisor, as where the promisor is required to deal with the promisee on his own terms....Nor will a contract be enforced if it has the effect of exempting a party from negligence in the performance of a public duty, or where a public interest is involved.”*

However, “required to deal” does not mean that the plaintiff was required to deal with the bank on the bank’s terms if he was to obtain the bank’s services. It does not mean “take it or leave it”. Rather, it involves the absence of alternatives; specifically, whether plaintiff was free to use or not to use the bank’s services. There being no showing of an absence of alternatives, the trial court is affirmed on this issue.

2. There was no claim that the exculpatory clause violated statutory law, or a public policy, or a duty to provide an escrow service under statutes or regulations. The service being performed could not be characterized as a public service merely because the defendant was a bank, because the escrow service was not a banking function. The Court concludes that the escrow business was not a public service because there was no regulation of the escrow business in New Mexico, therefore, the escrow business was not of a type generally thought suitable for public regulation.

Comment:

The New Mexico Escrow Company Act, providing for the regulation of independent escrow companies, was enacted in 1982, the year after this decision. However, banks were exempted from the Act. Query as to whether this Act, had it existed at the time, would have changed the decision of the Court.

Davisson v. Citizens’ National Bank of Roswell, 15 N.M. 680, 113 P.598 (1911)

Facts:

Money and a deed were placed in escrow “...until September 10th, when final settlement is to be made..... There was no instruction to the escrow agent regarding delivery or redelivery of escrowed money and papers. Bank returned money to the buyer upon demand.

Holding:

“...Nowhere in the memorandum was the bank authorized to make delivery of any paper, money or anything ... it should have held the escrow and let the parties either come to some agreement among themselves or appeal to the Courts..... However, it took sides in the matter and will be held ... to have acted at its peril.....”

DEFAULT and REMEDIES

Roberson Construction Company v. Montoya, 81 N.M. 566, 469 P.2d 715 (1970)

Facts:

- Montoya contracted to purchase a house to be constructed by Roberson, subject to VA approval of financing. Upon written notice of approval by VA, the contract obligated purchaser to execute papers and pay amounts due. Contract contained this clause: "Failure on the part of the Buyer to do so within 72 hours after receipt of such notice shall entitle the Seller to cancel this Contract and to retain all sums theretofore paid hereunder as liquidated damages."
- Upon receipt of written VA approval, Montoya refused to consummate the deal. Roberson sold the house to another party, and then sued Montoya for damages for the costs incurred in making the sale.
- Trial court ruled for Roberson, and awarded damages. Appealed.

Issue:

Whether Roberson was limited by the liquidated damages clause to a recovery of sums paid (\$50 down payment).

Holding:

1. Because Roberson did not declare a forfeiture or a cancellation of the contract, it could sue to recover damages for the breach.
2. The Court distinguishes *Hopper v. Reynolds*, 81 N.M. 255, 466 P.2d 101 (1970). In that case, the contract default clause allowed the seller to either sue for specific performance or terminate the contract and retain all previous payments as rent. When the contract limits the seller to one of two remedies, they are exclusive of other remedies. This case, however, "...does not involve the limitation of enumerated alternatives. Roberson had a choice of exercising one remedy...but chose not to exercise it. Therefore, he was left with his other normal contract remedies.". Affirmed.

Aboud v. Adams et al., 84 N.M. 683, 507 P.2d 430 (1973)

Facts:

- Adams signed a contract to purchase a furnished motel from Aboud. Adams took possession & operated the motel for eight days, after which he repudiated the contract and returned possession of the motel to Aboud.
- Aboud operated the motel for the next 17 months, after which he resold it. The original purchase price was \$214,000; the resale price was \$200,000.
- Aboud file a breach of contract action against Adams, seeking monetary damages. Trial court awarded Aboud \$14,000 damages, plus attorney fees.

Issues:

1. Issues on appeal involving whether the sales contract was conditional, and whether purchaser was entitled to rescind because of vendor's alleged misrepresentations, were disposed of under the "substantial evidence" rule, and are not discussed here.
2. Whether the trial court properly measured vendor's damages by awarding the difference between contract price and a subsequent resale price;
3. Whether the trial court erred in allowing attorney fees as an element of damages.

Holding:

1. Issues involving whether sales contract was conditional and whether vendor's misrepresentations justified purchaser's repudiation were decided in vendor's favor, as substantial evidence supported the trial court's conclusions.
2. The Court adopts the "loss of bargain" rule, citing *Corbin on Contracts* and *McCormick on Damages*: "In case of breach by the purchaser, the vendor's damages are the full contract price minus the market value of the land *at date of breach* and also minus any payment received.". While a subsequent sale is evidence of market value at the time of breach, it is not conclusive and the court must properly establish the market value at such time. Because the trial court did not make a finding as to the market value at time of breach, the case is remanded for a hearing on that issue.
3. Award of attorney fees is reversed. In the absence of a statute allowing attorney fees as damages, or an agreement between the parties providing for attorney fees, attorney fees cannot be considered as an element of damages, except in a few well-defined exceptions previously recognized by the Court (the exceptions are enumerated by the Court).

Comment:

The Court treated the measure of damages issue as a case of first impression in New Mexico. The Court had previously followed the "benefit of the bargain" rule in a case where the vendor was in breach (*Conley v. Davidson*, 35 N.M. 173, 291 P. 489 (1930)), but had never considered the situation where the purchaser was in default. Following *Corbin* and *McCormick*, the Court concludes that the same measure of damages should apply in either case: the difference between contract price and market value at the date of the breach.

DeVilliers v. Balcomb , 79 N.M. 572, 446 P.2d 220 (1968)

Facts:

- REC required annual payments of "\$5,000 or more each" and accumulated interest.
- Buyer paid more than \$5,000 in 1965.
- Annual payment for 1966 and taxes became delinquent, seller made written demand & terminated REC.

Issue: Is buyer permitted to credit overpayments made in one year to a delinquency occurring in subsequent years?

Holding: "We do not agree. An overpayment in one period by one who has purchased real estate under a contract obligating him to pay a specified sum or more each period does not relieve him of the duty of paying the specified amount on each and every payment date thereafter."

Comment: This case predates the RANM form REC, which contains the provision that "all payments shall be assumed to be regular payments, and not prepayments, unless otherwise specified by Purchaser in writing at the time of delivering such payments to Escrow Agent.". Thus, the decision would arguably be different under the RANM form IF the excess portion of the payment were equal to or greater than the amount of the regular payment amount.

Ott v. Keller, 90 N.M. 1, 558 P.2d 613 (1976)

Facts:

- Seller and buyer entered into a REC for the purchase of a residence. Buyer assumed a first mortgage, with payments of \$242.00 per month, and agreed to pay seller's "equity" at the rate of \$118.00 per month. Paragraph 8 of the REC (Form 103) allowed only 15 days for payment after written demand.
- Buyer did not make the February 1 payment of \$242.00 on the mortgage; on February 4, seller mailed a written demand to buyer to pay the \$242.00; the buyer did not make the payment on or before February 19; on February 20 seller elected to terminate the contract and retain all sums theretofore paid as rental (\$9,968.25).
- The demand letter was not actually received by the buyer. It was returned to sender by the post office, unopened. Paragraph 8 of the REC contained the usual language: 'after written demand for such payment ... has been mailed to the Purchaser'. The language used in the demand letter, however, was "if (15) days from the effective date of this notice,".
- The seller filed an unlawful detainer suit to evict the buyer from the property; the trial court ruled in favor of seller and evicted the buyer.

Issues:

1. Was the form of the lawsuit proper for maintaining an eviction of the buyer?
2. Was the notice of default sufficient to sustain the forfeiture?

Holding:

Reversed.

1. The statutory unlawful detainer suit is not the proper method for evicting a defaulting buyer under a REC.
2. Because the letter did not follow the language of the contract, the notice did not become operative when mailed, but only when (and if) it was received by the buyer. Since there was positive evidence of non-receipt, the notice never became operative.

Comment.

- The Court also noted that the forfeiture in this case was based upon failure to pay the assumed mortgage, not upon a failure to pay the owner's equity: "This litigation arose out of a claimed one-day default in payment of \$242.00 on an assumed mortgage, and not on Plaintiff's 'equity.' It is seriously questioned whether this default triggers a default of the real estate contract." This query can probably be disregarded, because the Supreme Court in 1967 held that a buyer was liable to the seller for a default on an assumed obligation, even after the seller's equity had been paid in full. See *Kuzemchak*, p. 11. Language was later incorporated in the RANM form, expressly declaring that a default on an assumed obligation is a default under the terms of the REC.
- Language employed in a demand letter should specify the letter's effective date-either date of mailing or date of receipt of the demand letter. Care must be taken to avoid ambiguity regarding the deadline for compliance.
- The Appeals Court went on to express its concern with the relative size of the buyer's equity which is forfeited:

"When a summary proceeding, which on its face deprives an equitable owner of title to the property, causes a forfeiture of 25% of the purchase price, and an eviction of the Defendants from the premises, and appears to be inequitable, the law and the facts should be viewed with care and caution through a spyglass. Forfeitures are not favored."

The Court was bothered by the fact that sellers allowed no additional time for payment after the 15-day demand period expired: "Furthermore, Plaintiffs violated the terms of their contract by terminating the escrow account upon a claimed one-day default. The time that elapsed was unreasonably short..."

Melfi v. Goodman, 73 N.M. 320, 388 P.2d 50 (1963)

Facts:

- Papers were placed in escrow with this instruction: "Should the purchaser make default in any of these payments and remain in default for at least 30 days the escrow agent is instructed to deliver all papers to the seller."
- Default occurred; several months later seller withdrew papers from escrow without notifying the buyer.

Issue:

Whether seller had a right to forfeit the buyer's interest, without first giving a notice of default.

Holding:

Forfeiture is upheld. Lack of express forfeiture clause does not help buyer. Written instructions to the escrow agent to redeliver papers is sufficient. The escrow agreement required no notice, and the Court will not rewrite the agreement for the parties.

Eiferle v. Toppino, 90 N.M. 469, 565 P.2d 340 (1977)

Facts:

- Eiferle purchased property on an REC (Form 103): purchase price \$23,500.00, \$3,000.00 down, \$17,259.93 by assumption of a mortgage and \$3,240.07 Seller's equity payable in monthly payments. Eiferle made the monthly mortgage payments outside of escrow.
- On March 1, Eiferle sent a monthly check to the mortgagee. The check bounced.
- On March 20, mortgagee returned the check to Eiferle, allowing until March 31 to cure the delinquency.
- On March 25, Eiferle sent a cashier's check in the proper amount to mortgagee.
- On March 28, Toppino's attorney sent a demand letter to Eiferle, demanding that the mortgage payment be made and that his \$25.00 attorney fee be paid. The escrow agent refused to accept Eiferle's April and subsequent equity payments unless the \$25.00 attorney fee was also paid.
- On June 1, Toppino terminated the REC and withdrew the papers from escrow. Eiferle sued; the trial court upheld the forfeiture.

Issue: Whether the facts support seller's declaration of termination of the REC.

Holding:

1. Reversed. Because the mortgagee's letter to Eiferle (a copy was sent to Toppino) allowed until March 31 to cure the delinquency, Toppino's demand letter of March 28 "was premature and of no effect."
2. "The rule is well settled in New Mexico that the type of real estate contract involved here is an enforceable one and upon default by a purchaser, the vendors are entitled to terminate the contract, regain possession of the property and retain the payments made as rental." (Citing *Davies* and *Bishop*) The Court recognizes that there is an exception to the rule: "...absent unfairness which shocks the conscience of the Court, the Appellees are entitled to enforce the contract as written." Under the specific facts of this case, the Court concluded that a forfeiture here would result in an "unfairness which shocks the conscience of the Court."

Comment:

- This decision reinforced the rule that the seller's forfeiture remedy in REC's is enforceable in New Mexico. The exception is recognized that forfeitures will be overturned when the result is "unfairness which shocks the conscience of the Court."
- The Court's decision was based on the "unfairness" exception to the general rule, because the mortgagee had given the buyer additional time to make the dishonored mortgage payment. It would seem that the Court could more appropriately have held that because the buyer was not regarded as being in default by the mortgagee, the buyer therefore could not be held to be in default under the terms of the REC.

Graham v. Albuquerque National Bank et al, 87 N.M. 174, 531 P. 2d 222 (1974)

Facts:

- In December, 1964 Graham purchased a house & lot on a form REC from the owners, who were C.R. Pitchford, Jean Pitchford, Brad Huckabee and Jerre Huckabee. Thereafter, the Huckabees assigned their interests by quitclaim deed to the Pitchfords, who then later assigned their interests to Bennye Brown in March of 1967. At that point in time, Brown was the sole owner of the vendor's interest.
- The Pitchfords divorced, and C.R. Pitchford then married Bennye Brown.
- In 1972, C.R. Pitchford mailed a notice of default to Graham.
- Graham sued all five vendors and the escrow agent, seeking damages for alleged unlawful action in default. Trial Court dismissed the complaint against as against the escrow agent and the Huckabees, and granted summary judgment to the Pitchfords and Brown. Graham appealed.

Issue: Whether notice of default mailed by Pitchford constituted effective notice under the terms of the REC.

Holding: Reversed. When the Pitchfords quitclaimed to Brown, they extinguished any rights they could previously have exercised as the “owner”, because “An assignment extinguishes the assignor’s rights”. Even though the Grahams received a letter of default and did not comply with its terms, there was a material issue of fact as to whether C.R. Pitchford was entitled to send the demand letter.

Ortiz v. Lane, 92 N.M. 513, 590 P.2d 1168 (1979)

Facts:

- Baca sold real estate to Brooks on a REC, subject to a mortgage which Brooks assumed and agreed to pay through the escrow agent.
- Baca conveyed to Lane by warranty deed and assignment, all his interest in the property. Lane was purchasing Baca’s interest as an investment.
- Brooks deeded the property to Ortiz, subject to the Baca-Brooks REC. The parties agreed that this conveyance was an assignment to Ortiz of Brooks’ equitable and beneficial estate in the property.
- Lane mailed a notice of default to Brooks for failure to make payments. Notice was not sent to Ortiz, although Lane had knowledge that Ortiz had purchased the property.
- Lane executed an affidavit of default, obtained the special warranty deed from the escrow agent, and recorded both instruments.
- Ortiz sued Lane for a return of the property. Trial court ruled that Lane was equitably estopped from asserting title, and that the recorded special warranty deed clouded Ortiz’ title, and ordered Lane to execute a quitclaim deed conveying the property to Ortiz. Lane appealed.

Issue: Lane contended on appeal that Brooks could not sell the property to Ortiz because Brooks did not own the property. The Opinion does not specify any other bases for the appeal.

Holding:

Reversed.

1. Citing the *Trickey* case, the Court applied the doctrine of equitable conversion and concluded that Brooks, as beneficial owner of the property, had the right to sell it.
2. Ortiz was entitled to notice of default before Lane could terminate his interest in the property. “It was wrongful for Lane to obtain possession of and file the Brooks-Baca Special Warranty Deed” because “Lane’s notice of default was sent to the wrong person...Ortiz is entitled to possession of the property under the Baca-Brooks real estate contract”.
3. The Court ordered that the Brooks-to-Baca special warranty deed be placed in the possession of the escrow agent, and that “Lane shall prepare for filing proper instruments that will declare that the Special Warranty Deed was inadvertently filed and that he does not hold the complete title to the property”.

Comment:

The Supreme Court reaches the same conclusion as the trial court, but under a different theory: where the forfeiture was based upon lack of notice to the sub-purchaser, the special warranty deed was mistakenly filed and conveyed nothing. The REC is therefore not terminated, and the recorded deed can be placed back in escrow, with a document (presumably an affidavit) being recorded to give notice that the deed had been “inadvertently” recorded.

Campbell v. Kerr v. Stepnowski, 95 N.M. 73, 618 P.2d 1237 (1980)

Facts:

(A) sold to (B) on a real estate contract.

(B) re-sold to (C) on a new real estate contract, wherein (C) assumed (B)'s obligation in the first contract.

(C) re-sold to (D) on a third contract, wherein (D) assumed the first two contracts.

(D) defaulted in making the payments.

(A) sent a written demand letter to (B) on 9/12/77 at the address specified in Paragraph 8 of the Form 103 REC. The letter was never actually received by (B), because (B) had moved to a new address. However, (B) had not given a change of address notice to (A) or to the escrow agent.

(B) made written demand upon (D) on 9/24/77, sending a copy to (C). After it became apparent that (D) did not receive (B)'s letter, (B) made another written demand on (D) alone on 10/12/77.

On 10/14/77, (A) picked up the escrow papers from the escrow agent of the (A)-(B) contract.

(C) filed suit to reinstate the contract between (A) and (B). A counterclaim was filed by (A) to quiet title against all the other parties. While these suits were pending, (B) paid off (A), and took over (A)'s position in the lawsuits.

Issues:

1. Whether a seller on a REC, who has actual knowledge of a junior REC, and who gives notice of default to the buyer, but does not give notice of default to the junior buyer, can forfeit the interest of the junior buyer.
2. Whether a REC buyer, whose equitable interest in the property has been terminated upon default, can subsequently enforce the payment terms of a junior REC on the same property.

Holding:

1. "We know of no affirmative duty placed upon a vendor in this situation to attempt to find the vendee, or to contact sub-purchasers.... If (B) wished to insure notice, he should have notified his vendor or the escrow agent....(A) had no legal duty to notify (C) of his demand upon (B)."
2. "The rule in New Mexico is that failure of a vendor to have the clear title he agrees to convey does not justify rescission or repudiation by a vendee if vendor can perform by delivery of the agreed title at the time required by the contract for such performance." In other words, (B) was not required to deliver title to (C) until (C) had made all payments due under the contract. (C) could have tendered all sums due under the contract to (B) at any time, thereby placing (B) in default, but did not do so.

Comment:

The holding that a seller has no duty to give notice of default to sub-purchasers, was later overturned by the *Martinez v. Logsdon* case in 1986 and the *Yu* case in 1992. See the discussion of those cases, below.

The sub-purchaser faces a problem in protecting his position vis-a-vis the junior REC upon a default and termination of the senior contract. The Court rules that he cannot simply rescind the junior contract unilaterally and "walk away from it." Instead, he must tender a pay-off on the junior contract, thereby maturing his seller's obligation to deliver title. When his seller fails to deliver, thereby breaching the contract, sub-purchaser could then presumably rescind the contract and retract the tender offer, or enforce the contract and sue his seller for the entire market value of the forfeited property, less the unpaid balance of the contract. Of course, it is critical that the procedure of tendering payoff be performed carefully:

- Tender should be made to the escrow agent. Escrow agent should be instructed to release the payoff funds to the seller only after the seller presents proof of his clear title.
- A reasonable time limit should be prescribed for seller to produce evidence of title.
- The escrow agent should be instructed that, upon the seller's failure to produce evidence of title within the prescribed time limit, the tendered payoff funds should be returned to sub-purchaser, along with escrow agent's affidavit establishing seller's nonperformance.
- Notice of the actions taken should be given to the seller.

Martinez v. Logsdon, 104 N.M. 479, 723 P.2d 248 (1986)

Facts:

- Logsdon sold to Mobley on standard REC for \$7,000.
- Mobley sold to Owen on REC, assuming the *Logsdon* REC.
- Owen sold to Martinez on REC for \$9,000.
- Martinez lived on the land 5 years, made improvements, and paid off the balance owed to Owen.
- Logsdon sent demand for late payments to Mobley, but to no one else. Balance owed to Logsdon was \$1,279.23. Escrow agent sent a copy of the demand letter to Owen, but not to Martinez. Logsdon was aware, or had constructive notice that Martinez had some interest in the land.
- After forfeiture of the *Logsdon/Mobley* REC, Martinez tendered payoff to Logsdon.
- Martinez sued to set aside the forfeiture by Logsdon; the trial court granted summary judgment to Martinez.

Issue: Whether a seller under a REC can terminate the interest of a sub-purchaser in possession, without first giving the sub-purchaser written notice of default.

Holding: Affirmed. The Court ruled on the basis that a forfeiture under the facts of this case would be 'shocking to the conscience of the Court', where the sub-purchaser:

- lived and worked on the property for five years;
- made significant improvements to the property;
- paid off the balance owing on the junior REC & received a deed;
- tendered payment in full of a relatively small unpaid balance on the senior REC;
- was unaware of the notice of default issued on the senior REC.

Comment: The Court said it distinguished the *Campbell* decision, based on two factual differences:

- the sub-purchaser in *Campbell* had notice of the vendor's written demand to another sub-purchaser, and thus had an opportunity to cure the default;
- the sub-purchaser in *Campbell* was in default on his REC, whereas Martinez had paid off his seller in full. This argument seems faulty, because Martinez had assumed the *Logsdon/Mobley* REC, but had not made the payments on it. The *Kuzemchak* decision in 1967 had already established that failure to pay an assumed obligation is a default of the REC.

See the 1992 *Yu* decision below, where the Court observed that the *Martinez/Logsdon* decision had modified *Campbell*. In this writer's opinion, the Court simply overruled *Campbell*. In either event, the *Yu* decision effectively overruled *Campbell*, by holding directly that the seller must give notice of default to sub-purchasers.

Yu v. Paperchase Partnership, 114 N.M. 635, 845 P.2d 158 (1992)

Facts:

- See *Paperchase v. Bruckner* for prior history.
- A & O sold on a third REC to Yu in 1980; Yu sold to Strahl in 1984. Each sub-purchaser except Strahl assumed the prior contracts and encumbrances.
- Paperchase sent a demand letter for reimbursement of taxes paid, to the Bruckners. No notice was sent to Yu. Paperchase elected to terminate, and picked up the deeds from the escrow agent. After releasing the deeds, the escrow agent notified Yu and Strahl in writing that forfeiture had occurred.
- Yu sued to vacate the forfeiture; the trial court grant summary judgment to Yu. Paperchase appealed.

Issue:

Whether a seller can terminate a REC and forfeit the interest of a sub-purchaser when there was a default in the buyer's obligation to pay property taxes and the seller did not notify the sub-purchaser of the default or give it an opportunity to cure.

Holding:

Affirmed. "A vendor with knowledge of a subvendee's interest in property subject to a real estate contract, where the subvendee has a significant equity in the property subject to the contract, cannot declare a forfeiture of the subvendee's interest without giving the subvendee notice of default and an opportunity to cure." The Court stated as its reason for this holding "the modern view that valuable contractual rights should not be surrendered or forfeitures suffered by a slight delay in performance unless such intention clearly appears from the contract or where specific enforcement upon the seller will work injustice after a delayed tender." (quoting from *Martinez v. Martinez*)

Comment:

The Court stated that "...Campbell has been modified by the subsequent case of *Martinez v. Logsdon*." (Emphasis added) However, the *Martinez* Court said it was distinguishing the *Campbell* decision. It probably doesn't matter, since the *Yu* decision clearly overrules *Campbell* on the issue of requirement for notice to a sub-purchaser.

The Court cites with favor the rule from Idaho and Washington that a mortgagee of a contract purchaser's equitable interest in the land subject to the contract is entitled to notice of a default and an opportunity to cure before the mortgagee will lose its interest. The Idaho case relied in part on *Shindledecker* (p. 6, *CLA*). The Court also cites Powell on Real Property, section 938.26[2]: "Nearly all courts now hold that notice is required when the vendor has actual or constructive notice of the vendee's mortgage."

English v. Sanchez, 110 N.M. 343, 796 P.2d 236 (1990)

Facts:

- On February 22, 1982, Donald English entered into a REC to sell 50 acres of land to Mr. & Mrs. Sanchez. No deeds were escrowed, and Donald's spouse, Emma English, did not join in the REC. Legal title was in name of Dixon Enterprises, Inc.
- On February 25, Dixon Enterprises deeded title to San Juan Enterprises, Inc., a corporation owned by Donald & Emma English. The deed was not recorded until August 1985.
- In February, 1988 the Sanchezes became delinquent on their monthly payments.
- On March 2, 1988 Donald English unilaterally executed an addendum agreement to the REC changing the name of the seller from Donald English to San Juan Enterprises, Inc.
- On March 10, San Juan deeded title to Donald English, recorded March 18.
- On the "next day", Donald's attorney mailed a default notice to the buyers.
- Donald filed suit (presumably after expiration of the notice period) to collect the entire unpaid principal balance. Buyers asserted as a defense the failure of Emma to join in the contract of sale, counterclaimed to rescind the contract, and filed a motion for summary judgment.
- Prior to a hearing on the motion for S.J., and three months after the suit was filed, Donald & Emma executed a separate property agreement, designating the property as Donald's separate property.
- Trial Court granted S.J. to Sanchez, holding that the property to be acquired & sold under the REC was community property, and the REC was void due to failure of Emma to join in the REC.

Issues:

1. Is a REC valid when the vendor holds no title at time of execution of the REC?
2. Was the property a community asset at the time of its acquisition by English?
3. Was the REC absolutely void for failure of the spouse to join?

Holding:

1. A person may enter into a valid contract to sell real estate to which he has no title, provided he is able to carry through with the transaction after the final payment is made or tendered. (Citing *Clark v. Ingle*, 58 N.M. 136, 266 P.2d 672 (1954).
2. Under sect. 40-3-8 NMSA 1978, all property acquired by either spouse during marriage that is not the separate property of one spouse, is community property. At the time English took title, there was no separate property agreement, and since the property was not acquired with separate funds or through gift, bequest, devise or descent, it was acquired as an asset of the marital community.
3. "We agree that the contract was void as to after-acquired community property, but hold it was valid as to the after-acquired real estate when it was transmuted and owned by the seller as his separate estate....The fact that the property was held for an interim as an asset of the community may have rendered the contract void for purposes of selling community property, but the interim holding of the property by the community need not void the contract for the purpose of selling separate property that is acquired through transmutation." Because the transmutation of the property from community property status to separate property status occurred before the hearing on the motion for S.J., the affidavits and written agreement raised a material issue of fact as to whether English had cured any deficiency in the original complaint and was entitled to a trial on the merits!

Comment: Because the appeal was from a ruling on motion for summary judgment on an issue involving contract formation, the issue had not yet arisen in the proceedings as to whether English was entitled to mail the default notice, in light of the transactions on March 2 & March 10. With regard to the joinder statute, the Court engaged in a lengthy review of the history of the statute, the New Mexico Equal Rights Amendment in 1972, the Community Property Act of 1973, and the subsequent case decisions. The Court then, in an acknowledged apparent contradiction of its previous history sustaining the "void and of no effect" doctrine, expressed its reluctance "...to expand the application of a nullity or wholly-void doctrine beyond its present limits, in this case to a contract for sale of land that was fully enforceable and valid at the time of its execution".

Albuquerque National Bank v. Albuquerque Ranch Estates, Inc., 99 N. M. 95, 654 P.2d 548 (1982)

Facts:

- Albuquerque Ranch Estates ('ARE') sold to Tract C (a partnership) on a REC.
- Tract C assigned all its rights in the REC to KAC with ARE's written consent.
- KAC defaulted on a payment; ARE sent a 30-day demand letter to KAC
- ARE did not send a default notice to Tract C, but Tract C had actual knowledge of KAC's default and that ARE had sent a notice of default to KAC.
- KAC failed to comply and ARE terminated the REC. Trial Court upheld the forfeiture.

Issues:

1. Was the default notice invalid because it failed to state the amount demanded, or the deadline for compliance?
2. Was the default notice invalid because it was mailed by certified mail, where the REC was silent as to method of mailing, even though the notice was actually received by KAC?
3. Was the default notice invalid because the seller failed to send a copy to the escrow agent and did not record a copy in the county clerk's office?
4. Was the termination of Tract C's interest invalid because of lack of a notice of default to Tract C?

Holding:

1. "A notice of default must be clear and sufficiently articulated so as to place the recipient on notice of an unmistakable intent to claim a forfeiture The provisions of the contract govern the requirements for notice of default and (Seller) had no duty to reiterate the amounts required to be paid under the contract."
2. In the absence of an express contractual provision as to the type of mailing required between parties, proof of actual delivery and receipt of the notice is sufficient.
3. While it is common practice to send a copy of notices of default to the escrow agent or to record a copy with the county clerk where the property is located, failure to do so under the facts herein did not invalidate the notice of default. The provisions of the contract did not impose such requirements.
4. Tract C's assignment to KAC of all of its right, title and interest under its contract with ARE relieved ARE of any obligation to send notices of default to Tract C.

Graham v. Stoneham, 73 N.M. 382, 388 P. 2d 389 (1963)

Facts:

- Graham sold land & an auto-wrecking business to Stoneham on a REC with installment payments.
- Buyer defaulted, seller demanded redelivery of possession of the property, and buyer complied.
- Seller then sued for damages because of loss of value of the inventory. Trial court awarded damages to seller.

Issue:

Whether the sellers, by repossessing the property, thereby rescinded the contract and waived any action on the contract.

Holding:

Reversed.

"At common law, under a conditional sales contract, the repossession of the property by the seller, upon default of the buyer, constitutes an election of remedies and amounts to a rescission of the contract, precluding further recovery from the buyer."

“We have held that, when provided for in a contract, (emphasis added) a vendor may have *alternative remedies* of (1) repossession of the property and retention of previous payments as liquidated damages; or (2) declaration of the balance of the purchase price as due, and suit therefor; or (3) repossession of the property with or without process of law and, after notice, foreclosure as required by law, with a right to recover any deficiency not realized in the sale. However, we recognized that only the first two are conventional remedies of a holder of a conditional sales contract, (emphasis added) (several citations)

“It is unquestioned that parties to a contract may provide that repossession and suit on the purchase price are cumulative remedies. (citations) However, the parties did not expressly agree on cumulative remedies. Under the contract entered into between the parties and the circumstances of this case, the vendors, having selected the remedy of repossession, are precluded from an action for the unpaid purchase price.”

Comment:

Although the Court described the action as being for the unpaid purchase price, the suit was actually for damages for loss of value of the inventory. The ruling should be seen as precluding any suit based on the contract, or arising from performance of the contract, when the seller has rescinded the contract and retaken possession of the property.

When the third optional remedy of repossession followed by foreclosure is available in the contract and is exercised, the instrument will be construed as an equitable mortgage, requiring that the buyer have a right of redemption. See *Bishop*, below and cases discussed therein.

Davies v. Boyd, 73 N.M. 85, 385 P. 2d 950 (1963)

Facts:

- Davies sold to Boyd on a REC. Part of the down payment was represented by a separate note due in two years, secured by a mortgage on another property owned by Boyd.
- Boyd defaulted after five months of payments, Davies gave notice of default, Boyd failed to cure, and Davies elected to terminate the REC.
- Davies then sued on the separate note to collect the balance of the down payment. Trial Court ruled for Davies.

Issue: Whether the note & mortgage were given ‘in lieu’ of a down payment, stood in the same position as any other payment made on the REC, and therefore were forfeited to seller upon cancellation of the REC.

Holding:

Reversed.

1. The forfeiture remedy is valid and is upheld.
2. A vendor may not maintain an action to recover any part of an unpaid purchase money where he has rescinded or forfeited a contract. "Where a contract for sale of real estate is accompanied by the Purchaser's note or other separate obligation for a part of the purchase price, termination or cancellation of the contract or claim of forfeiture under its terms, because of default by the purchaser, is generally held to destroy the consideration for the separate obligation of the purchaser and it is no longer enforceable against him."

Comment: The Court noted that the REC did not provide that the note & mortgage were accepted as part payment. Therefore, the note represented “a separate obligation of purchasers to pay one of the installments of the unpaid purchase price”. It would appear that this ruling would stand in the way of any attempt to take a promissory note for any portion of the purchase price as stated in the REC.

Bishop v. Beecher, 67 N. M. 339, 355 P. 2d 277 (1960)

Facts:

- Beecher sold a house to Bishop by REC.
- Bishop defaulted on payments; Beecher sent a 30-day demand letter as required by the REC, and Bishop failed to cure the default. Beecher terminated the REC & recorded the special warranty deed.
- Bishop thereafter offered to pay the entire balance with interest, costs and attorney fees; Beecher refused the offer.
- Bishop sued, asking the court to construe the REC as an equitable mortgage and allow a right of redemption. Trial Court upheld the forfeiture. Appealed.

Issues:

1. Whether or not a REC containing optional alternative remedies of rescission and acceleration constitutes an equitable mortgage, as a matter of law.
2. Whether the buyers were entitled to equitable relief, on the grounds that they had paid approximately one-third of the total purchase price.

Holding:

1. The REC is not an equitable mortgage as a matter of law, and the forfeiture remedy is proper.
"Admittedly, there may be some disadvantages to this type of contract, but it is felt that the advantages far outweigh them when the benefits, which are derived by thousands of people who have been enabled to purchase property by merely paying for it over the years in a manner likened to rent, are considered."
2. Purchasers are not entitled to equitable relief, even though they paid about 1/3 of the total of the contract and assumed mortgage, because they had use of the property for almost 6 years at a cost of less than \$60.00 per month.
"Under the circumstances, we will not rewrite the contract into which the parties freely entered. Appellants failed to comply with their agreement, and, absent unfairness which shocks the conscience of the Court, the Appellees are entitled to enforce the contract as written."

Hale v. Whitlock and Albuquerque National Bank, 92 N.M. 657,593 P.2d 754 (1979)

Facts:

- Over a period of eleven years, buyers had fallen behind twenty-five monthly installments on their REC.
- Seller, who had never exercised his right to demand payment of the past-due installments, then sold his interest in the contract to Whitlock, who proceeded to make written demand for past-due payments pursuant to the contract. Whitlock did not notify buyers that he would insist on strict performance before sending the demand letter.
- Buyers sued, asking the trial court to declare that they were not in default. Trial court ruled that buyers were in default, but granted them an additional fifteen days after entry of judgment to pay off the entire contract balance plus interest and attorney fees. Buyers tendered the required amount within the time allowed. Whitlock appealed.

Issues:

Whether the trial court erred in giving the buyers additional time to pay off the contract balance, or was acting within its equity jurisdiction.

Holding:

Affirmed.

"It is well settled in New Mexico that the type of real estate contract involved in this case is enforceable and upon default, the vendor may terminate the contract, regain possession of the property and retain the payments made (previous cases cited). However, it is also recognized in each of these cases that there are exceptions to this rule, and that under certain circumstances, the contract and acts of the parties should be construed if at all possible to avoid a forfeiture.

Under the facts in this case, the trial court properly exercised its equity jurisdiction in granting Appellees additional time within which to pay off the entire balance due under the real estate contract along with interest and attorney fees. The result was to place the parties in the positions they would have been in had the contract been fully performed."

Comment:

This decision suggests that it would be folly for a seller to attempt to enforce a forfeiture if the buyer tenders payment in full of the unpaid contract balance after a deadline for an installment payment set by a notice of default.

Huckins v. Ritter, 99 N.M. 560, 661 P.2d 52 (1983)**Facts:**

- Ritter sold a house to Huckins for \$155,000.00: \$45,000.00 down, \$40,725.73 by assuming an underlying mortgage and the balance of \$69,274.27 on an REC dated July 28, 1981, due as a single payment on October 15, 1981. Huckins defaulted, Ritter issued a demand letter.
- Huckins filed suit November 30, 1981 seeking an injunction to prevent the forfeiture. The parties agreed to an extension to January 10, 1982. Huckins defaulted again. Ritter obtained documents from escrow on February 25, 1982. Trial court upheld the forfeiture.

Issues:

1. Whether the trial court should have enjoined the seller from terminating the REC where the buyer made a large down payment and was in possession for a short period of time.
2. Whether the facts of the case entitle the buyer to equitable relief from a forfeiture.

Holding:

1. The termination provision of the REC is enforceable, and the Court upholds the forfeiture of the property.
2. Forfeiture of the \$45,000.00 down payment, when Huckins had possession of the property only from July 28, 1981 to February 25, 1982 would be so unfair as to shock the conscience of the Court. The rental value of the house was between \$600 and \$1500 per month. The Court orders a refund to Huckins of the \$45,000.00 down payment, less reasonable rental to be assessed during Huckins' occupancy of the house.

First National Bank in Alamogordo v. Cape v. Mullins, 100 N.M. 525, 673 P.2d 502 (1983)

Facts:

- Cape sold A-frame cabins to Donald McKeeman on a REC with monthly payments. The down payment and the first five monthly payments, totaling \$6,614.55, were paid by Dora Mullins, using her separate funds. Two months after execution of the REC, McKeeman and Mullins were married.
- Donald defaulted on the REC by failing to make the November 1977 payment. In March 1978 Dora was killed in an accident. In June 1978, Cape sent a 30-day default notice to Donald, who then signed an affidavit voluntarily giving up the cabins to Cape.
- Litigation determined that, as between Dora's estate and Donald, the estate should receive title to the cabins. The estate made several offers to bring the payments current; they were refused by Cape.
- FNB filed a Petition for Interpleader. The trial court refused to set aside the forfeiture, but ruled that Cape's title should be subject to a resulting trust in the amount of \$6,614.55 in favor of the estate. Appealed.

Issue: Whether the trial court erred in not ordering a reinstatement of the REC.

Holding: Affirmed. The Court reiterated the general rule and its exceptions, as previously stated in *Bishop, Eiferle, Hale*, and *Huckins*. It then concluded that the facts of this case do not support an exception to the general rule. However, because separate funds of Dora were used to make some of the payments and the down payment, it agreed with the trial court that substantial evidence supported the resulting trust in favor of Dora's estate.

Manzano Industries Inc. v. Mathis, 101 N.M. 105 (App.), 678 P.2d 1179 (1984)

Facts:

- Mathis sold to Manzano on a REC. Manzano was late with payments 23 times, and on 11 occasions written demand was issued, giving the 60-day notice required by the REC. Manzano failed to cure the default within 60 days after the demand for the July 1982 payment, and Mathis elected to terminate the REC.
- Manzano sued to set aside the forfeiture. Manzano alleged that the forfeiture provision in the REC is unconscionable and should not be enforced. Manzano also alleged unfairness due to forfeiture of a large down payment. The trial court ruled for Mathis.

Issues:

1. Whether the forfeiture clause in the REC is unconscionable and therefore should not be enforced;
2. Whether the fact that a large downpayment was made results in unfairness of a magnitude as to render the forfeiture provision of the REC unenforceable.

Holding:

Affirmed.

1. The termination provision is enforceable. "We have repeatedly held such contracts to be enforceable Strong public policy favors enforcement of such contracts."
2. The trial court was right to deny equitable relief to Manzano.
"Appellant seeks to analogize the facts in this case to those in *Huckins v. Ritter* The only similarity in facts between the two cases is that in both cases a substantial down payment was made. We refuse to hold that the forfeiture of a large down payment will, in every case, shock the conscience of the court. The size of the forfeited down payment is only one of the factors the trial court should consider. To hold otherwise would subvert the policy behind recognizing the enforceability of such contracts."

Jacobs v. Phillippi, 102 N.M. 449, 697 P.2d 132 (1985)

Facts:

- Jacobs made an offer to buy a house through Phillippi's real estate agent (Wolfley). The offer included a down payment, assumption of an existing mortgage, and the balance on a real estate contract, bearing 10% interest, with a balloon payment due within one year.
- Phillippi counter-offered, through Wolfley, increasing the REC interest rate to 12%.
- Jacobs instructed Wolfley to counter-offer, setting the interest rate at 10% for the first six months, and at 12% for the second six months. Wolfley did not communicate this counter-offer to Phillippi.
- A contract was prepared and signed, with terms incorporating the Phillippi counter-offer, but not the Jacobs counter-offer.
- Jacobs defaulted on the balloon payment, and Phillippi declared a forfeiture; later re-selling the house for \$4,000 less than the original sales price. In the meantime, Phillippi paid \$24,000 in post-default mortgage, utility, interest and repair payments, and lost \$3,600 in rent which Jacobs had agreed to but did not pay.
- Jacobs filed suit, seeking rescission of the REC, return of the down payment, and damages for misrepresentation by the real estate agent. Trial court dismissed the complaint. Appealed.

Issues:

1. Whether Jacobs was damaged by Wolfley's breach of fiduciary duty;
2. Whether the forfeiture was unwarranted;
3. Whether the REC was void for lack of mutual assent.

Holding:

1. Jacobs was not damaged by the misrepresentation, because the difference in the interest rates was not a material factor in the negotiations (confirmed by Jacobs' trial testimony) and in the execution of the contract.
2. Equitable considerations "do not exist in this case which would require application of an exception to enforcement of the real estate contract". The Court dismissed Jacobs' argument that the *Huckins* rule should apply, instead offering its observation that the equities of the case seem to be much in favor of Phillippi, rather than Jacobs.
3. Because only Jacobs believed that the interest rate should have been 10% for the first six months, this was a unilateral mistake. "This Court will not void a contract for a unilateral mistake except where the mistake is basic and material to the agreement, and the other party knew or reasonably should have known of the mistake."

Comment: The Court could have ruled that since Wolfley was Phillippi's agent, Wolfley's knowledge of Jacobs' unilaterally mistaken assumption would be imputed to Phillippi. However, in ruling on the damages issue, the Court had already concluded that the difference in interest rates was not a material factor in the negotiations or in the execution of the contract. The decision as to the mistake issue therefore seems to be based on the non-materiality of the interest rate difference.

Russell v. Richards, 103 N.M. 48, 702 P.2d 993 (1985)

Facts:

- Richards sold on REC to buyer, who assigned buyer's interest to Russell, who paid \$11,188 down, and assumed \$37,938 balance owed to Richards.
- Russell made 72 payments, reduced principal balance by \$10,782, leaving balance of \$26,504.
- Richards declared forfeiture for non-payment; Russell sued for damages.
- Property value had increased from \$48,989 to \$82,735 from time of purchase to time of default.
- The trial court awarded damages to Russell; it set aside the forfeiture as "shocking the conscience of the Court", the damage award included lost equity based on value increase; damages also included value of lost personal property not covered by the REC.

Issues:

1. Whether the trial court's refusal to enforce the forfeiture was an abuse of discretion;
2. Whether the trial court erred in awarding damages.

Holding:

1. The Court reversed the trial court's failure to uphold the forfeiture. The parties to a REC and their assignees agree to be bound by its terms and provisions, and to accept the burdens of the contract together with its benefits. A sub-purchaser takes the land subject to the terms of the contract of which he has knowledge. The courts will enforce a REC except where enforcement, under the equitable circumstances of the case would result in an unconscionable forfeiture. Such equitable circumstances as would avoid forfeiture are not present here. "The usual consequence of default, as clearly stated in the contract assumed by Russell, is forfeiture of all interest, only unusual equitable circumstances create an exception to that rule. "
2. The Court reversed the award of damages based on the increased value of the property, and affirmed the award of damages for lost personal property. The fact that Russell was in possession 6 years and paid \$10,782 on the contract principal to the Richards was properly considered by the trial court. Trial court's consideration of the down payment was not proper, because it was paid to Russell's assignor, and not to the Richards. (**Comment:** The Court is here using principals of unjust enrichment law, and not considering just the loss to the buyer.)
Trial court's consideration of the increased market value of the property was error: " . . . during the life of the REC any risk of loss or enhancement of value accrues to the purchaser. ". (quoting *MGIC*)
Damage award for loss of personal property not covered by the REC is affirmed; purchaser's uncontradicted testimony as to the value is sufficient evidence to support the award.

Comment:

While the trial court's conscience may have been shocked, the Court had no such problem, and had little sympathy for Russell: she had defaulted several times before, but cured the default each time ("She knew the consequences of default "). Also, Russell "had received benefit and profit during her possession". The Court noted that she had rented out 3 units of the property; at the time of default, the entire property was leased for a monthly payment far in excess of the REC payment.

Another Comment:

There was no indication in the Opinion that Russell was not in default, or that any defect existed in the notice procedure followed by Richards. Apparently the trial court had awarded damages to the purchaser on the sole basis that the forfeiture was "shocking to the conscience of the court". There was no indication that the purchaser had sought reinstatement of the REC.

Campos v. Warner, 90 N.M. 63, 559 P.2d 1190 (1977)

Facts:

- Warner sold land to Rentex, Inc. on a standard form REC. Rentex leased the property to Campos, then defaulted on the REC. Warner declared a forfeiture, and refused to honor the lease agreement.
- Campos sued Warner for damages for wrongful cancellation of the lease. Trial court found that Warner had ratified the lease by accepting rent payments after the forfeiture, and awarded damages to Campos. Warner appealed.

Issues:

1. Whether a seller under a REC is bound by a lease entered into by the buyer while the REC is viable.
2. Whether seller's actions in this case constituted a ratification of the lease agreement.

Holding:

Reversed.

1. Noting that this was a case of first impression in New Mexico, the Court adopted the rule that a conditional contract purchaser can create no greater interest in a lessee than the purchaser held, and that the lessee takes the property subject to all claims of title enforceable against the purchaser. The Court cites *Warren and Mutual Building & Loan Ass'n of Las Cruces*.
2. The Court concluded that there was no substantial evidence in the record to support the trial court's findings and conclusions that Warner ratified the lease agreement. The Court declined to recite the evidence bearing on this issue, and made no mention of the rent Warner had allegedly received after forfeiting the REC.

Western Bank v. Matherly, 106 N.M. 31, 738 P.2d 903 (1987)**Facts:**

- Matherly sold land & equipment to Merkling-Bell on a REC. Deeds and a bill of sale to the equipment were escrowed. Matherly also obtained 2 security agreements on the equipment, and perfected them. The escrow agreement provided that Matherly would subordinate the security interest in the equipment to First National Bank (FNB), who loaned \$50,000 to Merkling-Bell.
- Merkling-Bell then obtained a \$70,000 loan from Western Bank. FNB was paid in full, and FNB released of record its security agreement. Western obtained a new security agreement from Merkling-Bell, and filed it.
- Merkling-Bell defaulted, Matherly declared a forfeiture & obtained the deeds and bill of sale from escrow. Matherly then sold the land & equipment to McAllister, & Western Bank filed a declaratory judgment action to determine the parties' rights to the equipment.

Issue:

Whether a security interest in personal property governed by the controlling secured transactions sections of the UCC may be conjunctively forfeited with an interest in real estate under a real estate contract in New Mexico.

Holding:

"...the instant case is controlled not by Matherly's security interest, but by the fact that, upon default and forfeiture by Merkling-Bell, Western Bank lost any security interest it had by and through Merkling-Bell."

"We hold that, where there are no intervening equities whereby the vendor may be estopped to enforce a forfeiture against one claiming through a conditional vendee of *personal property*, a vendee can create no greater interest in *personal property* than is possessed by the vendee, and one claiming a UCC security interest through the vendee takes his interest in the property subject to all claims of title enforceable against the vendee, including forfeiture upon default." (emphasis added)

Comment:

The Court, citing *Warren, Petrakis* and *Mutual Building & Loan*, now extends to personal property sold conjunctively with real estate on a real estate contract, the rule that a buyer of real estate sold on a real estate contract can create no greater interest in the real estate than the buyer possessed. It follows that the rule should apply to any personal property, like motor vehicles and mobile homes, regardless of the statute controlling the manner in which security interests in such personal property are created and perfected. If the lien, although perfected, is junior to the conditional sales contract seller's interest, it is subject to "...all claims of title enforceable against the vendee, including forfeiture upon default".

Petrakis v. Krasnow, 54 N.M. 39, 213 P. 2d 220 (1949)

Facts:

- Buyer under REC for town lots, while in possession, and with seller's knowledge, contracted with supplier to build a dance hall. Seller timely posted notices of non-responsibility on the premises.
- After completion of work, buyer orally contracted with same supplier to build a card room adjacent to the dance hall. The original notices had been torn down, and seller, who was aware of new work, but believed it was a continuation of the original job, did not post new notices. Less than two weeks of non-work intervened between the two jobs.
- Two suppliers recorded their claim of mechanics' liens.
- Buyer defaulted on monthly payments, seller mailed a demand letter on the payment due date, elected to terminate after more than 30 days passed without cure, and filed suit to quiet title. Suppliers cross-claimed for foreclosure of their mechanics' liens. Trial court ruled for suppliers.

Issues:

1. Did seller's knowledge of the second construction project require him to post new notices to satisfy the statute (sect. 48-2-11 NMSA 1978)?
2. If new notices were not required, was the first posting sufficient to satisfy the statute, when the notices were torn down before the second job commenced?
3. Did the premature mailing of the demand letter void the notice, so that the forfeiture was invalid?

Holding: Reversed.

1. Since there were no circumstances from which seller could have known that the second job was under a new contract, seller did not have the knowledge required to put him under a duty to post a new notice of non-responsibility for the second construction job.
2. The original posting of three notices (the statute requires only one) in appropriate locations satisfied the statutory requirements. "...all that is required is a good faith effort to comply with the statute. The owner is not called upon to employ a sentry to stand watch throughout a period deemed reasonable to make certain the notice remains posted all the while".
3. The demand letter, although mailed on the payment due date, is effective as a demand made upon the first day of default, and would "start the running of the 30-day period of default, within which payment could be made, with the very first day of default". The Court observed that payment on or before the due date "would nullify the notice".

Hill v. Long, 61 N.M. 299, 299 P.2d 472 (1956)

Facts:

- Buyer under verbal REC contracted with a carpenter to do alterations & additions to the property, with seller's approval. Seller never posted a notice of non-responsibility.
- Buyer failed to make a payment, seller ordered carpenter to stop work, then terminated the REC.
- Carpenter filed a mechanic's lien within 120 days after default in payment. Carpenter filed suit to foreclose lien. Trial court held for the carpenter.

Issues:

1. Does the statutory mechanics' lien attach to the equitable interest of the buyer under a REC?
2. Is the seller under the REC an 'owner or person having or claiming an interest therein', and thereby required to post a notice of non-responsibility to protect his interest against the mechanics' lien?

Holding:

1. The word 'owner' in the mechanics' lien statute may have reference to one whose interest is less than a fee-simple estate, such as a lessee or a conditional vendee in possession. "One who deals with such a party directly is contracting with the 'owner', and... is an 'original contractor'."
2. The owner of the legal title who knows that work is being done on the property must post a notice of non-responsibility on the property in order to protect his legal title against the mechanics' lien.

Cano v. Lovato v. Est of Robinson v. New Mexico Title Co., 105 N.M. 522 (App.), 734 P.2d 762 (1986)

Facts:

- Lovato entered into a REC with the Estate on September 30, 1980 to purchase residential property for \$28,000. On the same day, the N.M. Property Tax Division conducted a tax sale of the property, selling it to Cano for a bid of \$1,900. The title company had knowledge of the delinquent taxes, but did not attempt to pay them until after the tax sale occurred.
- Lovato took possession, made improvements on the property (fair market value, \$37,500; cost, \$23,322.56).
- Cano filed a complaint in forcible entry & detainer in Bernalillo County Metropolitan Court; Lovato was served with summons. By agreement of parties, this action was dismissed and refiled as a quiet title action in district court.
- The trial court:
 - Determined Cano's title to be superior, and awarded possession to Cano;
 - Awarded a lien to Lovato against the property, for the fair market value of the improvements made, subject to offset for rental value during Lovato's possession;
 - Gave Lovato the right to remove certain improvements at his expense;
 - Rescinded the real estate contract;
 - Ordered the Estate and the title company to reimburse Lovato for money paid under the contract;
 - Ordered the title company to indemnify the Estate for any sums due Lovato.

Issues:

1. Priority of tax deed vs. REC;
2. Propriety of subjecting the tax deed to the improvements lien;
3. Proper amount of the improvements lien.

Holding:

The case was remanded to the trial court for a fact-finding hearing as to an issue involving the good-faith purchaser, but the Court proceeded to dispose of the other issues, in anticipation of their re-appearance after the fact-finding hearing.

1. The lien was imposed under the "betterment" statutes, NMSA 1978, Sections 42-4-14 to -19. Section 42-4-17 provides:

"When any person or his assignors may have heretofore made, or may hereafter make any valuable improvements on any lands, and he or his assignors have been or may hereafter be deprived of the possession of said improvements in any manner whatever, he shall have the right, either in an action of ejectment which may have been brought against him for the possession, or by an appropriate action at any time thereafter within ten years, to have the value of his said improvements assessed in his favor, as of the date he was so deprived of the possession thereof, and said value so assessed shall be a lien upon the said land and improvements, and all other lands of the person who so deprived him of the possession thereof situate in the same county, until paid; but no improvements shall be assessed which may or shall have been made after the service of summons in an action of ejectment on him in favor of the person against whom he seeks to have said value assessed for said improvements."

The trial court did not err in imposing the lien. The tax deed, under the provisions of Section 7-38-70(B), conveys the former owner's interest "subject only to perfected interests in the real property existing before the date the property tax lien arose.". However, the Court finds no conflict with this language in subjecting the tax deed to the operation of the subsequent improvements lien, because "The statute does not, by its express terms, extinguish liens arising against the property *after* the issuance of the tax deed." (emphasis supplied). To rule otherwise would be unreasonable, because "...we would be allowing the Canos to be unjustly enriched for the improvements placed upon the land by Lovato.", and because an avenue of security would be foreclosed for those performing services upon the property.

2. Trial court is reversed for allowing lien in the amount of the fair market value of the improvements. The Court adopts the reasoning of a decision from the 10th Circuit Court (*Madrid v. Spears*, 250 F.2d 51, 54): The "test of recovery is not how much the owner is enriched by the improvements, but how much he is unjustly enriched. And, the owner is not unjustly enriched more than the improver's cost.". Since Lovato's costs were \$23,322.56, the lien award is reduced to that amount.

Armstrong v. Csurilla, 112 N.M. 579, 817 P.2d 1221 (1991)

Facts:

REC default; seller elected to declare balance due; sued for money judgment and a decree of foreclosure in the same action.

Issue:

Does the *Graham v. Stoneham* decision preclude the seller from suing for the unpaid purchase price, then repossessing the property? (Converse of holding in *Graham*, which held that a seller cannot repossess the property, then sue for the balance)

Holding:

Remedy of foreclosure on a money judgment is not contradictory to the election of remedies requirement. "The Armstrongs did not retake possession of the property; they sued to enforce payment of the debt and then, after securing a judgment for that debt, obtained an order that their judgment constituted a lien and that the lien was foreclosed. Consolidation in a single action of claims for a money judgment and for a foreclosure is upheld, where no 3rd party rights are involved.

Comment:

The Court also ruled on an issue regarding the validity of the judicial sale, and reviewed the history distinguishing execution sales from foreclosure sales under chapter 39 of the statutes, with particular regard to the adequacy of the sales price. Treatment of that issue is outside the scope of this book.

Kepler v. Slade, 119 N.M. 802, 896 P.2d 482 (1995)

Facts:

- Bauers signed a note & mortgage to Home Mortgage, securing a debt on real estate.
- Bauers sold the property to Slade, taking a note secured by a deed of trust.
- Bauers assigned the note & deed of trust to Kepler.
- Slade sold the property to Betsworth, who defaulted on the Home Mortgage loan.
- Home Mortgage foreclosed on the mortgage, obtaining a judgment of foreclosure against all parties.
- Kepler then filed suit against Slade to collect on the note.
- Trial court ruled that the Home Mortgage foreclosure action was res judicata of Kepler's claim against Slade, and granted summary judgment to Slade.

Issue:

Whether a judgment in a prior foreclosure action bars a subsequent lawsuit to recover a debt on a personal note secured by a deed of trust on the same property, under the doctrine of res judicata.

Holding:

Reversed. At common law, upon default by the mortgagor, the mortgagee has independent, separate remedies: he may either sue on the note or foreclose the mortgage. The two remedies may be pursued at the same time, or consecutively. Because there are two separate causes of action, a judgment of foreclosure of a prior mortgage, where the parties had an opportunity to present their claims, bars only subsequent actions involving the same parties and the same cause of action, and does not bar a subsequent action on the junior note.

Comer v. Hargrave, 93 N.M. 170, 598 P.2d 213 (1979)

Facts:

- Comer sold real estate to Hargrave, who gave Comer a note and mortgage, which were placed in escrow. The note included a provision giving Comer the option to accelerate if Hargrave remained in default for more than 30 days.
- Hargrave tendered a monthly payment to the escrow agent more than 30 days after the grace period; the escrow agent returned the payment to Hargrave.
- Comer filed suit to foreclose the mortgage, without giving notice to Hargrave of his intention to do so. Trial court ruled for Comer; Hargrave appealed.

Issue: The Supreme Court held that *Carmichael v. Rice*, 49 N.M. 114, 158 P.2d 290 (1945) was controlling in this case, although the briefs of the parties on appeal did not mention that case.

Holding:

Reversed.

1. When the note contains an optional acceleration clause, a mortgagee must give notice to a defaulting mortgagor of his intention to accelerate the note before the mortgagee is entitled to file suit to foreclose the mortgage securing payment of the note. (This ruling deals with an optional acceleration clause. Would the ruling be different if the acceleration clause is automatic by its terms? Consult your attorney!)
2. Failure to accept a tender of the overdue payment made prior to notice is a waiver of the right to accelerate! In this case, the escrow agent refused to accept a past due payment tendered after the 30-day grace period provided by the note.

Wall v. Pate, 104 N.M. 1, 715 P.2d 449 (1986)

Facts:

- Wall contracted to buy a residence from Pate. Pate failed to consummate the sale, Wall purchased another house for a higher price at a higher interest, and sued Pate for damages.
- Trial court awarded \$3500 compensatory and \$500 punitive damages to Wall. Pate appealed, alleging a failure of proof on the elements of compensatory damages that would support any award.

Issue: What is the proper measure of damages for seller's repudiation of contract to sell?

Holding: Trial court used the wrong measure of damages. For seller's breach, compensatory damages are measured by the "loss of bargain" rule, which is the difference between the contract price and the fair market value of the property. Special damages may also be allowed, either alone or as an additional part of the compensatory award, which "flow from the disappointment of a special purpose for the subject matter of the contract or from unusual circumstances, either or both of which were known to the parties when they contracted. In such a case, the amount permitted under the general damage formula, alone, clearly will be either inadequate or nonexistent." Since there was no evidence of market value in the case, it is apparent that the compensatory award was not given for "loss-of-bargain" damages.

Hickey v. Griggs, 106 N.M. 27, 738 P.2d 899 (1987)

Facts:

- Mildred Hickey contracted to buy a triplex from Edward Griggs for \$75,000. Griggs' spouse did not join in the contract; the property was the separate property of Edward Griggs. The spouse had invested time and effort in the management of the property.
- Although Hickey was ready, able and willing to effectuate the agreement, Griggs declined to perform the contract.
- Hickey sued for specific performance and damages; trial court awarded her damages of \$7200, plus interest, costs and attorney fees.

Issues:

1. Whether evidence supported conclusion that Griggs was bound by the contract (he testified he was drunk when he signed it);
2. Whether Griggs' spouse had a lien against the property for her management services, and whether such lien made her joinder mandatory;
3. Whether the measure of Hickey's damages was correctly applied by trial court;
4. Whether trial court erred in granting attorney fees to purchaser.

Holding:

1. There was substantial evidence to support the conclusion that Griggs was not incapacitated at the time he signed the agreement; Court will not substitute its judgment for that of the trial court.
2. Community contributions and improvements to real property do not affect the title of separate ownership. "The right of the community to be reimbursed for the amount of the lien does not change the character of the property from separate to community...and separate property may be conveyed by the owner without the joinder of a spouse."
3. Reversed on this issue. "The general rule is that the purchaser is entitled, as general damages, for the refusal or inability of the vendor to convey, to recover the difference between the actual value of the property and the contract price. Since evidence supported a market value of \$95,000, Hickey's damages are set at \$20,000, being the difference between the purchase price and the market value.
4. Reversed on this issue. "It is an established rule in New Mexico that, absent statutory authority or rule of court, attorney fees or costs cannot be recovered as an item of damages....Nor did the contract provide recovery for reasonable attorney's fees."

Jeffers v. Martinez, 93 N.M. 508, 601 P.2d 1204 (1979)

Facts:

- Betty Martinez (formerly Doel) signed an REC in 1978 to sell a house to Jeffers. Earlier, in 1977, Betty had given a quitclaim deed to the property to herself and Frank Martinez as husband and wife, but the deed was never recorded. Frank did not join in the REC.
- Jeffers filed suit against Betty for specific performance of the REC. Betty contended the REC was void & unenforceable under NMSA 1978 sect.40-3-13(A), which provides that conveyances of real estate which is community property by one spouse alone is void. Jeffers claimed that they were bona fide purchasers for value without notice of the unrecorded deed and that, under NMSA 1978, sect. 14-9-3, the quitclaim deed, because it was not recorded, does not affect their rights under the REC.
- Trial court granted summary judgment to vendor (Martinez). Appealed.

Issue: Whether the provisions of the recording statute or the community property statute prevails in a conflict between them.

Holding: Reversed. Any conflict between sect. 40-3-13 and 14-9-3 should be resolved in favor of the latter statute. “Equitable principles require that the innocent purchaser should prevail over one who negligently fails to record a deed upon which he seeks to rely.” An issue of fact exists as to whether the Jeffers were innocent purchasers for value, or whether they had actual prior knowledge or notice of the unrecorded deed. The case is remanded for a hearing on that issue.

Comment: On remand, the trial court granted summary judgment a second time, and was again reversed because a material issue of fact still existed. On remand, the trial court granted summary judgment to Martinez for the third time, but awarded a refund to the Jeffers of their earnest deposit of \$300. The Court again reversed (99 N.M. 353, 658 P.2d 426 (1982), stating that the trial court had yet to determine whether the Jeffers were innocent purchasers for value, and therefore had not complied with the Court’s mandate. It added that if the Jeffers were found to be innocent purchasers for value, then the award of only the earnest deposit was error, because the correct remedy for refusal of a vendor to convey is the difference between the actual value of the property and the contract price (citing *Aboud*). We don’t know the eventual outcome of the case.

Montgomery v. Cook, 76 N.M. 199, 413 P.2d 477 (1966)

Facts:

- REC required buyers to make improvements to property within one year after date of REC, and to make first annual installment payment about 15 months after date of REC. The REC authorized escrow agent to deliver warranty deed to buyers upon proof that the improvements had been made.
- At inception of REC, sellers gave warranty deed to their attorney, to be placed in escrow. The attorney never delivered the deed to the escrow agent.
- Buyers completed the improvements within the year, asked bank escrow agent for the deed, and were advised the deed had never been put in escrow.
- Buyers did not pay the first annual installment, sellers instructed their attorney to not deliver the deed to the escrow agent until the payment was made.
- Sellers sent notice of default based on the missed annual payment, and thereafter terminated the REC and took possession of the property.
- Buyers sued for rescission and damages. Trial court awarded damages to buyers, plus interest.

Issues:

1. Is the failure of the seller to place a warranty deed in escrow a fundamental breach of the REC?
2. Were the buyers in default for not making the first annual installment payment, thereby excusing the sellers from the obligation to deposit the deed and barring the buyers suit for rescission and damages?
3. Was it proper to award damages to buyers, in addition to allowing rescission of the contract?

Holding:

1. The sellers' obligation to deliver the deed to the escrow agent 'was an absolute condition precedent so vital and essential to the contract that a failure to so deliver the deed relieved vendees of any obligation whatsoever until such deed was so deposited' (emphasis added).
2. The buyers were not in default for withholding the annual payment, because the sellers' failure to deliver the deed was a fundamental prior breach of the contract that suspended buyers' subsequent obligation to make the payment.
3. Award to buyers of market value of improved land less the purchase price, plus interest is affirmed.

Gonzales v. Garcia, 89 N.M. 337, 552 P.2d 468 (1976)

Facts:

1. Gonzales contracted to buy 22.675 acres from Garcia. Gonzales later discovered that 10.157 acres of the tract was not owned by Garcia; Gonzales then purchased the 10.157 acres from the owner for \$7,109.90.
2. Gonzales sued Garcia for fraud, misrepresentation and breach of the warranty covenants in the deed. Trial court found that the deficiency resulted not from fraud, but from mistake of the vendor. Trial court awarded \$7,109.90 to Gonzales; Court of Appeals reversed; Court granted certiorary.

Issue: Whether the Court of Appeals, in determining the standard of damages to be the proportionate part of the purchase price, applied the correct measure of damages.

Holding: Court of Appeals reversed; trial court affirmed.

1. Based on the theories of the complaint, two remedies are available.
 - (a) For breach of the covenant of seisin, because purchaser eventually acquired title from the actual titleholder, the measure of damages is the purchase price for the outstanding title, provided it is reasonable in amount.
 - (b) Under the theory of mistake of vendor, damages are generally limited to ratable abatement of the purchase price, plus interest, assuming that all the land had approximately equal quantitative value.
2. The correct measure of damages is the price of acquiring the deficient title. Although the mistake was innocent, "...it was a significant mistake because approximately 45% of the land area was not conveyable by this vendor. Vendor should know the extent of his property or at least make significant efforts in ascertaining it before selling it under a warranty deed. Vendor is in the best position to obtain this information....".

C. Lambert & Associates, Inc. v. Horizon Corporation, 106 N.M. 661, 748 P.2d 504 (1988)

Facts:

- Horizon sold land in Rio Rancho to Lambert on a land sales contract. Paragraph 1 stated that the total acreage was "36.0" acres. Paragraph 2 stated "The purchase price...shall be...\$720,000...".
- At trial, an officer of Horizon testified that the agreed price was \$20,000 per acre.
- Due to a realignment of a road bisecting the property, and a survey discrepancy, there was a shortfall of 1.3154 acres in the actual acreage conveyed.
- Contract required buyer to share any costs of resolving any drainage problems arising from the "...natural drainageways flowing across the property...". There was an encumbrance on the land consisting of the floodwaters of the "Black Arroyo". There was also a surface "swale" running across the property.
- The contract contained an "as is" clause, and an explicit statement that buyer had examined the property, was aware of the natural drainageways, and was not relying on the seller in any manner.
- Lambert sued for reduction in price for acreage diminution, and for declaratory judgment that Lambert had no financial obligation to pay for water diversion construction costs pertaining to the Black Arroyo.
- Trial court awarded price reduction based on acreage shortfall; but denied relief for construction costs.

Issues:

1. Whether the purchase price provision is ambiguous, and whether parol (oral) testimony is admissible.
2. What is the effect of an “as is” clause on (a) a shortfall in actual acreage from the contracted acreage, and (b) buyer’s obligation to pay part of the costs for required construction to divert flood waters from the “natural drainage way”?

Holding:

Trial Court is affirmed on both issues.

1. The provisions of paragraphs 1 and 2 of the contract created an ambiguity as to whether this was a single tract sold at a single price, or whether the subject of the sale was 36 acres, more or less, or 36 acres specifically. Quoting *Branch v. Walker*, 56 N.M. 594, 247 P.2d 172 (1952): “Whether a sale of real estate was a sale in gross or by acre, depends upon the intention of the parties....”. The Court ruled that the oral testimony of the corporate officer was admissible to resolve the ambiguity.
2. “An ‘as is’ clause provides absolute protection to a seller such as Horizon only when the buyer and seller possess equal knowledge of the property. Here, while Lambert’s knowledge of the property was equal to that of Horizon’s insofar as most essentials of the contract were concerned, Lambert relied on Horizon for its knowledge of the total acreage in the property, and for such information as would have informed him about the realignment of Golf Course Road.”
3. Where the issue of the arroyo was concerned, the Court concluded that Lambert did have knowledge of the property equal, and perhaps even superior, to that of Horizon. He was an experienced real estate broker, he inspected and investigated the property, and he had engineering drainage studies available to him. Therefore, as to this issue, the “as is” clause provided protection to Horizon.

Robison v. Katz, 94 N.M. 314, 610 P.2d 201 (1980)**Facts:**

- Katz purchased a mobile home park from Campbell in exchange for a house in Los Alamos, a duplex, cash, and an REC for the unpaid balance, in which she assumed underlying mortgages and REC’s. Katz defaulted in making payments on an underlying REC owned by Stepnowski, which she had assumed and agreed to pay. Stepnowski terminated that REC, and litigation ensued between Stepnowski, Campbell & others. See *Campbell* in this appendix.
- Seller, prior to the sale, had failed to disclose the poor condition of the park’s utilities and septic, and had misrepresented the repair and maintenance expenses. The real estate broker, Robison, was found to be in a fiduciary capacity as to Katz, but sold the property to Katz as exclusive listing agent for Campbell. Robison failed to investigate the information supplied to him by Campbell, and negligently misrepresented material facts and failed to disclose poor condition of the water & septic systems to Katz.
- Robison filed suit for a declaratory judgment determining his liability for misrepresentations. Katz counterclaimed, seeking rescission & consequential & punitive damages. Campbell cross-claimed, alleging abuse of privacy by Robison for allowing a 3rd party to listen to & record telephone conversations.
- Trial court held that Katz would be entitled to rescission based on negligent misrepresentation of facts, but that Katz’ inability to return the trailer park and restore Campbell to the status quo ante barred her from obtaining that remedy. Instead, it awarded Katz damages, less various set-offs, and denied Katz’ claim for consequential & punitive damages. All parties appealed.

Issues:

1. Whether rescission of a contract may be granted when the defrauded party is unable to restore the other party to the status quo ante;
2. Whether a party who obtains rescission is also entitled to consequential damages; and
3. Whether punitive damages are proper under the circumstances.

Holding:

1. "The general rule in New Mexico is that rescission should be granted a party who, in entering a contract, justifiably relied on a misrepresentation of a material fact, irrespective of the good or bad faith of the party making the misrepresentation.... Generally, the purchaser is allowed to rescind a contract only if he can place the vendor in the *status quo ante*" (citations omitted). However, strict compliance is not necessary where it has been rendered impossible by circumstances for which the purchaser is not responsible, or for which the vendor is responsible.

The Court was impressed by the fact that, although Katz had assumed the obligation of the Stepnowski REC, Campbell was also liable on that contract, knew that Katz was in financial difficulty and might not be able to make all underlying payments, had the opportunity to make the payment to preserve the property, and did not do so.

Also, at the time Katz filed her cross claim for rescission, she was in a position to restore the trailer park to Campbell. The trial was postponed on a motion by Campbell & Robison for a continuance, which was opposed by Katz on the ground that if the case was not tried as scheduled, she would be forced to default because of her dire financial condition. One month after the postponement, she defaulted. The conduct of Campbell made it equitable that he should suffer the loss resulting from the Stepnowski forfeiture, therefore the rule requiring complete restoration as a prerequisite for rescission does not apply. Reversed. Trial Court is ordered to grant Katz rescission of the REC. Because restitution would be complex, the Court ordered an accounting between the parties.

2. "...restitutionary damages conform with the purpose of rescission, which is to put the defrauded party back in as good a position as he occupied before entering the contract. Consequently, we hold that such damages may be awarded along with rescission." However, the damages should be limited to those expenses which must have been or should have been contemplated as probable consequences of the fraud by the parties whose actions are the basis for the rescission. In this case, because "...everything was arranged by Robison...", so Robison is ordered to pay the special damages.
3. "Reckless behavior will warrant the award of punitive damages, if the injured party is able to prove actual damages." Since the trial court found that Robison had made material misrepresentations in reckless disregard for their truth, a finding which was not challenged on appeal, the case is reversed and remanded for a hearing on the issue of actual damages.

Lloyd v. Southwest Underwriters, 50 N.M. 66, 169 P.2d 238 (1946)

Facts:

REC allowed Seller 30 days after date of REC to furnish an abstract of title. Purchaser was allowed 60 days thereafter to complete abstract examination to determine whether Seller had a good and merchantable title. Examination showed an outstanding defect. Purchaser demanded return of deposit from escrow agent.

Issue:

Whether escrow agent was obligated to return money to buyer upon showing of a defect in title or whether seller had a reasonable time to make a good title.

Holding:

In the absence of a contrary provision in the REC, the seller has a "reasonable time" to perfect title. Time is not of essence, unless the REC expressly so provides. "Time of Essence" provision contained in the default paragraph of REC was for the benefit of seller only, and did not apply to requirement to provide good title.

Comment: The RANM forms contain a broad "time is of the essence" clause expressly declared to be applicable to both parties, which would avoid the limited application of the clause as occurred in this case.

Meech v. Gallegos, 86 N.M. 28, 519 P.2d 124 (1974)

Facts:

- Meech purchased a motel from Gallegos on an REC containing standard contract purchaser's title insurance paragraph, with this added sentence: "Said policy of title insurance shall be furnished as soon as possible and in any event within one year after date of this instrument".
- Gallegos failed to comply within the allowed one year. There was an encroachment of buildings of six feet on adjoining property, and a quiet title suit was pending at the time Meech sued for rescission and restitution. Trial court granted summary judgment to Meech on the issue of rescission, and also on the counterclaim for compensation for use of premises.

Issues:

1. Whether the seller was entitled to a reasonable allowance of time to furnish title insurance.
2. Whether an issue of fact existed as to the proper amount of compensation to seller for buyer's use of the property.

Holding:

1. What is a reasonable time for the seller to perfect title is a question of fact. In the absence of a contrary contractual commitment, the seller may have a reasonable time to perfect title. However, the contract specified a time limit within which to provide a policy of title insurance. Since the time limit was not met, the trial court was correct in determining that a material issue of fact did not exist as to whether the delay was reasonable.
2. The complaint had alleged "that the premises...has been maintained and is in as good or better condition at the present time then [sic] it was at the time of the date of the contract...". This allegation was denied. The remedy of rescission includes the requirement that the parties be restored to their original status. Therefore, compensation for use of the premises, and the condition of the premises, are legitimate issues of fact. The trial court erred in granting summary judgment against the vendor on the counterclaim.

Lorentzen v. Sanchez, 109 N.M. 693, 789 P.2d 1260 (1990)

Facts:

- Lorentzen bought land on a form REC for \$10,000 with \$2500 down pmnt, balance on annual payments.
- A typed provision was added to the REC, wherein Lorentzen agreed to "commence and complete as soon as possible a suit to quiet title to the property herein conveyed at his own cost....It being further provided, however, that in the event the Quiet Title Suit is prevented from reaching its conclusion within six months hereof that the Purchaser may instruct the Escrow Agent to deliver to the Seller the Special Warranty Deed escrowed herewith, whereupon the Seller shall immediately pay \$2,500.00 to the Purchaser."
- Lorentzen did not elect to rescind the REC with the six month period. He filed suit to quiet title eight days after the six month period expired. He obtained judgment quieting title in his name, but also stating that his title was subject to the REC. He then sued Sanchez, seeking modification of the REC.
- Trial court found that Sanchez owned only a one-fourth interest in the property when the REC was made, and ruled that Lorentzen should pay only 25% of the purchase price, or \$2,500.

Issue: Whether Lorentzen contracted to assume the responsibility and costs for curing any title defects, in lieu of exercising his option to rescind the contract and obtaining a refund of the purchase price.

Holding: Reversed. Sanchez had no duty to perfect the property's title, as Lorentzen contracted to assume that burden. The REC gave Lorentzen six months to conclude a quiet title suit. Failing that, he had the option to rescind the REC within the six months and recover his down payment.

Chavez v. Gomez, 77 N.M. 341, 423 P.2d 31 (1967)

Facts:

Form 103 REC (apparently) with provisions for abstract or title policy showing “good and merchantable” title to be delivered at time warranty deed is delivered. Seller did not comply. Buyer insisted that seller comply, then accepted a warranty deed after final payment, then sued for damages after quieting title.

Issues:

1. Merger by deed?
2. Waiver?

Holding:

1. No merger. “Contract provisions as to title, possession, quantity or emblements of the land are, again generally speaking, conclusively presumed to be merged in a subsequently delivered and accepted deed.” “Where the contract provisions are not performed by delivery and acceptance of the deed, there is no merger. Such provisions are collateral to and independent of the deed...Here the obligation was to furnish either an abstract or title insurance ‘at the time of delivery’ of the deed showing good and merchantable title ‘on the date of the delivery of the warranty deed.’.... This obligation could not be performed by the delivery and acceptance of the deed.”
2. No waiver. There was conflicting evidence, so the Court lets the trial court judgment stand.

Comment:

This case is cited by *Kuzemchak*, this appendix.

Leigh v. Hertzmark, 77 N.M. 789, 427 P.2d 668 (1967)

Facts:

Purchase Agreement provision that buyer was to pay “water and sewer assessments at not more than \$216.84 per lot” was inadvertently omitted from the REC, which required buyer to pay “water and sewer assessments...”.

Issue: Did the doctrine of merger cause the omitted provision to be extinguished?

Holding: Doctrine of merger only applies in the absence of mistake. By mistake, the REC did not conform to the binder, and merger does not apply. The provision in the purchase agreement remains in effect.

FORMS APPENDIX

1.	Form 103, Real Estate Contract.....	FA-1
2.	RANM Form 11, Real Estate Contract (Revised 12/81)	FA-5
3.	RANM Form, Real Estate Contract (Revised 01/98)	FA-9
4.	RANM Form, REC Addendum to Purchase Agreement (Revision Pending)	FA-14
5.	(Reverse) Assignment of Trust Funds.....	FA-16
6.	Seller's Assignment of Real Estate Contracts.....	FA-17
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12.	Release of Seller's Collateral Assignment.....	FA-25
13.	Warranty Deed-Statutory Form.....	FA-26
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24.	Affidavit of Default.....	FA-43

Notice

The forms contained in this appendix are specimens only, and were current as of the copyright date of this book. The reader should contact the producers of the forms for current versions. The forms presented here should not be relied upon as being consistent with current statutes and case law.

If you do not have an attorney to prepare these forms for you, you may call Security Escrow for a referral.

THIS CONTRACT, made in triplicate, this _____ day of _____, 19____,
by and between _____

_____ of the first part hereinafter called the Owner, and _____

whose address is _____

_____ of the second part hereinafter called the Purchaser.

WITNESSETH:

1. That the said Owner, in consideration of the covenants and agreements on the part of the said Purchaser, hereinafter contained, agrees to sell and convey unto the said Purchaser the following real estate situate, lying and being in the County of _____ and State of New Mexico, to-wit:

2. The Owner undertakes and agrees, upon full performance of the conditions, covenants and agreements to be performed by the said Purchaser, to make, execute and deliver to said Purchaser, a good and sufficient warranty deed for the above real estate.

3. In consideration of the premises, the said Purchaser agrees to buy said real estate and to pay said Owner therefor the sum of _____ Dollars (\$ _____) lawful money of the United States of America, which sum is to be paid as follows, to-wit: _____ Dollars (\$ _____), cash in hand paid, the receipt of which is hereby acknowledged, and the balance of \$ _____ shall be payable as follows, to-wit:

If not otherwise specified the above-mentioned payments shall continue until the full purchase price and interest on deferred payments shall have been fully paid. All of said unpaid balance of the purchase price shall bear interest at the rate of _____ per centum (_____%) per annum from date, payable _____

Further, it is agreed that if this Real Estate Contract is placed by the Owner in the hands of an attorney upon default by the Purchaser in the payment of any monies due hereunder for the purpose of mailing of written demand, pursuant to the termination provision of Paragraph 8 hereof, the Purchaser shall pay, in addition to the payment of all other sums required hereunder, the sum of \$ _____ to cover the costs, expenses, and fees involved in such action.

4. Said Purchaser agrees to keep the buildings upon said real estate insured against the hazards covered by fire and extended coverage insurance in an insurance company satisfactory to said Owner in the sum of \$ _____, for the benefit of said Owner as his interest may appear, and deliver said insurance policy to said Owner.

5. Said Owner undertakes and agrees to pay all taxes up to and including _____ half of 19____, together with all other liens and charges now against said real estate, except as herein stated, and said Purchaser agrees to assess said real estate for taxation to himself for the year 19____, and, thereafter, pay all taxes and assessments and make all street improvements of every kind and nature whatsoever that may hereafter be levied or ordered by lawful authority and which would in the event of failure so to create a charge against the said real estate. All taxes, assessments, liens, and other charges against said real estate have been prorated to the date hereof, and the Purchaser has assumed the payment of the same for the current year.

6. Said Purchaser undertakes and agrees to assume any paying lien now assessed against said property and agrees to pay all installments of principal and interest thereon from and after date hereof.

7. Should the said Purchaser fail so to keep the said buildings insured; so to assess said property; so to pay said taxes and assessments; so to make said street improvements or so to pay said paving installments, the said Owner shall have the right to insure the buildings, assess the property, pay the taxes and pay the paving lien installments with whatever costs and legal percentages there may be added thereto, and any amounts so paid, with interest at eight per cent per annum from date of payment until repaid shall be included in the unpaid balance of this contract and shall be repaid by the said Purchaser.

8. It is mutually agreed that time is the essence of this contract. Should the Purchaser fail to make any of the said payments at the respective times herein specified, or fail or refuse to repay any sums advanced by the Owner under the provisions of the foregoing paragraph, or fail or refuse to pay said taxes, assessments or other charges against said real estate and continue in default for _____ days after written demand for such payments, or payment of taxes or payments of assessments or other charges against said real estate, or repayment of sums advanced under provisions of the foregoing paragraph has been mailed to the Purchaser addressed to _____ h _____ at _____

then the Owner may, at his option, either declare the whole amount remaining unpaid to be then due, and proceed to enforce the payment of the same; or he may terminate this contract and retain all sums theretofore paid hereunder as rental to that date for the use of said premises, and all rights of the Purchaser in the premises herein described shall thereupon cease and terminate and _____ h _____ shall thereafter be deemed a tenant holding over after the expiration of _____ h _____ term without permission. An affidavit made by said Owner or his agent showing such default and forfeiture and recorded in the County Clerk's office shall be conclusive proof, in favor of any subsequent bona fide purchaser or encumbrancer for value, of such default and forfeiture; and the Purchaser hereby irrevocably authorizes the Owner or his agent to thus declare and record such default and forfeiture, and agrees to be bound by such declarations as _____ free act and deed.

9. Said Purchaser shall be entitled to take possession of said real estate and retain possession thereof until this contract shall be terminated by the exercise by the Owner of the option above provided, or until the delivery by the hereinafter-named escrow agent back to the Owner of all the papers held in escrow herewith, but the legal title to said real estate shall remain in said Owner until this contract has been fully performed upon the part of the Purchaser and deed executed and delivered as hereinbefore specified.

10. It is understood and agreed upon the completion of all the stipulations and agreements herein contained, said Owner will, at the time of delivery of Warranty Deed, also deliver to said Purchaser, abstract of title or title insurance, showing said real estate to be of good and merchantable title on the date of the delivery of the Warranty Deed. It is further understood and agreed, however, that in the event the said Purchaser should cause any entries to be made upon the County Records which would affect the title to the above-described land and which would put the Owner to an extra expense in having his title abstracted or insured, then the said Purchaser shall pay to said Owner any and all sums of said extra expense.

11. It is further understood and agreed that no assignment of this contract shall be valid unless the same be endorsed hereon and countersigned by the Owner.

12. It is mutually understood and agreed that all the covenants and agreements herein contained shall extend to and be obligatory upon the heirs, executors, administrators, successors and assigns, respectively, of the parties to this contract.

13. It is understood and agreed that, coincident herewith, the Owner has executed a good and sufficient warranty deed conveying the above-described premises to the Purchaser, which said deed, together with a copy hereof, shall be placed in escrow with

who is hereby designated and appointed Escrow Agent, to be delivered by the Escrow Agent to the Purchaser upon full compliance on his part with all the conditions of this contract. In consideration of that fact the said Purchaser executes, coincident herewith, a special warranty deed reconveying the above-described premises to the Owner, which said special warranty deed shall also be placed in escrow herewith to be delivered by the Escrow Agent to the Owner in the event that the said Purchaser defaults as hereinabove set forth, and remains in default for a period of _____ days after written demand for payment as provided for in Paragraph 8.

14. For the purpose of carrying out the terms of this contract, the following letter is directed to the Escrow Agent, to-wit:

ESCROW LETTER

To _____, New Mexico

In re the sale under contract by _____
to _____
of the property hereinabove described, we hand you herewith the following papers to be placed in escrow, to-wit:
1. Original copy of this Real Estate Contract 2. Warranty Deed 3. Special Warranty Deed

We also hereby appoint you Escrow Agent hereunder, and direct you as such Escrow Agent to collect the payments provided for in the above contract and place the money so collected to the credit of _____

Upon full compliance with the terms of said contract on the part of the Purchaser, you are directed to deliver all the above-mentioned papers to said Purchaser. In the event that the said Purchaser should default as set forth in the foregoing contract, and so remain in default for a period of _____ days after written demand for payment as provided for in Paragraph 8 of the foregoing contract, you are directed to deliver all the above-mentioned papers to said Owner.

Further, the Escrow Agent is hereby instructed by the parties hereto that after each and every written demand is mailed to the Purchaser, pursuant to Paragraphs 3 and 8, and a copy hereof is furnished to the Escrow Agent, not to accept less than the full amount of the sums due hereunder, as specified in such written demand, including the said additional \$ _____

IN WITNESS WHEREOF the said parties have hereunto signed and sealed this contract in their own proper persons the day and year first above written.

_____, N. M., _____, 19____ (SEAL)
We hereby accept the appointment and designation of
Escrow Agent herein and acknowledge receipt of the
above-mentioned papers. _____ (SEAL)
_____ (SEAL)
_____ (SEAL)

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(SEAL)

Notary Public

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(SEAL)

Notary Public

ASSIGNMENT

(Date)

_____, N. M.

For value Received I We do hereby grant, set over and assign unto _____

all my our right, title and interest in and to the foregoing contract and in and to the property therein described.

WITNESS MY OUR HAND AND SEAL the day and year last above written.

(SEAL)

(SEAL)

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(SEAL)

Notary Public

ASSIGNEE'S ACCEPTANCE

(Date)

_____, N. M.

The undersigned Assignee named in the above assignment of the foregoing contract hereby approve and accept the same and agree to be bound by all the terms, covenants, and conditions thereof.

WITNESS MY OUR HAND AND SEAL the day and year last above written.
Assignee's address for notices and demands:

(SEAL)

(SEAL)

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(SEAL)

Notary Public

OWNER'S CONSENT

(Date)

_____, N. M.

I We the undersigned, Owner of the property described in the foregoing contract, hereby consent to the foregoing Assignment and agree to mail a copy of any notice of default and/or demand for payments, or payment of taxes, assessments, or other charges, or repayment of any sums advanced by the Owner, which I we may cause to be sent to the Purchaser under the terms of the said Real Estate Contract, to the said Assignee at Assignee's address for notices and demands as set forth above.

WITNESS MY OUR HAND AND SEAL the day and year last above written.

(SEAL)

(SEAL)

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(SEAL)

Notary Public

No. _____ \$ _____

REAL ESTATE CONTRACT

TO _____

Dated _____, 19____

STATE OF NEW MEXICO, }

ss.

County of _____

I hereby certify that this instrument was filed
for record on the _____ day of _____

A. D., 19____

at _____ o'clock _____ M., and was duly

recorded in Book _____ of Records of

Deeds and Conveyances, page _____

on this _____ day of _____

A. D., 19____

Clerk and Ex-Officio Recorder.

Deputy.

Bring this Contract when you make payments
and have same endorsed hereon.

Consideration \$ _____

PAYMENTS

DATE	RECEIVED	BY	PRINCIPAL	INTEREST	BALANCE
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PAYMENTS—Continued

DATE	RECEIVED	BY	PRINCIPAL	INTEREST	BALANCE
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Real Estate Contract

THIS CONTRACT IS MADE in triplicate this _____ day of _____, by and between **seller's name**, whose address is **seller's address** hereinafter called the Seller, and **purchaser's name, as joint tenants**, whose address is **purchaser's address** hereinafter called the Purchaser. Whenever a masculine pronoun is used it shall also be considered as referring to the female gender and plural pronouns, whichever is proper.

1. SALE: The Seller, in consideration of the promises and agreements herein made by the Purchaser, agrees to sell and convey to the Purchaser the following described real estate, hereinafter called the Property, in the County of _____ and State of New Mexico:

Legal Description

Subject to reservations, restrictions, and easements of record and to taxes for the year 1998 and years thereafter.

The Seller agrees, upon completion of all terms and conditions of this contract by the Purchaser, that the Purchaser shall then receive the Warranty Deed and related documents placed in escrow with this Contract.

2. PRICE AND PAYMENT: The Purchaser agrees to buy the above-described Property and to pay Seller therefor the total sum of **NINE HUNDRED NINETY NINE THOUSAND NINE HUNDRED NINETY NINE AND 99/100 DOLLARS (\$999,999.99)**, payable as follows: **NINE HUNDRED NINETY NINE THOUSAND NINE HUNDRED NINETY NINE AND 99/100 DOLLARS (\$999,999.99)**, cash down payment, the receipt of which is hereby acknowledged, and the balance of **ZERO AND NO/100 DOLLARS (\$0.00)**, payable as follows:

In monthly installments of \$0.00 each, or more, at Purchaser's option, including interest from date hereof on the unpaid principal balance at the rate of 0.00% per annum, commencing _____ and on or before the 1st day of each successive month thereafter until paid in full.

Purchaser shall pay a late payment penalty of \$25.00 on any payment that is over fifteen (15) days past due, payable at the time such late payment is made. Any late payment penalties shall be paid to Seller as additional interest. Unless otherwise instructed by Seller in writing, Escrow Agent may accept a regular payment without the late charge, which shall be due upon demand.

The payments as above provided shall be paid to the escrow agent and continue until the entire unpaid balance of the purchase price (exclusive of any prior lien or obligation being assumed) plus any accrued interest due to the seller is fully paid. Said unpaid balance shall bear interest at the rate of **Zero percent (0.00%)** per annum from the effective date.

APPLICATION OF PAYMENTS: Check and initial only one of the following two paragraphs.

☐ (a) Payments, excepting prepayments, shall be applied to regularly scheduled installments in the order in which the same were due and shall be credited as though the payments were made on their respective due dates.

Initials

☐ (b) Payments shall be applied as of the date of receipt by Escrow Agent first to accrued interest then to principal balance of this contract.

Initials

All payments shall be assumed to be regular payments, and not prepayments, unless otherwise specified by Purchaser in writing at the time of delivering such payments to Escrow Agent. Unless otherwise provided, Purchaser may prepay the unpaid balance in whole or in part at any time. Any prepayment shall be credited first to unpaid or deferred late charges, then to accrued interest, then to the principal balance of this Contract exclusive of assumed liens or obligations, then to assumed liens or obligations as described in this paragraph. Notwithstanding any prepayments, Purchaser shall make the next regularly scheduled payments.

If Purchaser fails to make any of the payments or perform any other obligations required hereunder, including the payment of any assumed obligation, and if Escrow Agent or Seller's attorney makes written demand therefor pursuant to Paragraph 5 below, the Purchaser shall pay within the time allowed the additional sum of \$75.00, unless otherwise stated, for the demand letter fee.

The following lien(s) or obligation(s) is currently outstanding on the property:

Type of Lien or Obligation Holder	Loan Number	Recording Data: Book & Page
Lien or Obligation	loan number	rec data
Lien or Obligation	loan number	rec data

This space is intentionally left blank.

3. PURCHASER TO PAY INSURANCE, TAXES AND PAVING LIENS, AND SELLER'S RIGHTS:

(a) **Insurance.** The Purchaser agrees to keep the insurable improvements upon the Property insured against the hazards covered by fire and extended coverage insurance, with an insurance company satisfactory to Seller in the sum of not less than **N/A**, for the benefit of the Purchaser and Seller as their interests may appear, and furnish a copy of the insurance policy or certificate of the insurance policy to Seller annually prior to expiration of existing insurance.

(b) **Taxes.** Unless otherwise stated herein, the property taxes for the current year have been divided and prorated between Seller and Purchaser as of the date of this Contract, and the Purchaser is responsible for and shall pay the taxes and assessments of every kind hereafter billed. Purchaser shall have the Property assessed for taxation in Purchaser's name. Purchaser shall send copies of the paid tax receipts each year to Seller, within 30 days after taxes are due.

(c) **Paving and Other Improvement Liens and Standby Charges.** Unless otherwise stated herein, the Purchaser assumes any paving and/or other improvement lien and/or standby charges now assessed against the Property and agrees to pay all installments of principal and interest thereon that hereafter become due.

(d) **Seller's Rights.** If the Purchaser fails to pay insurance premiums, taxes and assessments, paving liens, improvement liens or standby charges, or other such matters prior to the same becoming delinquent, Seller may pay the same (but is not obligated to do so) for protection of the Property and his interest therein. Payment of such charges shall not be deemed a waiver of any default of Purchaser for failure to pay such charges, and such amounts as have been so paid shall be immediately due and payable to Seller, and shall bear interest until paid at the same rate as provided in Paragraph 2 above.

4. PURCHASER'S RIGHT, SELLER'S RETENTION OF INTEREST:

Purchaser shall be entitled to take possession of the Property and retain possession unless and until Purchaser's interests under this Contract shall be terminated by Seller as provided in Paragraph 5 below. Legal title to the Property shall remain in Seller's name until this Contract has been fully performed upon the part of Purchaser and the Warranty Deed delivered as specified.

5. SELLER'S RIGHTS IF PURCHASER DEFAULTS:

(a) **Default Notice.** Time is of the essence in this Contract, meaning that the parties shall perform their respective obligations within the times stated. If Purchaser fails to make any of the payments required in Paragraph 2, herein, at the times specified, or fails or refuses to maintain insurance or to pay taxes, assessments or other charges against the Property, or fails or refuses to repay any sums advanced by the Seller under the provisions of Paragraph 3 above, the Seller may make written demand upon the Purchaser, with such notice to specify the default and the curative action required, at his address as follows: **purchaser's address** or at such other address that Purchaser may designate by a written statement delivered to the Escrow Agent.

(b) **Manner of Giving Default Notice.** Notice in writing shall be given by certified mail, return receipt requested, addressed to the Purchaser at the effective address for Purchaser as provided in Paragraph 5(a), with a copy to Escrow Agent. Purchaser expressly acknowledges that notice to him by mail, in the manner above specified, is sufficient for all purposes, regardless of whether he actually receives such notice.

(c) **Purchaser's Failure to Cure Default Results in Termination of Contract or Acceleration of Entire Unpaid Balance.** If the Purchaser fails or neglects to cure any default within **thirty (30)** days after the date Seller's default notice is mailed, then the Seller may, at his option either declare the whole amount remaining unpaid to be then due and proceed to enforce payment of the entire remaining unpaid balance, plus any accrued interest, together with reasonable attorney's fees, or he may terminate Purchaser's rights to the Property and retain all sums paid as liquidated damages to that date for the use of the property, and all rights of Purchaser in the Property shall thereupon end. If the final day for curing the default shall fall on a Saturday, Sunday, or non-business day of the Escrow Agent, then the period for curing the default shall extend to the close of business on the next regular business day of the Escrow Agent.

Acceptance by Escrow Agent of any payment tendered shall not be deemed a waiver by Seller, or extension of the time for cure, of any other default under this Contract. In the event of termination, Purchaser hereby waives any and all rights and claims for reimbursement for improvements he may have made upon the Property.

(d) **Affidavit of Uncured Default and Election of Termination.** A recordable affidavit made by Seller, his agent, or Escrow Agent, identifying the parties, stating the legal description of the Property or the recording data of this Contract and stating the date that notice was duly given as provided above, that the specified default has not been cured within the time allowed and that the Seller has elected to terminate, and delivered to the Escrow Agent shall be conclusive proof for the Escrow Agent and any subsequent Purchaser or encumbrancer for value of such uncured default and election of termination.

(e) **Purchaser Becomes Tenant.** Upon termination Purchaser has no continuing right to possession. If Purchaser remains in possession of the Property after this Contract has been terminated as above provided, Purchaser shall then become a tenant at will, for a rental amount equivalent to the installment payment theretofore required as monthly payments under this Contract, with the first such rental payment due immediately, in advance, and such tenancy being subject to termination by either party upon thirty (30) days separate prior written notice. Seller's acceptance of such rental payment(s) shall not be deemed as any waiver of his rights, nor shall it constitute any manner of estoppel.

(f) **Legal Right to Evict Purchaser.** Foreclosure entry and detainer proceedings, in addition to any other appropriate legal remedies, may be utilized by the Seller if necessary to obtain possession of the Property following termination of this Contract and termination of Purchaser's continued tenancy thereafter. If such proceedings are filed, Purchaser shall be liable for Seller's reasonable attorney's fees plus the legal costs of such action.

6. TITLE INSURANCE:

Seller is delivering a Contract Purchaser's Title Insurance Policy to Purchaser at the time this Contract is made, showing merchantable title to the Property as of the date of this Contract, subject to the matters referred to in this Contract, and Seller is not obligated to provide any other or further evidence of title.

7. PURCHASER'S RIGHT TO SELL:

(a) **First Provision:** Purchaser shall be entitled to sell, assign, convey or encumber his entire interest in this Contract (but not a portion thereof) and the Property to any person or entity, hereinafter called the Assignee, and may retain a security interest therein, without obtaining the consent or approval of the Seller. The Purchaser shall not, however, be released from his obligations hereunder by any such sale, assignment, conveyance or encumbrance. In the event Purchaser does sell, assign, convey or encumber said interest, then Purchaser, his Assignee, or any subsequent Assignee shall deliver a copy of such written sale, assignment, conveyance or encumbrance document to Escrow Agent.

Such sale, assignment, conveyance or encumbrance document shall specify the address of the Assignee and upon receipt of such document by the Escrow Agent, Seller shall send notice of any default to the Assignee. If such document is not received by the Escrow Agent, Seller shall not be required to send notice of default to the Assignee, unless Seller has actual knowledge of the Assignee's name, address and interest in the property.

(b) **Special Alternative Provision:**

CAUTION: THE FOLLOWING PROVISION SEVERELY RESTRICTS THE RIGHT OF PURCHASER TO SELL, ASSIGN, CONVEY OR ENCUMBER THIS CONTRACT AND THE PROPERTY. If the parties wish to invoke this Provision, they should check the box as indicated and each initial as provided. If the Special Alternative Provision is elected, the First Provision does not apply.

☐
Initials

Purchaser shall not be entitled, directly or indirectly, to sell, assign, convey or encumber all or any portion of the Purchaser's interest in this Contract or in the Property without first obtaining the written consent of Seller, and Seller shall not be under any obligation of any kind to give such consent. In the event that purchaser shall, directly or indirectly, sell, assign, convey or encumber or contract to sell, assign, convey or encumber, directly or indirectly, all or any portion of the Purchaser's interest in the Contract or in the Property without consent of Seller, it shall be an event of default subject to the rights of Seller in Paragraph 5, herein.

Caution: If the Property is subject to any prior mortgage(s), Deed(s) of Trust or Real Estate Contract(s), then the provisions thereof should be examined carefully for any conflict with the above provision.

8. BINDING EFFECT: This Contract shall extend to and be obligatory upon the heirs, executors, administrators, personal representatives, successors, and assigns of the parties to this Contract.

9. APPOINTMENT OF AND INSTRUCTIONS TO ESCROW AGENT:

The Parties hereby appoint as Escrow Agent:

The following papers are herewith placed in escrow:

1. Signed copy of this Contract
2. Original Warranty Deed signed by Seller
3. Original Special Warranty Deed signed by Purchaser

Add following information, if applicable.

Name and address of mortgagee:

None

Loan No.

Name and address of Escrow Agent under any other contract on the Property

None

(a) The fee(s) of the Escrow Agent shall be paid as follows.

If such fee(s) are paid wholly or in part by Purchaser, such amount shall be in addition to the amounts due from Purchaser as provided in Paragraph 2, herein. The Escrow Agent is instructed to accept all monies paid in accordance with this Contract and remit the money received (less applicable escrow fees) as follows:

(b) All payments shall be deemed provisionally accepted when tendered, subject to determination by the Escrow Agent of the correct amount and its timeliness

(c) Upon full payment of all amounts due and owing to the Seller under this Contract by the Purchaser, the Escrow Agent is directed to release and deliver the escrow documents to the Purchaser

(d) If the Seller or his agent delivers an Affidavit of Uncured Default and Election of Termination (as described in Paragraph 5 above) to the Escrow Agent, then the Escrow Agent shall release and deliver the escrow documents to the Seller. The Escrow Agent shall be entitled to rely on such Affidavit as conclusive proof of termination

(e) The Escrow Agent is instructed that after each and every written demand is mailed to the Purchaser, pursuant to Paragraph 5 above, and a copy thereof is furnished to the Escrow Agent, not to accept less than the full amount of the sum stated as due in the written demand, plus the additional \$75.00, unless otherwise stated, for the demand letter fee.

(f) The Escrow Agent is entitled to charge its standard fees current as of the date the service is rendered, but all changes shall become effective only after sixty (60) days written notice to the party or parties paying the fee of the Escrow Agent.

(g) Seller and Purchaser will each indemnify and save harmless the Escrow Agent against all costs, damages, attorney's fees, expenses and liabilities which it may incur or sustain in connection with this Contract, including any interpleader or declaratory judgment action brought by Escrow Agent, but excepting failure of the Escrow Agent to comply with this Paragraph 9

(h) The Escrow Agent shall have the right to resign as Escrow Agent under this Contract by giving the Parties sixty (60) days written notice of intent to resign. The Parties shall thereupon mutually select a successor Escrow Agent and give written notice to the Escrow Agent of such selection. If the Parties fail, for any reason, to mutually select a successor Escrow Agent and give Escrow Agent written notice of such selection within sixty (60) days after mailing by the Escrow Agent of notice of intent to resign as aforesaid, then the Escrow Agent may select the successor Escrow Agent. Delivery by the Escrow Agent to the successor Escrow Agent of all documents and funds, after deducting therefrom its charges and expenses, shall relieve the Escrow Agent of all liability and responsibility for acts occurring after the date of the assignment in connection with this Contract.

10. SEVERABILITY CLAUSE: The invalidity or unenforceability of any provision of this Contract shall not affect the validity or enforceability of the remainder of this Contract.

The Parties have signed and acknowledged this Contract effective as of the date stated at the beginning of this Contract

CAUTION: YOU SHOULD READ THIS ENTIRE CONTRACT BEFORE SIGNING. IF YOU DO NOT UNDERSTAND THIS CONTRACT, YOU SHOULD CONSULT YOUR ATTORNEY.

SELLER

PURCHASER

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF

} ss.

This instrument was acknowledged before me this day of , 1998, by and .

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF

} ss.

This instrument was acknowledged before me this day of , 1998, by and .

My commission expires:
(Seal)

Notary Public

Real Estate Contract

THIS CONTRACT IS MADE on _____ day of _____, 19____ (the "Effective date"), by
(the "Seller"), and _____, whose address is _____
(the "Buyer"), who is purchasing as (CIRCLE ONE) INDIVIDUAL / TENANTS IN COMMON / JOINT TENANTS / COMMUNITY
PROPERTY / OTHER _____
Seller and Buyer agree

1. SALE: Seller sells to Buyer the following described real estate (the "Property"), in the County of _____ and State of New Mexico,
Address _____
Legal Description _____

Subject to reservations, restrictions, and easements of record, taxes and assessments and the "Prior Obligations" (the
"Permitted Exceptions").

2. PRICE AND PAYMENT:

A. BUYER WILL PAY:

CONTRACT SALES PRICE

\$ _____
(Total of Down Payment, Assumed Prior Obligations and Balance Due Seller)
(_____ Dollars)

(1) DOWN PAYMENT \$ _____
(_____ Dollars)

(2) ASSUMED PRIOR OBLIGATION \$ _____
(_____ Dollars)

(3) BALANCE DUE SELLER (including wrapped Prior Obligations) \$ _____
(_____ Dollars)

PAYABLE AS FOLLOWS:

This form does not contain disclosures required by Federal Reserve Regulation Z and Consumer Act "Truth in Lending." Use this form only in conjunction with another instrument incorporating the required disclosures or for transactions exempt from the ACT.

B. INTEREST ON BALANCE DUE SELLER. Except as specifically stated to the contrary in Paragraph 2A, the Balance Due Seller will bear interest at the rate of _____ % per year (the "Interest Rate") from the effective date, and the payments will be paid to Escrow Agent (named below) and continue until the entire Balance Due Seller plus any accrued interest due to Seller is fully paid.

C. LATE CHARGES AND COLLECTION COSTS. Buyer will pay all late charges and all collection costs incurred on all Prior Obligations paid directly by Buyer or through Escrow Agent. A late charge of \$ _____ will be due and payable by Buyer on any payment that is over _____ days overdue. Late charges will be paid to Seller as additional interest.

D. APPLICATION OF PAYMENTS ON BALANCE DUE SELLER.

(1) Initial only one of the following two paragraphs.

☐ **PERIODIC INTEREST.** Payments received by Escrow Agent, excepting prepayments, will be applied to regularly scheduled installments in the order in which payments are due and will be credited as though the payments had been made on their respective due dates, first to interest and then to the Balance Due Seller.

☐ **DAILY INTEREST.** Payments will be applied as of the date of receipt by Escrow Agent first to accrued interest then to the Balance Due Seller.

(2) All payments will be assumed to be regular payments, and not prepayments, unless otherwise specified by Buyer in writing at the time of delivering such payments to Escrow Agent. Buyer may prepay all or any part of the Balance Due Seller, without penalty. Any prepayment will be credited first to accrued interest, then to the Balance Due Seller, and then to Prior Obligations assumed by Buyer. Notwithstanding any prepayments, Buyer will make the next regularly scheduled payments.

3. PRIOR OBLIGATIONS.

A. Each of the following Prior Obligations is currently outstanding on the Property:

Type of Lien or Obligation	Holder	Loan Number	Recording Data:	Book & Page
1.				
2.				
3.				

B. IF ANY PRIOR OBLIGATIONS ARE CURRENTLY OUTSTANDING ON THE PROPERTY, INITIAL ANY OF THE FOLLOWING PARAGRAPHS WHICH APPLY. ONLY THE INITIALED PARAGRAPHS WILL APPLY. Seller and Buyer appoint Escrow Agent as their Attorney-in-Fact for the limited purpose of obtaining account information as needed from the holders of the Prior Obligations.

(1) ASSUMED PRIOR OBLIGATIONS.

☐ **(a) PAID THROUGH ESCROW.** Buyer assumes and agrees to pay and perform the Prior Obligations in accordance with their terms. Buyer will make the required payments on the Prior Obligations, together with the required payments on this contract, to the Escrow Agent, which will remit the payments to the proper payee. Buyer will advise Escrow Agent of any changes in the amount of the payment due on any Prior Obligations. When the Balance Due Seller is fully paid, this Escrow will terminate and Buyer will make the required payments on the Prior Obligations directly to the proper payee. This Paragraph applies to the following Prior Obligations:

☐ **(b) PAID DIRECTLY BY BUYER.** Buyer assumes and agrees to pay and perform the Prior Obligations in accordance with their terms. Buyer will make the required payments on the Prior Obligations directly to the proper payee. If the Buyer fails to pay the required payments before they become delinquent, Seller may pay the payment. Payment by the Seller will not be deemed a waiver of Buyer's default, and the amount paid by Seller will be immediately due and payable to Seller and will bear interest from date of payment by Seller until paid at the highest Interest Rate in Paragraph 2B. This Paragraph applies to the following Prior Obligations:

(2) WRAPPED PRIOR OBLIGATIONS.

☐ **(a) PAID THROUGH ESCROW.** Buyer does not assume or agree to pay the Prior Obligations. All required payments due on the Prior Obligations will be remitted by the Escrow Agent to the proper payee out of the payments on the Balance Due Seller. If Buyer fails to pay the required payments before they become delinquent, Seller may make the payment. Payment by seller will not be deemed a waiver of Buyer's default, and the amount paid by Seller will be immediately due and payable to Seller and will bear interest from date of payment by Seller until paid at the highest Interest Rate in Paragraph 2B. Upon payment of the Balance Due Seller, Seller will obtain a release of the Property from the lien of the wrapped Prior Obligations. This Paragraph applies to the following Prior Obligations:

☐ **(b) PAID DIRECTLY BY SELLER.** Buyer does not assume and does not agree to pay the Prior Obligations. Seller will be responsible for all payments required by the Prior Obligations and will keep the Prior Obligations in good standing. Upon payment of the Balance Due Seller, Seller will obtain a release of the Property from the lien of the wrapped Prior Obligations. This Paragraph applies to the following Prior Obligations:

4. BUYER TO MAINTAIN PROPERTY, PAY INSURANCE, TAXES AND PAVING LIENS; SELLER'S RIGHTS.

A. MAINTENANCE. Buyer will maintain the Property in as good condition as on the Effective Date, excepting normal wear and tear and casualty losses insured pursuant to this contract.

B. INSURANCE. Buyer will keep the insurable improvements upon the Property insured against the hazards covered by fire and extended and comprehensive public liability insurance, with an insurance company satisfactory to Seller in the amount of:

- (1) not less than the greater of the replacement cost of the improvements or the Balance Due Seller, for the benefit of Buyer and Seller as their interests may appear, as to fire and extended coverage; and
- (2) not less than \$ _____ as to comprehensive liability with Seller as additional named insured,

and Buyer will furnish a copy of the insurance policy to Seller annually before expiration of existing insurance stating that coverage will not be cancelled or diminished without a minimum of 15 days prior written notice to Seller.

C. TAXES. The property taxes for the current year have been divided and prorated between Seller and Buyer as of the effective date, and Buyer is responsible for and will pay the taxes and assessments of every kind against the Property. Buyer will have the property assessed for taxation in Buyer's name. Unless taxes are paid through an escrow account, Buyer will send copies of paid tax receipts to Seller within 30 days after taxes are due.

D. PAVING, UTILITY AND OTHER IMPROVEMENT LIENS AND CHARGES. Subject to proration, Buyer assumes any paving utility or other improvement liens or charges now assessed against the Property and will pay all installments of principal and interest thereon that become due after the Effective Date.

E. SELLER'S RIGHTS. If Buyer fails to pay any amounts required to be paid by Paragraphs 4B, C and D before the amounts become delinquent, Seller may pay the amounts (but is not obligated to do so) for protection of the Property and Seller's interest in the Property. Payment of the amounts will not be deemed a waiver of the Buyer's default for failure to pay the amounts, and the amounts that have been paid will be immediately due and payable to Seller, and will bear interest until paid at the highest Interest Rate provided in Paragraph 2B.

5. BUYER'S RIGHT TO POSSESSION. Buyer will be entitled to take and retain possession of the Property unless and until Buyer's rights in the Property are terminated by Seller as provided in Paragraph 8.

6. BUYER'S RIGHT TO SELL, ASSIGN, CONVEY, OR ENCUMBER. A sale, assignment, conveyance or encumbrance of all or any portion of Buyer's interest in this Contract or the Property to any person or entity (an Assignee") constitutes a Transfer under this Contract.

A. SALE WITHOUT CONSENT OF SELLER. A Transfer to an Assignee will not require the consent of Seller. Buyer will not, however, be released from Buyer's obligations under this Contract by any Transfer under this Paragraph. Buyer will deliver a copy of the written evidence of the transfer (the "Transfer Document") to Escrow Agent.

B. NO SALE WITHOUT CONSENT OF SELLER.

CAUTION: THE FOLLOWING PARAGRAPH SEVERELY RESTRICTS THE RIGHT OF BUYER TO TRANSFER THIS CONTRACT AND THE PROPERTY. To invoke this Paragraph, initial where indicated. If this Paragraph is initialed, paragraph 6A does not apply.

☐ Initials

A transfer without payment of the Balance Due Seller will require obtaining the prior written consent of Seller, which Seller will not unreasonably withhold. A Transfer without payment of the Balance Due Seller, and without the prior written consent of Seller, will be an event of default for which Seller will have the right to send a Default Notice pursuant to paragraph 8 and to demand payment of the Balance Due Seller.

Caution: If the Property is subject to any prior mortgages, deeds of trust or real estate contracts, their provisions should be examined carefully for any conflict with Paragraph 6.

7. TITLE INSURANCE OR ABSTRACT. Seller is delivering a Contract Purchaser's Title Insurance Policy to Buyer or Abstract of Title to Escrow Agent at the time this Contract is escrowed, showing merchantable or marketable title to the Property as of the Effective Date, subject to the Permitted Exceptions, and Seller is not obligated to provide other evidence of title.

8. SELLER'S RIGHTS IF BUYER DEFAULTS.

A. DEFAULT NOTICE. Time is of the essence in this Contract. If Buyer fails to pay or perform any obligation of Buyer under this Contract, the failure will constitute a default and Seller may give notice of default to Buyer specifying the default and the curative action required (the "Default Notice"), at Buyer's mailing address as follows:
or at such other address that Buyer may designate by a written signed statement delivered to Escrow Agent. If Seller's attorney sends a Default Notice, Buyer will pay within the time allowed the additional sum of \$100.00, plus gross receipts tax and postage, for Seller's attorney's fees and costs in connection with sending of the Default Notice.

B. MANNER OF GIVING DEFAULT NOTICE. Default Notice will be given by certified mail, return receipt requested, and regular first class mail, addressed to Buyer at the address for Buyer provided in Paragraph 6A, with a copy to Escrow Agent. Default Notice given as provided in Paragraph 6A is sufficient for all purposes, whether or not the Default Notice is actually received.

C. BUYER'S FAILURE TO CURE DEFAULT RESULTS IN TERMINATION OF BUYER'S EQUITABLE RIGHTS IN THE PROPERTY OR ACCELERATION OF BALANCE DUE SELLER

(1) If Buyer fails or neglects to cure any default within thirty (30) days after the date Seller's Default Notice is mailed, then Seller may, at Seller's option, either

(a) declare the Balance Due Seller to be then due and proceed to enforce payment of the Balance Due Seller, plus any accrued interest, reasonable attorney's fees, postage and costs; or

(b) terminate Buyer's rights in the Property and retain all sums paid as liquidated damages to that date for the use of the property, and all rights of Buyer in the Property will end. If the final day for curing the default falls on a non-business day of Escrow Agent, then the period for curing the default shall extend to the close of business on the next business day of the Escrow Agent. If the Contract is terminated by Seller, Buyer will forfeit all payments made pursuant to this Contract. Buyer waives any claim to the payments if a default occurs and Seller elects to terminate Buyer's rights in the Property. If Buyer's rights in the Property are terminated, Buyer waives any and all rights and claims for reimbursement for improvements Buyer may have made to the Property.

(2) Acceptance by Escrow Agent of any payment tendered shall not be deemed a waiver by Seller of Buyer's default or extension of the time for cure of any default under this Contract.

D. AFFIDAVIT OF UNCURED DEFAULT AND ELECTION OF TERMINATION. A recordable affidavit (the "Default Affidavit") made by Seller, Seller's agent, or Escrow Agent, identifying the parties, stating the legal description of the Property or the recording data of this Contract, stating the date that Default Notice was given, stating that the specified default has not been cured within the time allowed and that the Seller has elected to terminate Buyer's rights in the Property, and delivered to Escrow Agent, will be conclusive proof of the uncured default and election of termination of Buyer's rights in the Property.

E. BUYER BECOMES TENANT. Upon termination of Buyer's rights in the Property, Buyer has no continuing right to possession. If Buyer remains in possession of the Property after Buyer's rights in the Property have been terminated, Buyer will then become a tenant at will, for a rental amount equivalent to the regularly scheduled installment payment due and payable under this Contract, with the first such rental payment due immediately, in advance, and such tenancy being subject to termination by either party upon thirty (30) days separate prior written notice. Seller's acceptance of such rental payment will not be deemed a waiver of any of Seller's rights, nor will it constitute any manner of estoppel against Seller.

F. LEGAL RIGHT TO EVICT BUYER. A Forcible entry and detainer action, in addition to any other appropriate legal remedies, may be used by the Seller if necessary to obtain possession of the Property following termination of Buyer's rights in the property and to terminate Buyer's continued possession.

G. NOTICE TO ASSIGNEES. In addition to sending a Default Notice to Buyer, Seller will send all Default Notices to all Assignees who have given written notice of their name, address, and interest in the Property and who have provided a copy of the Transfer Document to Escrow Agent.

H. RIGHTS AND OBLIGATIONS SURVIVING TERMINATION. Upon termination of Buyer's rights in the Property, Buyer will provide an accounting to Seller of any rents and deposits received by Buyer from the Property, which obligation will survive termination. Notwithstanding the termination of Buyer's rights to the Property, Buyer will be liable to Seller for any waste to the Property as well as for any unpaid taxes or utilities liens which survive the termination of Buyer's rights, prepaid rent, and rental deposits.

9. BINDING EFFECT. This Contract will bind and benefit the heirs, devisees, personal representatives, successors and assigns of Seller and Buyer.

10. APPOINTMENT OF AND INSTRUCTIONS TO ESCROW AGENT.

A. ESCROW AGENT.

Seller and Buyer appoint as Escrow Agent:

**Security Escrow Corporation
1721 Girard NE
Albuquerque, NM 87106**

B. ESCROW DOCUMENTS. The following papers (the "Escrowed Documents") are placed in escrow:

- (1) Signed copy of this Contract.
- (2) Original Warranty Deed signed by Seller.
- (3) Original Special Warranty Deed signed by Purchaser.
- (4)
- (5)

C. PRIOR OBLIGATIONS. Add the following information, if applicable:

- (1) Name and address of mortgagees/escrow agents/servicing agents:

Account or Loan No.

- (2) Name and address of mortgagees/escrow agents/servicing agents:

Account or Loan No.

D. FEES.

- (1) The Escrow Agent will be paid as follows:

If any part of the fees are paid by Buyer, that amount will be in addition to the amounts due from Buyer as Provided in Paragraph 2.

- (2) Escrow Agent will accept all amounts paid in accordance with this Contract and remit the amounts received (less applicable escrow fees) as follows:

E. ACCEPTANCE OF PAYMENTS. All payments shall be deemed provisionally accepted when tendered, subject to determination by the Escrow Agent of the correct amount and its timeliness of payment. After each Default notice is mailed to Buyer and any Assignee, pursuant to Paragraph 8, and a copy is furnished to Escrow Agent, Escrow Agent will not accept less than the full amount of the sum stated as due in the Default Notice.

F. RELEASE AND DELIVERY OF ESCROWED DOCUMENTS. Upon full payment of the Balance Due Seller and full performance under this Contract by Buyer, other than payment of the assumed Prior Obligations, Escrow Agent is directed to release and deliver the Escrowed Documents to Buyer.

G. DEFAULT BY BUYER. If the Seller or Seller's agent delivers a Default Affidavit to Escrow Agent, then the Escrow Agent will release and deliver the Escrowed Documents to the Seller. The Escrow Agent shall be entitled to rely on such Default Affidavit as conclusive proof of termination.

H. CHANGES IN ESCROW FEES. Escrow Agent may charge its standard fees current as of the date the service is rendered, but all changes will become effective only after sixty (60) days written notice to the party or parties paying the fee of the Escrow Agent.

I. INDEMNIFICATION. Seller and Purchaser and any Assignee will each indemnify and save harmless the Escrow Agent against all costs, damages, attorney's fees, expenses and liabilities which Escrow Agent may incur or sustain in connection with this Contract, including any interpleader or declaratory judgment action brought by Escrow Agent, but not for the failure of Escrow Agent to comply with this Paragraph 10 or the negligence or intentional act of Escrow Agent.

J. RESIGNATION BY ESCROW AGENT. Escrow Agent may resign as Escrow Agent by giving Seller and Buyer sixty (60) days written notice of intent to resign. Seller and Buyer will select a successor Escrow Agent and give written notice to the Escrow Agent of such selection. If the Parties fail, for any reason, to select a successor escrow agent and give Escrow Agent written notice of the selection within sixty (60) days after mailing by the Escrow Agent of notice of intent to resign, then Escrow Agent may select the successor escrow agent.

11. SEVERABILITY CLAUSE. The invalidity or unenforceability of any provision of this Contract will not affect the validity or enforceability of the remainder of this Contract.

12. ATTORNEY FEES. If either party uses the services of an attorney to enforce that party's rights or the other party's obligations under this Contract, the prevailing party will recover reasonable attorney's fees and costs from the non-prevailing party.

CAUTION: PLEASE READ THIS ENTIRE CONTRACT BEFORE SIGNING. IF YOU DO NOT UNDERSTAND THIS CONTRACT, YOU SHOULD CONSULT YOUR ATTORNEY.

SELLER

BUYER

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF

} ss.

This instrument was acknowledged before me this ____ day of _____, 19____, by _____.

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF

} ss.

This instrument was acknowledged before me this ____ day of _____, 19____, by _____.

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR ENTITIES

STATE OF NEW MEXICO

COUNTY OF

} ss.

This instrument was acknowledged before me this ____ day of _____, 19____, by _____.

My commission expires:
(Seal)

Notary Public

**REAL ESTATE CONTRACT
PURCHASE AGREEMENT ADDENDUM**

The following agreement is an addendum to, and a part of, the Purchase Agreement (Deposit Receipt and Agreement) dated 19____ between the

SELLER(S):

and PURCHASER(S):

for the property located at (address)

Legal Description:

It is mutually understood and agreed that the following terms and conditions shall be made a part of the above described Purchase Agreement (Deposit Receipt and Agreement):

Amount of contract: \$ _____ Interest Rate. _____ % per annum.

Interest to accrue from 19____.

Regular monthly principal and interest payments to be in the amount of \$ _____ or more.
The contract balance may be pre-paid in full or in part at any time without penalty. However, partial pre-payment will not alter the amount or the sequence of any subsequent payment called for under the contract.

A late charge of \$ _____ will be due and payable by the purchaser on any payment that is over _____ days past due. Late charges collected on the contract balance will be paid to the seller as additional interest. The purchaser will pay all late charges due on any underlying obligations assumed by the purchaser.

First payment due 19____ with subsequent payments due on the _____ day of each month thereafter until paid in full.

Other payments or terms to be as follows

The Real Estate Contract shall have a _____ day clause to cure default.

Fire and extended coverage insurance to be not less than \$ _____

Escrow Agent shall be:

Escrow Fees to be paid by:	Set Up Fee	Purchaser_____	Seller_____
	Disbursement Fee	Purchaser_____	Seller_____
	Close-out Fee	Purchaser_____	Seller_____

Escrow Agent to contact Purchaser, as required, at the following address:

IF A RANM 11 REAL ESTATE CONTRACT IS BEING USED, COMPLETE THE FOLLOWING.

APPLICATION OF PAYMENTS: Check and initial only one of the following two paragraphs.

☐ (a) Payments, excepting prepayments, shall be applied to regularly scheduled installments in the order in which the same were due and shall be credited as though the payments were made on their respective due dates

☐ (b) Payments shall be applied as of the date of receipt by Escrow Agent first to accrued interest then to principal balance of this Contract

IF ANY LIEN(S) OR OBLIGATION(S) IS/ARE CURRENTLY OUTSTANDING ON THE PROPERTY, CHECK AND INITIAL ONLY ONE OF THE FOLLOWING THREE PARAGRAPHS. ONLY THAT PARAGRAPH SHALL APPLY.

☐ (a) Purchaser assumes and agrees to pay the above-mentioned prior lien(s) or obligation(s) in accordance with its/their terms. Purchaser shall make the installment payments on the prior lien(s) or obligation(s), together with installment payments on this Contract, to the Escrow Agent named below, who will remit the payments to the person or company to whom they are payable. Purchaser shall advise the Escrow Agent of any change in the amount of the payment due on any assumed obligation(s). Failure to make such payments at the time required shall be a default under this Contract. At such time as the unpaid balance of the purchase price due the seller is fully paid, this Escrow shall terminate and the purchaser shall thereafter make the installment payments on said prior lien(s) or obligation(s) directly to the person(s) or company(ies) to whom they are payable.

☐ (b) Purchaser assumes and agrees to pay the above-mentioned prior lien(s) or obligation(s) in accordance with its/their terms. Purchaser shall make the installment payments on the prior lien(s) or obligation(s) directly to the person or company to whom payable. Failure to make such payments at the time required shall be a default under this Contract.

☐ (c) Purchaser does not assume or agree to pay the above-described lien(s) or obligation(s). All payments due on such lien(s) or obligation(s) shall be remitted by the Escrow Agent to the person or company to whom they are payable out of the payments made by Purchaser. If the payments due from Purchaser are insufficient to satisfy the amounts due to be made on the above-described lien(s) or obligation(s), Seller shall pay Escrow Agent such additional funds as are necessary to keep such lien(s) or obligation(s) current.

PURCHASER'S RIGHT TO SELL:

(A) First Provision.

Purchaser shall be entitled to sell, assign, convey or encumber his entire interest in this Contract (but not a portion thereof) and the Property to any person or entity, hereinafter called Assignee, and may retain a security interest therein, without obtaining the consent or approval of the Seller. The Purchaser shall not, however, be released from his obligations hereunder by any such sale, assignment, conveyance or encumbrance. In the event Purchaser does sell, assign, convey or encumber said interest, then Purchaser, his Assignee, or any subsequent Assignee shall deliver a copy of such written sale, assignment, conveyance or encumbrance document to Escrow Agent.

Such sale, assignment, conveyance or encumbrance document shall specify the address of the Assignee and upon receipt of such document by the Escrow Agent, Seller shall only be required to send notice of default to the most recent Assignee who has given notice of such sale or assignment and his address to the Escrow Agent as provided herein. If such document is not received by the Escrow Agent, any notice of default need be sent only to the last person or entity and address for which written notice has been provided to the Escrow Agent as provided herein.

(B) Special Alternative Provision

CAUTION. THE FOLLOWING PROVISION SEVERELY RESTRICTS THE RIGHT OF PURCHASER TO SELL, ASSIGN, CONVEY OR ENCUMBER THIS CONTRACT AND THE PROPERTY. If the parties wish to invoke this provision, they should check the box as indicated and each initial as provided. If the Special Alternative Provision is elected, the First Provision does not apply.

☐ Initial Purchaser shall not be entitled, directly or indirectly, to sell, assign, convey or encumber all or any portion of the Purchaser's interest in this Contract or in the Property without first obtaining the written consent of Seller, and Seller shall not be under any obligation of any kind to give such consent. In the event that Purchaser shall, directly or indirectly, sell, assign, convey or encumber or contract to sell, assign, convey or encumber, directly or indirectly, or indirectly, all or any portion of the Purchaser's interest in this Contract or in the Property without the consent of Seller, it shall be an event of default subject to the rights of Seller in Paragraph 5 of RANM Form 11 Real Estate Contract.

PURCHASER

PURCHASER

DATE

TIME

SELLER

SELLER

DATE

TIME

REVERSE ASSIGNMENT OF TRUST FUNDS

I hereby agree that all payments heretofore or hereafter received by
Mortgagee in connection with the Mortgage dated to
as Document Number , Recorded on
insurance, or for any other purpose, are assigned to , for the payment of taxes, assessments,
husband and wife.

WITNESS my hand this day of , 1998

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO }

ss.

COUNTY OF

This instrument was acknowledged before me on this day of , 1998 by
and

My commission expires:
(Seal)

Notary Public

ASSIGNMENT OF SELLER'S INTEREST IN A REAL ESTATE CONTRACT

That I/we _____, for valuable consideration, receipt of
which is hereby acknowledged, do assign to _____ whose address is
all my right, title and interest in and to that certain
real estate contract dated the _____ of _____, 1998 by and between
_____, as Purchaser and _____,
as Seller.

Legal Description

I/We represent that the unpaid balance of said contract is _____ and that the next payment is
due _____ Said contract is escrowed at _____,
Account No. _____.

WITNESS my hand and seal this _____ day of _____, 1998.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO } ss.
COUNTY OF _____

This instrument was acknowledged before me on this _____ day of _____, 1998, by
and _____.

My commission expires: _____
(Seal) _____ Notary Public

Assignee's Acceptance

The undersigned Assignee(s) named in the foregoing assignment of the real estate contract therein described
hereby approve(s) and accept(s) the same and agree(s) to be bound by all the terms, covenants, and conditions of
said contract. Receipt of a copy of said contract is hereby acknowledged.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO } ss.
COUNTY OF _____

This instrument was acknowledged before me on this _____ day of _____, 1998, by
and _____.

My commission expires: _____
(Seal) _____ Notary Public

**ASSIGNMENT OF SELLER'S INTEREST IN A REAL ESTATE CONTRACT
AND CONVEYANCE OF TITLE**

That I/we _____, for valuable consideration, receipt of
which is hereby acknowledged, do assign to _____ whose address is
all my right, title and interest in and to that certain
real estate contract dated the _____ of _____, 1998 by and between
_____, as Purchaser and _____,
as Seller.

I/We hereby grant and convey to said Assignee(s), as **joint tenants** with special warranty covenants, the real
property which is the subject of said contract, said property being located in _____ County in the State
of New Mexico, and described as follows, to wit:

Legal Description

I/We represent that the unpaid balance of said contract is _____ and that the next payment is
due _____ Said contract is escrowed at _____,
Account No. _____.

WITNESS my hand and seal this _____ day of _____, 1998.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO }
COUNTY OF _____ ss.

This instrument was acknowledged before me on this _____ day of _____, 1998, by
_____ and _____.

My commission expires:
(Seal)

Notary Public

Assignee's Acceptance

The undersigned Assignee(s) named in the foregoing assignment of the real estate contract therein described
hereby approve(s) and accept(s) the same and agree(s) to be bound by all the terms, covenants, and conditions of
said contract. Receipt of a copy of said contract is hereby acknowledged.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO }
COUNTY OF _____ ss.

This instrument was acknowledged before me on this _____ day of _____, 1998, by
_____ and _____.

My commission expires:
(Seal)

Notary Public

ASSIGNMENT OF FRACTIONAL INTEREST AGREEMENT

Date:

PARTIES:

Seller:

Address:

Buyer:

Address:

1. DESCRIPTION:

Seller is the owner and holder of the secured obligation described as follows:

a. Security

b. Dated:

Lien Position:

c. Recording No

Vol.

Page

County:

State:

2. DEFINITIONS:

As used herein, these terms have the following meanings:

(A) **ADDITIONAL EXPENSES:** Any and all of the expenses incurred by Buyer in connection with this Assignment, including without limitation, advances on superior liens and encumbrances, costs, disbursements, title and appraisal fees, attorney fees, taxes and insurance premiums, repairs, maintenance expenses, and real estate commissions together with interest thereon at the rate as specified in the Security Instrument from the date said expenses was incurred.

(B) **MAKER or PAYOR:** The person(s) originally obligated to pay the Note and Security Instrument or the Buyer under a Real Estate Contract, together with any and all persons paying, assuming and/or guaranteeing that obligation with the exception of the Seller as named herein.

(C) **PAYEE:** The person(s) originally entitled to receive payments under the Note and Security Instrument or the original Seller under a Real Estate Contract, together with any and all successors and assigns thereof.

(D) **SECURITY INSTRUMENT:** The Promissory Note and Trust Deed, Promissory Note and Mortgage, Real Estate Contract, or other evidence of indebtedness described above, together with all instruments, agreements and documents which secure such indebtedness.

(E) **DEFAULT:** Failure of the Maker/Payor to perform pursuant to the terms and conditions of the Security Instrument.

(F) **AMOUNT PURCHASED:** The right to receive the net sum of \$ _____ together with interest at the rate set forth in the Security Instrument described above.

(G) **NET SUM (NET PROCEEDS):** The amount received by Buyer and retained by Buyer.

3. ASSIGNMENT:

In consideration of the amount of \$ _____ paid by Buyer, Seller does hereby assign, transfer, set over and convey to the Buyer the following:

(A) The net sum as specified in 2(F) plus any additional expenses as specified in paragraph 2(A) incurred by Buyer subsequent to the execution of this Agreement; and

(B) All of Seller's right, title and interest in and to the above-described Security Instrument together with all of Seller's rights, claims and causes of action which Seller has or may have against the Maker and/or Payor of the Security Instrument and all of Seller's right, title and interest in and to the real property which is described in the Security Instrument to be reassigned as provided for herein.

Seller shall deliver to Buyer any and all promissory notes which are subject to this agreement and endorse the same without recourse to the order of Buyer. Seller shall execute any and all documents requested of Seller by Buyer to evidence this agreement including, but not limited to, a recordable short form of the assignment of the Security Instrument

4. DISBURSEMENT OF PROCEEDS:

Only after the Buyer has received the amount purchased and any other additional expenses which Buyer is entitled to receive together with any additional funds to which Buyer may be entitled to receive pursuant to paragraph 8 shall Seller be entitled to receive the remaining proceeds, if any, due the Payee pursuant to the Security Instrument.

5. PREPAYMENT:

In the event of a total prepayment of the Security Instrument, Buyer shall be entitled to receive the amount purchased and any and all additional expenses to which Buyer is entitled to receive pursuant to this agreement. The remainder, if any, shall be paid to the Seller. Payment amounts to be used for computation shall be the net sum received by Buyer.

6. PARTIAL PAYMENTS:

Escrow agent/Buyer shall accept any partial prepayments and shall deliver such partial prepayments to Buyer, who shall apply them to Buyer's right to payment as specified in paragraphs 2 (A) and 2 (F).

7. NO DEFAULT: SELLER'S OPTION TO REPURCHASE:

Should the Maker/Payor not be in default the Seller may purchase Buyer's interest in the Security Instrument by paying the amount due Buyer pursuant to paragraph 2 (F) together with all other additional expenses to which Buyer is entitled to receive pursuant to the terms of this agreement.

8. DEFAULT: SELLER'S OPTION TO REPURCHASE:

(A) In the event of a default by Maker/Payor under the terms of the Security Instrument for a period of thirty (30) days, Seller, upon written notice of such default, shall have the opportunity to protect its residual interest in the Security Instrument by purchasing Buyer's interest in the Security Instrument within (15) days by paying to Buyer the amount due Buyer pursuant to 2 (F) together with any and all other additional expenses for which Buyer is entitled to be reimbursed. Should the Seller fail to exercise Seller's option to purchase Buyer's interest in the Security Instrument within said fifteen (15) days, Buyer may proceed to foreclose on the Security Instrument, accept a Deed in Lieu of Foreclosure or initiate legal proceedings against the Maker/Payor to collect the amounts owing pursuant to the Security Instrument. Should the Seller wish to purchase the Security Instrument after said fifteen (15) day period and prior to the repossession of the property, Seller may only do so by paying to Buyer the amount due Buyer by catching up delinquent payments and continue to make payments on the original real estate contract, deed of trust, or mortgage pursuant to paragraphs 2 (F) and 2 (A).

(B) **OPTION TO REPURCHASE AFTER REPOSSESSION:** In the event that the Buyer completes a foreclosure or otherwise obtains title to the property described in the Security Instrument Buyer agrees to give Seller written notice that the property has been repossessed. Seller shall have the option to purchase the property from Buyer within sixty (60) days of said notice by paying to buyer delinquent payments current and continuing payments of original real estate contract, deed of trust, or mortgage.

WARNING: IF SELLER FAILS TO EXERCISE SELLER'S OPTION TO PURCHASE THE PROPERTY WITHIN SIXTY (60) DAYS OF THE NOTICE THAT THE PROPERTY HAS BEEN REPOSSESSED SUCH FAILURE SHALL TERMINATE ANY AND ALL OF SELLER'S RIGHTS TO ANY MONEY AND/OR SETTLEMENT WHATSOEVER RELATING TO THE ORIGINAL SECURITY INSTRUMENT, THIS AGREEMENT, THE REPOSSESSION OF THE PROPERTY, A SUBSEQUENT RESALE OF THE PROPERTY BY BUYER AND ANY NEW SECURITY INSTRUMENT WHICH MIGHT SUBSEQUENTLY BE HELD BY BUYER IN CONJUNCTION WITH A RESALE OF THE REAL PROPERTY.

9. TERMINATION OF ASSIGNMENT:

This assignment shall terminate at such time as Buyer has received the amounts due Buyer pursuant to paragraph 2 (F), together with all other additional expenses for which Buyer is entitled to receive pursuant to paragraph 2 (A). Upon such termination, Buyer shall reassign to Seller all Buyer's then remaining right, title and interest in the Security Instrument and shall execute such documents and instruments as may be necessary to effect such reassignment and terminate Buyer's interest as a matter of record. Upon reassignment any and all liability of the Buyer in regard to the Security Instrument or in regard to obligations, if any, owed the Seller shall cease.

NOTWITHSTANDING ANY OTHER TERM OR PROVISION IN THIS AGREEMENT, THE BUYER MAY TERMINATE ANY RESIDUAL INTEREST THAT THE SELLER MAY HAVE IN THE SECURITY INSTRUMENT AT ANY TIME SIXTY (60) DAYS AFTER A DEFAULT HAS OCCURRED ON THE SECURITY INSTRUMENT, BY PAYING TO SELLER THE AMOUNT THEN OWED ON THE SECURITY INSTRUMENT LESS THE UNPAID BALANCE DUE BUYER PURSUANT TO PARAGRAPHS 2 (F) AND 2 (A).

10. ASSIGNMENT OF INSURANCE:

(A) Seller assigns to Buyer all Seller's rights to proceeds of any casualty loss payment or settlement in regard to the Security Instrument.

(B) Said proceeds shall be allocated first to repairs or the replacement of the insured property; secondly to satisfy the balance due Buyer, and the remainder, if any, to the Seller in accordance with the Security Instrument.

11. MERGER:

This Agreement between the parties hereto with relation to the transaction contemplated hereby embody the entire Agreement between the parties and there have been no covenants, agreements, representations, warranties or restrictions between the parties hereto with regard to this transaction other than those set forth herein.

12. NOTICES:

All notices which may be required under this Agreement shall be delivered personally, or mailed, to the last address given, in writing, by one party to the other, and shall be deemed given when deposited in the United States mail, postage prepaid.

13. MISCELLANEOUS:

(A) Seller acknowledges that Seller has had an adequate time to read and understand this Agreement and has done so; and that, there have been no other oral or written representations or agreements made by the Buyer except those set forth herein.

(B) Seller further acknowledges that Buyer is purchasing an interest as defined in this agreement and specifically acknowledges that this is not a loan or loan type transaction. Seller shall indemnify and hold harmless Buyer from any liability, loss, damage or additional expense which buyer may suffer as a result of any claim that this is a loan or loan type transaction.

(C) Seller has been requested by Buyer to seek the advice and counsel of a lawyer of his own choice and at his own expense should Seller have any questions concerning any aspect of this transaction.

(D) This Agreement shall inure to the benefit of and be binding upon the heirs, successors, representatives and assigns of the parties hereto.

- (E) This Agreement shall not be modified except in writing signed by all of the parties hereto.
- (F) In the event any term or provision of this Agreement is found to be unenforceable or unlawful for any reason, the remainder shall be carried into effect as though the unenforceable portion was stricken herefrom.
- (G) This Agreement shall be deemed to be made and performed in the State of New Mexico and shall be governed by and constructed in accordance with the laws of that State.

14. PAYOFF:

The undersigned Buyer understands that this is a partial purchase of this certain security instrument. The purchaser is buying the next ___ payments of this security instrument.

In the event of payoff, the payoff balance will begin at \$. The following is an example of what the approximate payoff amount would be for different periods of time

months: \$
months: \$
months: \$
months: \$
months: \$
months: \$

IN WITNESS THEREOF, this agreement has been executed effective the day and year first above written.

SELLER

BUYER

Charles Bombach & Co. Realtors, Inc., by
R. Charles Bombach, President

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF
COUNTY OF

, 19 97, personally appeared before me,

and acknowledged the foregoing instrument to be voluntary act and deed.

My Commission expires

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF
COUNTY OF

19 , personally appeared before me,

and acknowledged the foregoing instrument to be voluntary act and deed.

My Commission expires

ACKNOWLEDGMENT OF CORPORATION

STATE OF New Mexico
COUNTY OF Bernalillo

, 19 97, personally appeared before me, R. Charles Bombach, who being duly sworn, did say the he/she is the president of Charles Bombach & Co. REALTORS, and at that said instrument was signed on behalf of said corporation by authority of its Board of Directors, and he/she acknowledges said instrument to be its voluntary act and deed.

My Commission expires

***TO BE HELD IN ESCROW FOR PAYOFF
WARRANTY DEED
AND SELLER'S ASSIGNMENT OF REAL ESTATE CONTRACT**

to _____ for consideration paid, grant
whose address is _____
the following described real estate in _____ County, New Mexico (including any interest in said
property which grantor may hereafter acquire):

Subject to:

with warranty covenants.

that certain real estate contract dated the ____ day of ____

between

and

as seller

as purchaser

escrowed at _____

, account no. _____

for the sale and purchase of the above described real property, Grantor hereby assigns, transfers and sets over
unto grantee the seller's interest in said real estate contract. The grantee assumes no obligations on the real
estate contract other than to deliver the deed to the real property placed in escrow under the real estate contract
to purchaser upon payment in full of the real estate contract.

WITNESS _ hand and seal this ____ day of _____ 1998

(Seal)

(Seal)

(Seal)

(Seal)

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF New Mexico

COUNTY OF Bernalillo

The foregoing instrument was acknowledged before me this ____ day of _____ 1998
by _____

My commission expires: _____

Notary Public

(Seal)

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF BERNALILLO

The foregoing instrument was acknowledged before me this ____
day of _____ 19 ____
by _____

(Name of Officer)

of _____

(Title of Officer)

(Name of Corporation Acknowledging)

a _____ corporation, on behalf of said corporation.
(State of Incorporation)

My commission expires: _____

(Seal)

Notary Public

FOR RECORDER'S USE ONLY

**ASSIGNMENT OF PURCHASER'S INTEREST IN A REAL ESTATE CONTRACT
and CONVEYANCE OF TITLE**

That I/we _____ for valuable consideration, receipt of which is
hereby acknowledged, do assign to _____, whose
address is _____ all our right, title and interest in and to that
certain real estate contract dated the _____ day of _____ 199_ by and between
and _____ as _____ purchaser
Number _____, as Seller. recorded _____, 199_ as Document
_____, records of the County Clerk of _____ County.

We hereby grant and convey to said Assignee(s), with special warranty covenants, the real property which is the
subject of said contract, said property being located in _____ County in the State of New
Mexico, and described as follows, to wit:

Legal Description

**Subject to reservations, restrictions, and easements of record and to all liens and obligations described in
said contract.**

We represent that the unpaid balance of said contract is _____ and that the next payment is
due _____ Said contract is escrowed at _____, as Escrow Account
No. _____

WITNESS our hand and seal this _____ day of _____, 199_.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO }
COUNTY OF _____ ss.

This instrument was acknowledged before me on this _____ day of _____, 19____
source not found.8, by _____ and _____

My commission expires: _____
(Seal) _____ Notary Public

Assignee's Acceptance

The undersigned Assignee(s) named in the foregoing assignment of the real estate contract therein described
hereby approve(s) and accept(s) the same and agree(s) to be bound by all the terms, covenants, and conditions of
said contract. Receipt of a copy of said contract is hereby acknowledged.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO }
COUNTY OF _____ ss.

This instrument was acknowledged before me on this _____ day of _____, by _____

My commission expires: _____
(Seal) _____ Notary Public

COLLATERAL ASSIGNMENT OF REAL ESTATE CONTRACT

do hereby grant, set over and assign unto _____ for value received,
security on certain indebtedness evidenced by a _____ as
(a copy of which is on file in the books and records of _____, dated
Western Bank, Albuquerque, New Mexico) all of _____ right, title, interest and
equity (including any proceeds due there from) in and to that certain real estate
contract and all related documents, dated the _____ day of _____, 19____,
entered into by and between _____
as Owner, and _____, as
Purchaser for the purchase and sale of the real property described as follows:

Said real estate contract, together with its associated documents, is presently
escrowed at _____
Albuquerque, NM.
WITNESS _____ hand this _____ day of _____, 19____.

ACKNOWLEDGMENT

STATE OF _____)
COUNTY OF _____) ss

The foregoing instrument was acknowledged before me this _____ day of _____,
19____ by _____

Notary Public

My Commission Expires: _____

RELEASE OF ASSIGNMENT

FOR VALUE RECEIVED, all right, title and interest is hereby relinquished and released.

Signed and sealed on this day of , 19__.

WESTERN BANK

By:

STATE OF NEW MEXICO
COUNTY OF BERNALILLO

The foregoing instrument was acknowledged before me this _____ day of
_____, 19_____ by _____ of _____

My commission expires:

Notary Public

WARRANTY DEED

_____, for consideration paid, grant
to _____
whose address is _____
the following described real estate in _____ County, New Mexico:

with warranty covenants.

WITNESS _____ hand _____ and seal _____ this _____ day of _____, 19_____

(Seal) _____ (Seal)

(Seal) _____ (Seal)

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____

ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal)

Notary Public

FOR RECORDER'S USE ONLY

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF _____

ss.

The foregoing instrument was acknowledged before me this _____
day of _____, 19_____
by _____
(Name of Officer)

(Title of Officer) of _____
(Name of Corporation Acknowledging)

a _____ corporation, on behalf of said corporation.

(State of Incorporation)
My commission expires:
(Seal)

Notary Public

SPECIAL WARRANTY DEED (Joint Tenants)

_____ for consideration paid, grant
to _____
whose address is _____
and _____
whose address is _____
as joint tenants the following described real estate in _____ County, New Mexico:

with special warranty covenants.

WITNESS _____ hand _____ and seal _____ this _____ day of _____, 19_____
_____. (Seal) _____ (Seal)
_____. (Seal) _____ (Seal)

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____
by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal) _____

Notary Public

FOR RECORDER'S USE ONLY

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____
day of _____, 19_____,
by _____
(Name of Officer)

(Title of Officer)

of

(Name of Corporation Acknowledging)

a _____ corporation, on behalf of said corporation.
(State of Incorporation)

My commission expires:
(Seal) _____

Notary Public

QUIT CLAIM DEED

_____, for consideration paid, quitclaim to
_____, the following described real estate in
_____, County, New Mexico:

Legal Description

Subject To Clause

WITNESS our hand and seal this _____ day of _____, 1998.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF _____ }
COUNTY OF _____ } ss.

This instrument was acknowledged before me this _____ day of _____, 1997,
by _____ and _____.

My commission expires:
(Seal)

Notary Public

This Indenture, made this _____ day of _____, 19____,
by and between _____

_____,
hereinafter, whether singular or plural, masculine, feminine, or neuter, designated as "Mortgagor," which
expression shall include mortgagors, jointly and severally, and shall include Mortgagor's heirs, executors,
administrators, assigns, and successors in interest, and _____

_____,
whose address is _____

_____,
hereinafter, whether singular or plural, masculine, feminine, or neuter, designated as "Mortgagee," which
expression shall include Mortgagee's heirs, executors, administrators, assigns, and successors in interest,
WITNESSETH:

WHEREAS, the Mortgagor is indebted to the Mortgagee and as evidence thereof has made, executed, and
delivered to the Mortgagee _____ certain note _____ of even date herewith, described as follows, to-wit:

WHEREAS, the Mortgagor desires to secure the payment of said indebtedness;

NOW, THEREFORE, in consideration of the premises and of the sum of One Dollar (\$1.00) to it in hand
paid, the receipt whereof is hereby acknowledged, the Mortgagor has granted, bargained, sold, and con-
veyed, and does hereby grant, bargain, sell, and convey, unto the Mortgagee forever the following real
estate, situate, lying, and being in the County of _____, State of New Mexico, to-wit:

Together with all and singular the lands, tenements, privileges, water rights, hereditaments and appurtenances thereto belonging or in anywise appertaining, and the reversion and reversions, remainder and remainders, rents, issues, and profits thereof, and all the estate, rights, title, interest, claim, and demand whatsoever of the Mortgagor, either in law or equity, of, in, and to the above bargained premises; TO HAVE AND TO HOLD said premises above bargained and described, together with all and singular the lands, tenements, privileges, water rights, hereditaments and appurtenances thereto belonging or in anywise appertaining, and the reversion and reversions, remainder and remainders, rents, issues, and profits thereof, and all the estate, right, title, interest, claim, and demand whosoever of the Mortgagor, either in law or in equity, of, in, and to the above bargained premises, to the Mortgagee forever as security for the faithful performance of the aforesaid promissory note, and each and all of them if there be more than one, and as security for the faithful performance of each and all of the covenants, agreements, terms, and conditions of this Mortgage.

The Mortgagor hereby covenants and agrees with the Mortgagee as follows:

1. That, at the time of the enrolling and delivery of these presents, the Mortgagor is well seized of the premises above conveyed in fee simple, and has good right, full power, and lawful authority to grant, bargain, sell, convey, and mortgage the same in manner and form aforesaid, and that the same are free and clear from all former and other grants, bargains, sales, liens, taxes, assessments, and encumbrances of whatsoever kind and nature, except

and that the Mortgagor shall and will forever warrant and defend the Mortgagee's quiet and peaceable possession of the same against the lawful claims and demands of all persons, except as in this paragraph stated;

2. That the Mortgagor shall promptly pay and otherwise perform all amounts and obligations, as provided in the obligation secured hereby, or any renewal or extension thereof, and in the manner, form, and at the time or times provided in said obligation or in any renewal or extension thereof; and that the Mortgagor shall promptly pay all such additional sums as may hereafter be advanced to the Mortgagor or expended by the Mortgagee on behalf of the Mortgagor for any purpose whatsoever and evidenced by notes, drafts, open account, or otherwise, together with interest thereon at rates to be fixed at the time of advancing or expending such additional sums; provided, however, that the making of such advances or expenditures shall be optional with the Mortgagee; that this mortgage shall secure the payment and performance of all renewals or extension of the obligation secured hereby and shall secure the payment and performance of all such additional sums as may hereafter be advanced to the Mortgagor or expended by the Mortgagee on behalf of the Mortgagor for any purpose whatsoever and evidenced by notes, drafts, open account, or otherwise together with interest thereon, and for all of which this mortgage shall stand as continuing security until fully paid; that the Mortgagee may apply any payments made on any indebtedness secured hereby, at its option, on any such indebtedness;

3. That the Mortgagor shall perform the conditions of any prior mortgage, encumbrance, condition, or covenant;

4. That the Mortgagor shall pay when due and payable all taxes, charges, and assessments to whomsoever and whenever laid or assessed upon the mortgaged premises or on any interest therein; that the Mortgagor shall pay when due and payable all rent, charges for electrical, gas, sewage, water, and all other utility and other charges, fines, or impositions, and all laborers', mechanics', or materialmen's or other liens of whatsoever kind that may be laid or assessed upon the mortgaged premises or on any interest therein;

5. That the Mortgagor shall, during the continuance of any of the indebtedness secured hereby, keep all buildings and other destructible improvements now existing or hereafter erected on the mortgaged premises in good order, condition, and repair at Mortgagor's own expense and shall not commit or suffer any strip or waste of the mortgaged premises;

6. That the Mortgagor shall keep the buildings and all other destructible improvements now existing or hereafter erected on the mortgaged premises insured in the sum specified by the Mortgagee from time to time but in no event less than the total amount of the indebtedness secured hereby and against the hazards of fire and those covered by extended coverage insurance and against such additional hazards as the Mortgagee may from time to time specify, for the benefit of the Mortgagee, its executors, administrators, successors, and assigns, such insurance to be in such form and in such insurance companies as the Mortgagee shall approve; that the Mortgagor shall pay when due and payable all premiums for such insurance, shall deliver such policy or policies of insurance to the Mortgagee, and shall deliver to the Mortgagee at least two days prior to the expiration of any policy on such premises a new and sufficient policy to take the place of the one so expiring; that in the event of loss or damage, Mortgagor shall give immediate notice by mail to the Mortgagee, who may make proof of loss or damage, if not made promptly by the Mortgagor; and that each such insurance company concerned is hereby authorized and directed to make payment for such loss or damage directly to the Mortgagee alone, and not to the Mortgagor and Mortgagee jointly, and the insurance proceeds, or any part thereof, may be applied by the Mortgagee at its option to the reduction of the indebtedness secured hereby or to the restoration and repair of the property damaged or lost;

7. That in the event of the failure or refusal of the Mortgagor to keep in good order, condition, and repair all buildings and other destructible improvements now existing or hereafter erected on the mortgaged premises at Mortgagor's own expense, as in Paragraph 5 above provided; or to keep the premises insured or to deliver the policies of insurance, as in Paragraph 6 above provided; or to pay all taxes, charges, and assessments, and all rent, charges for electrical, gas, sewage, water and all other utility and other charges, fines, or impositions, and all laborers', mechanics', or materialmen's or other liens of whatsoever kind that may be laid or assessed upon the mortgaged premises, as in Paragraph 4 above provided; or to perform the conditions of any prior mortgage, encumbrance, condition, or covenant, as in Paragraph 3 above provided, the Mortgagee, and its executors, administrators, successors, or assigns may, at its option, make, do, perform, and/or pay all such things, and all moneys thus paid and/or all such expenses and costs thus incurred shall bear interest at the rate of ten per centum (10%) per annum and shall be payable by the Mortgagor on demand and shall be so much additional indebtedness secured by this mortgage;

8. That the Mortgagee shall have the right at any time by it deemed necessary to incur the expense of procuring and/or continuing an abstract of title to the said mortgaged premises, or other showing of title, and any expense so incurred shall bear interest at the rate of ten per centum (10%) per annum and shall be payable by the Mortgagor on demand and shall be so much additional indebtedness secured by this mortgage;

9. That, if there is any default in or breach of any covenant, term, condition, or agreement of this mortgage or of any indebtedness secured hereby, all indebtedness secured by this mortgage, whether the same shall be due and payable according to the tenor and effect thereof or not, and anything herein to the contrary notwithstanding, shall, at the option of the Mortgagee, immediately become due and payable without notice to the Mortgagor of the exercise of such option. Upon the happening of such event, this mortgage shall be subject to foreclosure at the option of the Mortgagee, and the premises may be sold in the manner and form prescribed by law; that, in the event of any sale hereunder, the Mortgagee may become the purchaser of the mortgaged premises or any part thereof and shall be entitled to a credit on the purchase price in the amount of its interest in the proceeds of such sale.

10. That, if there is any default in or breach of any covenant, term, condition, or agreement of this mortgage or of any indebtedness secured hereby, the Mortgagee shall have the right, and it is hereby so authorized, to take possession of the mortgaged premises and collect and receive the rents, issues, and profits thereof, and the Mortgagee shall have the right to apply the residue of the same, after deducting all charges and expenses of collection, to the payment of all sums due hereunder or due upon any indebtedness secured hereby; that, whenever any application to any court or referee shall be made to compel the payment of any indebtedness secured hereby or to foreclose this mortgage, the Mortgagee shall have the right and is hereby entitled to the immediate appointment of a receiver, without notice to the Mortgagor, to take possession of the mortgaged premises and to collect and receive the rents, issues, and profits thereof and to apply the residue of the same, after deducting all charges and expenses of collection to the payment of all sums due hereunder or due upon any indebtedness secured hereby, under the direction of the court or referee appointing such receiver; and that the right to the appointment of such a receiver shall not be dependent upon the solvency or insolvency of the Mortgagor or upon the value of the mortgaged premises.

11. That the Mortgagor will pay to the Mortgagee in addition to all of the other indebtedness secured hereby ten percent (10%) of the total amount due hereunder, including all indebtedness secured hereby, as attorney's fees whenever any applications to any court or referee shall be made to compel the payment of any indebtedness secured hereby or to foreclose this mortgage, and the amount of such attorney's fees shall be so much additional indebtedness secured hereby.

12. That no waiver of any obligation hereunder or of the obligation secured hereby shall at any time be held to be a waiver of the terms hereof or of the indebtedness secured hereby. That no sale of the mortgaged premises and no forbearance on the part of the Mortgagee and no extension of time for the payment of the indebtedness secured hereby given by the Mortgagee shall operate to release, discharge, modify, change, or affect in any way the original liability of the Mortgagor.

13. That all of the grants, covenants, terms, conditions, and agreements hereof shall be binding upon and inure to the benefit of all of the heirs, executors, administrators, assigns, and successors in interest of the parties hereto.

IN WITNESS WHEREOF, the Mortgagor has executed this indenture the day and year first above written.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO } ss.
COUNTY OF _____

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,

by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO } ss.
COUNTY OF _____

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,

by _____ of _____
(Name and Title of Officer) (Corporation Acknowledging)

_____, a corporation, on behalf of said corporation.

My commission expires:
(Seal)

Notary Public

\$ 0.00

Albuquerque, New Mexico
Dated this 10th day of February 1998

REAL ESTATE MORTGAGE NOTE

(For individual borrower, Installments include interest.)

After date, as hereinafter set forth, for values received, I we or either of us, promise to pay to the order of Mortgagees' Names at Security Escrow Corporation, 1721 Girard NE, Albuquerque, NM, 87106 \ P.O. Box 25426, Albuquerque, NM 87125 the sum of (\$ 0.00) in monthly installments of \$ 0.00 each, or more, at Maker's option, including interest from date hereof on the unpaid principal balance at the rate of (0.00%)per annum, commencing and on or before the 1st day of each successive month thereafter until paid in full.

The said monthly installments of \$ 0.00 shall include interest on said principal amount and/or on the unpaid balance thereof at the rate of (0.00%)per annum, and when said installments are paid, they shall be apportioned between interest and principal, and applied first to the payment of all interest due at date of payment, and the balance applied on the principal amount.

And I, we, or either of us, agree, in case of default on said installment, when, by the terms hereof, the same shall fall due, that such installment shall bear interest at the rate of ten per cent (10.00%) per annum; and that, if said installment or any interest due thereon is not paid within ten days after the same becomes due and payable, the whole of the principal sum then remaining unpaid, together with the interest that shall have accrued thereon, shall forthwith become due and payable without notice or demand, at the option of the holder of this note.

Every maker, endorser, and guarantor hereof waives presentment, protest, demand, notice of nonpayment, notice of dishonor, notice of protest, and all other demands and notices with respect to this note, and any guaranty of this note, and agrees that any extension or postponement of the time of payment or any other indulgence by the holder of this note, any substitution, exchange, or release of any collateral for this note, and/or the addition or release of any party primarily or secondarily liable hereunder may be made without notice to or the consent of any maker, endorser, or guarantor hereof, and without prejudice to the holder of this note and without releasing any maker, endorser, or guarantor hereof, and that no delay or omission of the enforcement hereof, or of any guaranty hereof, or in the exercise of any right hereunder or under any guaranty hereof shall effect the liability of any maker, endorser, or guarantor of this note.

And I, we, or either of us, agree to pay, in addition to all other sums due hereunder, all costs and expenses of collection of this note and/or enforcing the same including a reasonable attorney's fee which shall not be less than ten per cent (10.00%) of the total amount unpaid hereon at the time of collection and/or enforcement, should this note be placed in the hands of an attorney for collection and/or enforcement, or is collected or enforced through bankruptcy, probate, or other judicial proceedings.

This Note is secured by a Real Estate Mortgage bearing even date herewith.

THIS FORM DOES NOT CONTAIN DISCLOSURES REQUIRED BY SECTIONS 56-8-11.1 THROUGH 56-8-11.4 NMSA 1978, AND/OR DISCLOSURES REQUIRED BY THE TRUTH IN LENDING REFORM AND SIMPLIFICATION ACT AND BY REGULATION Z PROMULGATED THEREUNDER. USE THIS FORM ONLY IN CONJUNCTION WITH A SEPARATE DISCLOSURE STATEMENT OR OTHER SIMILAR INSTRUMENT INCORPORATING THE REQUIRED DISCLOSURES, OR FOR TRANSACTIONS EXEMPT FROM SAID ACTS.

WITNESS our hand and seal this 10th day of February 1998.

Mortgagor1 Name

Mortgagor2 Name

RELEASE OF MORTGAGE

Mortgagees' Names, mortgagee under a certain mortgage executed by **Mortgagors' Names** on the **10th** day of **February 1998**, and recorded in **Book** **Page** **Document** **Number** of the records of **Bernalillo** County, New Mexico, do hereby discharge all of the real estate mentioned in said mortgage from the lien and operation thereof.

legal description

WITNESS our hand and seal this 10th day of February 1998.

Mortgagee1 Name

Mortgagee2 Name

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF **Bernalillo**

}

ss.

This instrument was acknowledged before me this **10th** day of **February 1998**, by **Mortgagee1 Name** and **Mortgagee2 Name**.

My commission expires:
(Seal)

Notary Public

This Indenture made this _____ day of _____, 19____, by and between _____

(hereinafter, whether singular or plural, or masculine, feminine or neuter, called "Mortgagor", and sometimes referred to by the singular neuter pronoun), whose address is _____

and _____

(hereinafter, whether singular or plural, or masculine, feminine or neuter, called "Trustee", and sometimes referred to by the singular neuter pronoun), whose address is _____

WITNESSETH:

WHEREAS, the Mortgagor is indebted to _____ and as evidence thereof has made, executed, and delivered to said _____ certain note _____ of even date herewith, described as follows, to-wit:

payable at _____

with interest at the rate of _____ per cent (_____ %) per annum from date until paid, interest payable

In case of default in the payment of any of said installments, when the same shall fall due, such installments shall bear interest from the date of their respective maturities until paid at the rate of _____ per cent (_____ %) per annum; and if any one of said installments or any interest due thereon is not paid within ten days after the same becomes due and payable, the whole of the principal sum then remaining unpaid, together with the interest that shall have accrued thereon, shall forthwith become due and payable without notice or demand at the option of the holder of the said note _____, with ten percent additional on amount unpaid should the said note _____ be placed in the hands of an attorney for collection.

WHEREAS, the Mortgagor desires to secure the payment of said indebtedness;

NOW, THEREFORE, in consideration of the premises and of the sum of One Dollar (\$1.00) to it in hand paid, the receipt whereof is hereby acknowledged, the Mortgagor has granted, bargained, sold, and conveyed, and does hereby grant, bargain, sell, and convey, unto

the Trustee, and its successors in trust, the following real estate, situate, lying, and being in the County of _____, State of New Mexico, to-wit.

Together with all and singular the hereditaments and appurtenances thereto belonging or in anywise appertaining, and the reversion and reversions, remainder and remainders, rents, issues, and profits thereof, and all the estate, right, title, interest, claim, and demand whatsoever of the Mortgagor, either in law or equity, of, in, and to the above bargained premises, with the hereditaments and appurtenances; TO HAVE AND TO HOLD said premises above bargained and described, with the appurtenances, unto the Trustee and its successors in trust, forever, in trust for the uses and purposes hereinafter mentioned.

And the Mortgagor, for itself, its legal representatives, successors, and assigns, hereby covenants with the Trustee and its successors in trust, as follows:

1. That, at the time of the enrolling and delivery of these presents, the Mortgagor is well seized of the premises above conveyed of a good, sure, perfect, absolute, and indefeasible estate of inheritance in law and in fee simple, and has good right, full power, and lawful authority to grant, bargain, sell, convey, and encumber the same in manner and form aforesaid, and that the same are free and clear from all former and other grants, bargains, sales, liens, taxes, assessments, and encumbrances of whatsoever kind and nature, except

and that the Mortgagor shall and will forever warrant and defend the same to the Trustee and its successors in trust against the lawful claims and demands of all persons, except as in this paragraph stated;

2. That the Mortgagor will pay promptly when due the indebtedness evidenced as aforesaid and the interest thereon;

3. That the Mortgagor will pay promptly when due all indebtedness, principal and interest, secured by any and all prior and superior mortgages, if any, and all taxes and assessments, rent, and charges, and all laborers', mechanics' or materialmen's or other liens of every name and nature which shall be levied or imposed upon said real estate, or upon or on account of this indenture, or the indebtedness secured hereby, or upon the interest or estate in said property represented by this mortgage, whether levied or assessed or imposed against the Mortgagor, or otherwise;

4. That the Mortgagor will keep all destructible property described herein, or situated upon the lands described herein, insured against loss and damage by fire and such other risks and hazards as the Trustee may from time to time specify, all in responsible insurance companies approved by the Trustee, in an amount not less than the amount of the indebtedness secured hereby, with loss payable by any insurer to the Trustee as its interest created hereby may appear, and will pay promptly the premiums therefor, and will deliver said policies, as soon as issued, to the Trustee;

5. That the Mortgagor will keep all buildings and improvements on said premises in good and substantial repair, and will make no alterations therein (except to keep them in good repair) without the written consent of the Trustee, and will commit no waste upon said premises; and, if the Mortgagor shall neglect so to keep in repair, the Trustee may, at its discretion, enter upon said premises from time to time and repair and keep in repair said buildings and improvements without thereby becoming liable as a Mortgagee in possession, and that the expense of so doing shall be repaid by the Mortgagor on demand, with interest at the rate of 10% per annum, and, until so repaid, shall become and be so much additional indebtedness secured hereby;

6. That the Trustee shall have the right at any time by it deemed necessary to incur expense in procuring and/or continuing an abstract of title to said premises, or other showing of the title, and any expense so incurred shall be repaid by the Mortgagor, with interest at the rate of 10% per annum, and, until so repaid, shall be so much additional indebtedness secured hereby;

7. That if the Mortgagor shall make default in the payment of any of the aforesaid taxes, assessments, rates, charges, mortgages, and liens, or in procuring and maintaining insurance as above covenanted, the Trustee, or any payee of the indebtedness secured hereby, at its option, may pay such taxes, assessments, rates, charges, mortgages or liens, and effect and maintain such insurance, and the sum or sums so paid shall be repaid by the Mortgagor to the Trustee or payee on demand, and, until so repaid, shall bear interest at the rate of 10% per annum and shall be a further lien on the aforesaid property and premises as so much additional indebtedness secured by this indenture;

8. That, in case of the breach or default in the performance by the Mortgagor of any covenant herein contained, all of the indebtedness secured by this instrument, whether the same shall be due and payable according to the tenor and effect of any promissory note secured hereby or not, and anything herein to the contrary notwithstanding, shall, at the option of the Trustee, or of the payee of the indebtedness secured hereby, immediately become and be due and payable without notice to the Mortgagor of such option or election: PROVIDED, that if the indebtedness secured be evidenced by more than one promissory note, such election may be made either by the

9. That, in case of any suit or proceeding at law or in equity, or in any probate or administration proceeding, wherein the Trustee or any payee of the indebtedness secured hereby shall become a party by reason of being interested in the premises as Trustee or as such payee, or for any purpose other than for the collection of the indebtedness secured hereby or the foreclosure of this indenture, there shall accrue hereunder and be paid by the Mortgagor all reasonable costs, charges, attorney's and solicitor's fees thereby occasioned, and the same shall be a further charge and lien on said premises secured hereby, and shall draw interest at the rate of 10% per annum from the date of such accrual until paid;

10. That the Mortgagor will pay to the Trustee, in addition to all of the other indebtedness secured hereby, ten per cent on the amount of such other indebtedness then due and payable as attorney's fees whenever any application to any Court or Referee shall be made to compel the payment of the indebtedness secured hereby, or any part thereof, or to realize on the security created hereby, whether by foreclosure or otherwise, and whether the proceeding, suit or actions be instituted in the first instance by the Trustee, or by any payee of the indebtedness secured hereby, or otherwise, and the amount of such attorney's fee shall be so much additional indebtedness likewise secured hereby;

11. That, whenever any application to any Court or Referee shall be made to compel the payment of the indebtedness secured hereby, or any part thereof, or to realize on the security created hereby, whether by foreclosure or otherwise, and whether the proceeding, suit or action be instituted in the first instance by the Trustee, or by any payee of the indebtedness secured hereby, or otherwise, the Trustee and those for whose benefit this security is held shall be entitled, without notice to the Mortgagor, to the immediate appointment of a receiver to take possession and control of said premises, and collect, receive and apply the rents, issues and profits thereof, during foreclosure and period of redemption, under direction of the Court appointing such receiver, and all such rents, issues and profits, as may accrue during the term of this instrument, are hereby specifically assigned and pledged as additional security for the payment of the indebtedness aforesaid, with the understanding, however, that so long as the Mortgagor is not in default of performance of any covenant herein contained, it may collect, use and enjoy the rents, and profits aforesaid;

12. In case the Mortgagor, its legal representatives and assigns, shall well and truly keep and perform each and all of the covenants herein contained, this indenture shall become void and of no effect, but in case of default in the due and proper performance of said covenants, or any of them, then, and in that case, this indenture shall remain and be in full force and effect and may be foreclosed immediately in any Court of competent jurisdiction, and thereupon the net proceeds of foreclosure sale shall be applied toward the payment of the indebtedness secured hereby. Any person interested in the proceeds, or any part thereof, of such foreclosure sale shall be entitled to become a purchaser, and, in such event, at the option of such purchaser, he shall be entitled to a credit on the purchase price in the amount of this interest in such proceeds, except that all costs adjudged payable to others than the purchaser shall be paid in cash;

13. When the indebtedness secured hereby shall have been fully paid, this indenture shall, on demand of the Mortgagor, its legal representatives or assigns, and upon payment to the Trustee of the sum of One and 50/100 Dollars (\$1.50) therefor, be released by the Trustee without expense to the Trustee or payee for the recording of such release;

14. In case of the resignation, refusal, failure, or inability of the Trustee at any time to act, the then acting Sheriff of the county in which said real estate is situated shall be and he hereby is appointed and made successor in trust, with all of the rights, powers, and duties of the Trustee as herein expressed, to the same extent as if he had been specifically named herein as Trustee, and any person dealing with or concerning said real estate and premises or with said Sheriff as successor trustee shall not be required to inquire into the inability of the original Trustee to act, and, as to such person, it shall be conclusively presumed that such successor trustee at the time of his act had all the powers, rights, and duties herein granted to and imposed upon the original Trustee;

15. All of the grants, agreements, and covenants of the Mortgagor herein contained shall be binding upon the heirs, executors, administrators and assigns of the Mortgagor, if the Mortgagor be one or more natural persons, and upon the successors and assigns of the Mortgagor, if the Mortgagor be one or more corporations, as well as upon the Mortgagor, and shall inure to the benefit of the Trustee and of every successor trustee. The term "Payee" as used herein shall be construed to include any person, firm or corporation entitled, for the time being, to receive payment of the indebtedness secured hereby, or any part thereof, and the Trustee may be a payee without modifying or impairing its capacity as Trustee.

IN WITNESS WHEREOF, the Mortgagor has executed this indenture the day and year first above written.

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____

ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,

by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF _____

ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19____,

by _____ of _____
(Name of Officer) (Title of Officer) (Name of Corporation Acknowledging)

a _____ corporation, on behalf of said corporation.
(State of Incorporation)

My commission expires:
(Seal)

Notary Public

ASSIGNMENT OF MORTGAGE

_____, holder of a mortgage from _____ dated _____ and recorded in Book _____, page _____, as Document # _____ of the records of _____ County, New Mexico, hereby assign said mortgage and the obligation secured thereby to _____, which Mortgage is secured by _____, New Mexico, towit: the following real estate situate and lying within the County of _____

Legal Description

WITNESS our hand and seal this ____ day of _____, 1998..

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____

This instrument was acknowledged before me on this ____ day of _____, 1998, by _____ and _____.

My commission expires:
(Seal)

Notary Public

Assignment of Deed of Trust

For a valuable consideration, the undersigned beneficiary in that certain deed of trust executed by:

on the _____ day of _____, and recorded in Book _____ page (folio) _____ of the records of _____ County, New Mexico, does hereby sell, assign, transfer and set over unto

the said deed of trust with all of the security, rights, benefit, protection and remedy of the beneficiary therein, but without recourse on the undersigned. The Note _____ mentioned in and secured by said deed of trust has _____ also on this day been sold and assigned to the assignee hereof.

Dated this the _____ day of _____

Beneficiary.

STATE OF NEW MEXICO }
County of _____ } ss.

On this _____ day of _____, before me personally appeared _____ to me known to be the person _____ described in and who executed the foregoing instrument, and acknowledged that _____ he executed the same as _____ free act and deed.

Witness my hand and notarial seal on this the day and year first above written.

My Commission Expires:

Notary Public, _____
New Mexico County,

* * * * *

STATE OF NEW MEXICO }
County of _____ } ss.

On this _____ day of _____, before me appeared _____ to me personally known, who, being by me duly sworn did say that he is the _____ of _____ a corporation organized under the laws of _____, and that the seal affixed to said instrument is the corporate seal of said corporation, and that said instrument was signed and sealed in behalf of said corporation by authority of its board of directors, and the said _____ acknowledged said instrument to be the free act and deed of said corporation.

Witness my hand and notarial seal on this the day and year first above written.

My Commission Expires:

Notary Public, _____
New Mexico County,

RELEASE OF DEED OF TRUST

under a certain deed of trust executed by _____ trustee
on the _____ day of _____, 19_____, and recorded in Book _____ page _____
of the records of _____ County, New Mexico, does hereby, at the written request of the beneficiary of
said deed of trust, discharge all of the real estate mentioned in said deed of trust from the lien and operation thereof.

WITNESS hand and seal this _____ day of _____, 19_____
(Seal) (Seal)
(Seal) (Seal)

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____
by _____

(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal)

Notary Public

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF _____

} ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____
by _____

(Name of Officer)

(Title of Officer)

of

(Name of Corporation Acknowledging)

a _____ corporation, on behalf of said
(State of Incorporation) corporation.

My commission expires:

(Seal)

Notary Public

FOR RECORDER'S USE ONLY

PARTIAL RELEASE OF MORTGAGE

_____, mortgagee_____

under a certain mortgage executed by_____

on the_____ day of _____, 19_____, and recorded in Book_____ page_____ of the

records of _____ County, New Mexico, do_____ hereby discharge the following portion only of the real estate described in said mortgage:

WITNESS _____ hand _____ and seal _____ this _____ day of _____, 19_____

_____(Seal) _____(Seal)

_____(Seal) _____(Seal)

ACKNOWLEDGMENT FOR NATURAL PERSONS

STATE OF NEW MEXICO

COUNTY OF _____ } ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____

by _____
(Name or Names of Person or Persons Acknowledging)

My commission expires:
(Seal)

Notary Public

FOR RECORDER'S USE ONLY

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO

COUNTY OF _____ } ss.

The foregoing instrument was acknowledged before me this _____ day of _____, 19_____

by _____
(Name of Officer)

_____ of _____
(Title of Officer) (Name of Corporation Acknowledging)

a _____ corporation, on behalf of said corporation.
(State of Incorporation)

My commission expires:
(Seal)

Notary Public

PARTIAL RELEASE OF DEED OF TRUST

on the _____ day of _____, 199_ and recorded in Book _____ at page _____ as
Document # _____ of the records of _____ County, New Mexico, does hereby, at the request of
the beneficiary of said deed of trust, discharge all of the real estate mentioned in said deed of trust from the lien and operation thereof.

WITNESS our hand and seal this _____ day of _____, 199_.

ACKNOWLEDGMENT FOR CORPORATION

STATE OF NEW MEXICO }

COUNTY OF _____ }

ss.

This instrument was acknowledged before me this _____ day of _____, 199_, by _____.

My commission expires:
(Seal)

Notary Public

AFFIDAVIT OF DEFAULT

STATE OF NEW MEXICO

COUNTY OF

}
SS

RE: Real Estate Contract dated

Sellers,

Purchasers

, having first been duly sworn upon his oath, states:

1. That he is the (attorney or agent for the seller, or seller) named in that Real Estate Contract described above, which agreement is for the purchase of certain real estate located in County, to-wit:

Legal Description

2. That the said Purchasers failed to make the payment(s) due in the amount of to the escrow agent as required by the real estate contract, and therefore are in default of their obligations imposed by said contract.

3. That on , the affiant, at the request of the sellers sent a letter of demand to the purchasers for the payment due by certified mail, return receipt requested, addressed to them at Copies of the demand letter is attached hereto as Exhibit A.

4. That the purchasers failed to make the payments as required by said demand letter on or before and therefore have forfeited their rights as provided by the aforesaid contract.

Dated:

Subscribed and sworn to before me this ____ day of , 199_, by

My commission expires:

Notary Public