**Installment Contracts and Seller Financing –**
**Alternatives for Selling Real Estate in Today's Financial Market**

The current lending market has provided an increase in obstacles to both buyers and sellers of residential properties. When lending markets tighten, or other financial elements make traditional borrowing difficult (i.e. high interest rates), a common alternative is seller financing, or installment sales contracts. These two (2) options are not synonymous, and the choice of method differs depending on whether the analysis is on behalf of the buyer or seller.

## Seller Financing

Seller financing is a situation where the seller acts like a traditional lender. Under this scenario, a buyer executes a Promissory Note in favor of the seller. The seller delivers a Deed to the buyer, to transfer title to the real estate into the name of the buyer. The buyer then executes a Mortgage in favor of the seller, granting the seller a lien against the property as security for repayment of the Promissory Note.

A buyer obtains greatest benefit from this method of financing. With this transaction, the buyer obtains has complete ownership and control of the property, subject only to the seller's lien rights. Conversely, the seller no longer has an ownership interest in the property, and cannot use the property as collateral, or do anything that could create a lien against the property in favor of a third party.

The recording of the Mortgage in the County Recorder's Office puts the public on notice of the seller's lien against the property. This protects the seller in the event the buyer decides to sell the real estate, or further encumber the real estate with liens.

If the buyer defaults on repayment of the Promissory Note, the only recourse available to the seller is to sue the buyer. This is generally done by the filing of a foreclosure lawsuit in a Court of proper jurisdiction. In a foreclosure action, the buyer has the right to defend itself and to redeem the real estate. Other lienholders, if any, are also given the right to assert their interest in the property. If the seller ultimately prevails in the foreclosure, it may obtain a judgment against the property (resulting in a sheriff's sale where the property is sold to satisfy the seller's judgment) and a judgment against the individual, personally (to satisfy any deficiency between the sales price and the judgment).

## Installment Sales

An Installment Sales Agreement (or Installment Contract) is a contract between the buyer and seller for the sale of the real estate over a period of time. Under the agreement, the buyer makes periodic (typically monthly) payments to the seller for the real estate. The seller retains ownership of the real estate and, therefore, has ultimate control over the title to the property. This is called "legal title" to the real estate.

Since the buyer has the rights set forth in the Agreement and is making payments toward the purchase of the real estate, the buyer holds "equitable title" to the real estate. The term "equitable" is meant to impart what is just and right, in this case that the buyer does have some vested interest in the real estate, the amount of which is dependant upon how much the buyer has paid toward the purchase.

An Installment Sales Agreement tends to provide more benefit to the seller than the buyer. Since the seller still holds title, the seller is able to use the real estate as collateral unless otherwise prohibited by the Agreement. Even more importantly, if the buyer defaults on his payments, the seller may have the option to declare the buyer's rights forfeited, so that the buyer no longer has an interest in the real estate and the seller retains the buyer's previous payments as liquidated damages.

However, forfeiture is not favored by the law. While there are no statutory laws outlining the rights of an installment purchaser to its equitable title, the courts over the years have issued rulings designed to protect the buyer's equitable interests. In a 1973 lawsuit where an installment purchaser had paid well over one-half (1/2) of the purchase price under the Installment Agreement, the Indiana Supreme Court ruled that forfeiture was excessive and that foreclosure was a more appropriate remedy. Accordingly, the ability to forfeit a buyer's equitable interest is limited to what the legal system views as fair and just, generally where little money has been paid toward the purchase.

**Similarities between Methods**

Under both the alternative financing methods outlined above, the buyer is usually responsible for payment of the taxes, insurance and maintenance of the real estate. Under the seller financing method these responsibilities come from ownership of the real estate and under the terms of the Mortgage. Under the Installment Sales Agreement, the responsibilities are contractual and therefore can be more flexible, allowing the buyer to handle these responsibilities directly or through reimbursement of the seller.

Also under both methods, the buyer has an insurable interest in the real estate, either as an owner of legal title or as an owner of equitable title. Title insurance is important to protect the buyer's title in the event of an unknown title defect. Finally, both methods provide the ability to effect a purchase and sale of real estate when traditional financing is unavailable.

When assessing the sale of a residence, both buyer and seller should carefully consider the agreement they are going to sign and seek professional assistance before executing any contract. While the content of the agreement may not be useful so long as both parties behave as expected, if the deal turns bad the wording of the contract may make or break either party.

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