Bankruptcy and the Land Sale Contract

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NOTE

Bankruptcy and the Land Sale Contract*

The primary impact of a bankruptcy is usually absorbed by the creditors of the bankrupt party. But when the party taking bankruptcy is in the business of selling land with land sale installment contracts, the party's customers, the vendees, can suffer losses even more onerous than the creditors. This Note examines the legal status of the vendee who purchases land by an installment contract and compares him to the land purchaser who relies, instead, on a mortgage. Then, on the basis of economics and equity, the author concludes that the vendee should not be subjected to the extreme penalties he may now undergo when the vendor of the land becomes bankrupt. Because the existing protection for the vendee appears inadequate, the author suggests various changes in the law, principal among which is an amendment to the Bankruptcy Act.

I. INTRODUCTION

In most bankruptcy situations, the bankrupt's creditors are the only ones who are likely to suffer financial injury. The creditors frequently do not recover the full amount of their debts from the bankrupt's estate, and the bankrupt himself is relieved of his financial obligations. But the result is different when the bankrupt is the vendor in a land sale contract. Again, his creditors may suffer some loss, but that is not cause for unusual concern — a chance of loss is one of the risks of being a commercial creditor. What is disturbing and inequitable is that the bankrupt land vendor's debtor — the vendee under the land sale contract — will likely incur financial loss although still ready, willing and able to perform in compliance with the land sale contract. The vendee in this situation may suffer substantial losses because of section 70(b) of the Bankruptcy Act, which authorizes a bankruptcy trustee to reject executory contracts.

* The writer wishes to acknowledge the help of Professor Morris G. Shanker, whose conversation, writings and private correspondence have been useful in the preparation of this Note.

1 There are two basic types of land sale contracts. One is the "buy-sell" agreement, in which a deed is conveyed and closing of terms follows. The other is the installment sale contract, in which legal title remains with the vendor until the contract is performed and which is used as a security device in place of a mortgage or deed of trust. This Note is concerned with the latter. See generally G. Osborne, HANDBOOK ON THE LAW OF MORTGAGES 29-31 (2d ed. 1970).

This Note is also limited to the problem of land sale installment contracts. Installment contracts for the purchase of personality raise a number of different questions, both legal and economic, not present when dealing with realty. See, e.g., UNIFORM COMMERCIAL CODE § 9-506 (which gives the buyer-debtor rights similar to a mortgagor's equity of redemption).

An example will clarify the vendee’s position. Assume the prospective vendor owns a tract of land and his ambition is to subdivide it into quarter-acre lots to be sold as modest home sites to low and middle income purchasers.

For a number of reasons, the vendee may make his purchase using a land sale contract, rather than a mortgage. When a land sale contract is used, the vendee acquires legal title only after he has made his final installment payment. Location of title in the vendor pending performance of the contract means that the contract may be deemed executory as to both parties, and the vendee may remain an unsecured party, except to the extent that an equitable lien might afford him relief in bankruptcy court.

Continuing with the example, assume the parties enter into a land sale contract with a purchase price of $10,000, allowing the vendee to take immediate possession and obligating him to begin payments. Even though the vendee subsequently pays $9,000 of the $10,000 contract price, if the vendor goes bankrupt, the danger is that the vendor’s trustee in bankruptcy may reject any tender of final payment by the vendee. The trustee’s authority is section

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3 A land sale contract usually involves only two parties, vendor and vendee, as opposed to the general three-party arrangement of a purchase money mortgage where a third party serves as financier. Other tripartite arrangements are the blanket mortgage and the subdivision trust. In a blanket mortgage, the vendor gives a bank a mortgage on the entire parcel of land under development and obtains a release; the vendee of each lot becomes a mortgagor of the bank, and the vendor is no longer a debtor. The bank then could acquire some control regarding who becomes the bank’s mortgagors.

Under a subdivision trust, title remains with a trustee until payments have been completed by the beneficiary, the vendee. These arrangements are not executory contracts and would not be subject to rejection by the vendor’s trustee in bankruptcy. See Carlock, The Subdivision Trust — A Useful Device in Real Estate Transactions, 5 ARIZ. L. REV. 1 (1963); Rehnquist, Subdivision Trusts and the Bankruptcy Act, 3 ARIZ. L. REV. 165 (1961).

4 The foreclosure provision in the standard land sale contract of a Pennsylvania recreation lot vendor reads as follows:

This conveyance is also made upon the express condition and covenants that Grantee will make all the payments as provided in the Agreement of Sale and if Grantee fails to do so, then the title and interest in and to the premises hereby conveyed shall be and become wholly void and the premises and all interests therein shall revert to and become reinvested in Grantor.

5 It has not yet been decided conclusively whether an equitable lien could be extended to the vendee in a bankruptcy situation. If so, he would take priority over unsecured creditors in obtaining a refund of his payments from the bankrupt’s estate. See notes 44-53 infra & accompanying text.

6 The trustee may reject without an express order from the court. 4A COLLIER ON BANKRUPTCY § 70.43 (5), at 530 (14th ed. 1969).

A bankruptcy receiver could also exercise the power of assumption or rejection of executory contracts under section 70 (b). He would be the appropriate officer in a reorganization proceeding, as distinct from the trustee in a non-reorganization bankruptcy. See In re Forgee Metal Products, Inc., 229 F.2d 799 (3d Cir. 1956).
70(b) which permits rejection of an executory contract. The trustee may at the same time sell the land to a third party for a price greater than the contract terms and apply the revenue to the estate for the benefit of creditors. The original vendee becomes nothing more than a creditor for that portion of the contract price he has paid, unless the contract gave him a legal lien or the bankruptcy court recognizes his lien in equity. In the role of an unsecured creditor, the vendee would benefit from the land sale in the same percentage as the vendor's other unsecured creditors.

This sequence of events may occur when financing for purchase-money mortgages is scarce, or when the vendee does not have sufficient funds to pay for the portion of the purchase price not covered

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7 Section 70(b) of the Bankruptcy Act reads, in full:

The trustee shall assume or reject an executory contract, including an unexpired lease of real property, within sixty days after the adjudication or within thirty days after the qualification of the trustee, whichever is later, but the court may for cause shown extend or reduce the time. Any such contract or lease not assumed or rejected within that time shall be deemed to be rejected. If a trustee is not appointed, any such contract or lease shall be deemed to be rejected within thirty days after the date of the order directing that a trustee be not appointed. A trustee shall file, within sixty days after adjudication or within sixty days after he has qualified, whichever is later, unless the court for cause shown extends or reduces the time, a statement under oath showing which, if any, of the contracts of the bankrupt are executory in whole or in part, including unexpired leases of real property, and which, if any, have been rejected by the trustee. Unless a lease of real property expressly otherwise provides, a rejection of the lease or of any covenant therein by the trustee of the lessor does not deprive the lessee of his estate. A general covenant or condition in a lease that it shall not be assigned shall not be construed to prevent the trustee from assuming the same at his election and subsequently assigning the same; but an express covenant that an assignment by operation of law or the bankruptcy of a specified party thereto or of either party shall terminate the lease or give the other party an election to terminate the same is enforceable. A trustee who elects to assume a contract or lease of the bankrupt and who subsequently, with the approval of the court and upon such terms and conditions as the court may fix after hearing upon notice to the other party to the contract or lease, assigns the contract or lease to a third person, is not liable for breaches occurring after the assignment.

8 The Bankruptcy Act grants the status of creditor to persons injured by the rejection of executory contracts. Report of the Senate Comm. on the Judiciary, reprinted in 1 BANKR. L REP. § 8212 (May 27, 1938) (explanatory note).

9 One remedial proposal is to lower interest rates on mortgages, by putting more money into the hands of lending institutions, through reduction of reserve requirements. Gillies, The Scarcity of Capital for Mortgage Lending in California: An Economic or Legal Problem?, 9 U.C.L.A. L REV. 545, 547, 551-60 (1962).

The Federal Government can exercise considerable influence over the real estate industry by its monetary policy as a whole. For example, if it limits the sales of its own securities, notably treasury bills, in the open market, interest rates may remain high; or a significant increase in the amount of money permitted in circulation by the Federal Reserve Board may cause interest rates to drop. The current wage-price freeze, if extended to interest rates, could foster the growth of the real estate industry, because prospective home buyers would find an incentive in lower borrowing costs.
by the amount of the mortgage.10 When mortgage money becomes scarce, commercial or consumer land development companies that have little capital turn to land sale contracts as a means of low-equity financing.11

Although the number of actual bankruptcies and reorganizations has been "relatively minor in the overall picture"12 of land sales, there is a significant potential for such bankruptcies in the consumer area. Installment contracts are customary where builders have acquired land for development, and mail-order developers in Florida, California, the Southwest and the Midwest13 have been generating a high volume of land installment contract sales for a period of years. In fact, the mail-order land business has an annual sales volume that ranges from an estimated $700 million to over one billion dollars,14 of which a significant percentage is conducted with installment contracts. An economic downswing could drive some of these vendor-developers into bankruptcy.

Vendors with marginal financing, then, can endanger the invest-

10 G. Osborne, supra note 1, at 29.

11 The experience of the Penn Central Railroad, which is a major land owner, is an example of how unexpectedly a commercial giant can fall into reorganization or bankruptcy and subject the vendee to land sale bankruptcy problems.


In addition to their use by commercial vendees, installment contracts are used in the purchase and sale of retirement havens, vacation lots, investment acreage, homesteads in developing communities and farmland. 113 Cong. Rec. 315 (1967). Land sale contracts are also necessary for the purchase of inner city lots on which homes are already built, because many buyers otherwise have difficulty obtaining financing. See generally, Mixon, Installment Land Contracts: A Study of Low Income Transactions, with Proposals for Reform and a New Program to Provide Home Ownership in the Inner City, 7 Houston L. Rev. 523 (1970). Unlike the large-scale land sale promotions, the individual inner city transactions are often outside the coverage of the Interstate Land Sales Registration Act, whose provisions were drafted to enable the purchaser to rescind where the vendor has used fraud regarding any material term of the contract. See 15 U.S.C. §§ 1701-20 (1970). See generally Coffey & Welch, Federal Regulation of Land Sales: Full Disclosure Comes Down to Earth, 21 Case W. Res. L. Rev. 5 (1969).
ments of substantial numbers of land sale contract purchasers. This Note will demonstrate that the risk to the land sale installment contract vendee is an unwarranted one and that, when the vendor takes bankruptcy, the vendee who purchased property using a land sale contract should receive the same protection afforded the purchase-money mortgagor. Second, it will show that existing remedies are inadequate to provide the required protection to the vendee. Consequently, the author will propose new remedies to enable the land sale vendee who continues performance to retain possession of his land and have his contract completed, despite the vendor’s bankruptcy.

II. THE LAND SALE VENDEE’S RIGHTS WHEN THE VENDOR TAKES BANKRUPTCY

In order to understand the vendee’s position, it is best to examine his rights in comparison with those of a mortgagor, and then to consider the vendee’s rights in the context of the vendor’s bankruptcy.

A. How the Vendee Compares with the Mortgagor

The purchase-money mortgage and the land sale contract have the same function: to secure the payment of unpaid purchase money. As purchasers, the mortgagor and the person who buys with an installment contract occupy parallel positions, in that both have delayed part of their payment obligation until some time after possession. But their similarity from the economic perspective is not reflected in their legal positions. A defaulting mortgagor has an equity of redemption—the right to get back his land by tendering late payment—while a defaulting vendee ordinarily may not redeem. And a defaulting vendee may lose more than his land: the vendor may retain all of the vendee’s payments, and even sue for installments yet due if the contract so provides. The vendee is treated differently than the mortgagor because the mortgagor’s equity of redemption historically became established as a “right.”

15 The chief distinction between the two from an economic perspective is the traditionally smaller initial payment required under an installment contract. See also note 22 infra.

16 See generally G. OSBORNE, SECURED TRANSACTIONS 218-22 (1967).

17 E.g., Heckard v. Sayre, 34 Ill. 142 (1864).

18 OSBORNE, supra note 16, at 29. If a court were to hold that such contractual provisions constituted liquidated damage clauses, it could refuse to enforce them.

19 The statutory right to redeem from the purchaser on a foreclosure sale does not arise until the equity of redemption has been extinguished. Id. at 219.
while the vendee's position under contract principles made specific performance and relief from forfeiture discretionary. In *Rothenberg v. Follman*, a Michigan court put the comparison in an historical framework:

One way of viewing the matter is to visualize the present state of the law regarding specific performance and relief from forfeiture in favor of a defaulting land contract purchaser as equivalent to the state of the law preceding recognition of the equity of redemption as the mortgagor's undoubted right, when the court of equity relieved against the condition of the mortgage in some cases and not in others as a matter of discretion depending on the equities.

Thus, under present law the land sale vendee receives, at best, a lien in equity for his payments, unless other rights are given in the contract or by statute. If the vendor becomes insolvent and his trustee in bankruptcy rejects the executory land contract, the vendee may lose both possession of the land and his payments because he lacks the rights which the mortgagor would have under similar circumstances.

Why then would a prospective vendee run the risk of entering a land sale contract when he might have the security of a mortgage instead? The land sale contract may appeal to the vendee because it involves a relatively small initial payment, although the interest rate on the installment payments is often higher than for a purchase-money mortgage. Furthermore, in periods of tight money, when mortgage loans are difficult for the vendee to obtain, the land sale installment contract may be the only alternative. Land sale contracts likewise may be attractive to a vendor because he has the right to recover the property in a forfeiture action against a defaulting purchaser, which enables the vendor to contract with higher risk purchasers, and also to reap unusual profits. The net result is that the lack of a right of redemption in the vendee distinguishes a land sale contract from a mortgage. 16 U. MIAMI L. REV. 493 (1962).


21 Id. at 848 n.4.

22 Frequently the vendee may not be able to finance a mortgage agreement requiring a high down payment. In this situation he might consider a land sale contract with a lower down payment and a higher rate of interest as the best alternative. Contract terms, however, are set by the parties, and land contracts do exist which, to the purchaser, have rates more favorable than mortgages. The underlying assumption of this Note, nevertheless, is that many commercial and consumer purchasers enter into disadvantageous land contracts because of their weak financial position.

If the Uniform Consumer Credit Code is widely adopted, the vendee will receive increased protection if he can establish that the land sale was a consumer credit transaction. See CCH INSTALLMENT CREDIT GUIDE, New Rules on Consumer Credit Protection (eff. February 10, 1969), § 4721, at 254.
vendee obtains credit for that portion of the sale price remaining unpaid, and the commercial vendor acquires working capital from both the down payment and subsequent installments.

B. Land Sale Contracts and the Policies of the Bankruptcy Act

The common law distinction between the mortgagor’s rights and the vendee’s contract rights had been read into the Bankruptcy Act, even before section 70(b) made the power to reject executory contracts explicit.\(^{23}\) The enactment of section 70(b) has been construed to merely reaffirm the prior case law.\(^{24}\) The pertinent part of that section provides that:

The trustee shall assume or reject an executory contract, including an unexpired lease of real property, within sixty days after the qualification of the trustee, whichever is later, but the court may for cause shown extend or reduce the time. Any such contract or lease not assumed or rejected within that time shall be deemed to be rejected.

Nothing in either the text or legislative history indicates that land contracts should be treated differently than any other executory contract. Thus, section 70(b) appears to permit rejection of the land sale vendee’s contract and it has been so read.\(^{25}\)

The land sale contract, however, need not be considered executory as to both parties. It could be argued that the bankrupt vendor has completed performance, except for the passing of title, and that the contract, as to him, is no longer executory\(^{26}\) and thus not subject to rejection under section 70(b). Although logically consistent, this argument has not been accepted in bankruptcy court.\(^{27}\)

A further argument that may be available to avoid rejection is that the trustee can only reject burdensome executory contracts and that a land sale contract which is already profitable is not burdensome merely because the trustee can find a more profitable contract in the current market.\(^{28}\) However, foremost in the trustee’s mind

\(^{23}\) See Sunflower Oil Co. v. Wilson, 142 U.S. 313 (1892).
\(^{24}\) \textit{4A} COLLIER, supra note 6, \S 70.43(2), at 521.
\(^{25}\) \textit{In re} New York Investors Mutual Group, Inc., 143 F. Supp. 51 (S.D.N.Y. 1956). Note that section 70(b) explicitly provides that the lessee cannot be deprived of his estate.
\(^{26}\) See Creedon & Zinman, \textit{Landlord's Bankruptcy: Laissez Les Lessees}, BUS. LAWYER 1391, 1401-05 (1971). Clearly the Act considers a mortgage executed when title has passed. \textit{See also} \textit{In re} Grayson-Robinson Stores, Inc., 321 F.2d 500, 502 (2d Cir. 1963), in which the court held guarantees of leases were executory contracts which could not be rejected in bankruptcy.
\(^{28}\) Cf. American Brake Shoe & Foundry Co. v. New York Rys. Co. 278 F. 842, 843-44 (S.D.N.Y. 1922), where the court stated that a
is the need to marshal assets for the benefit of creditors. If he assumes a contract, the bankrupt's estate is charged with the expense of managing the contract, so the trustee will not assume a contract unless it is profitable enough to outweigh the attendant liabilities. But it does not necessarily follow from this conception of the trustee's role under the Bankruptcy Act that the trustee should be permitted to reject an already profitable contract.

 Nonetheless, the only cases that have applied section 70(b) in similar factual situations have held that the purchaser in a land sale contract cannot compel specific performance from the seller's trustee in bankruptcy. In In re New York Investors Mutual Group, Inc., Judge Weinfeld refused to allow specific performance for a land sale vendee against the vendor's trustee in bankruptcy and commented generally on section 70(b): "Its underlying principle, and that of the case law which preceded its enactment, is that the trustee in bankruptcy may abandon burdensome property and reject unprofitable executory contracts in order to further the best interests of the estate." Although this language emphasizes the burdensome aspects of executory contracts, the opinion gave no indication that specific performance would ever be available, regardless of the circumstances. Under New York Investors, the rejecting trustee stands in the shoes of the vendor and has legal title, which prevails against any equitable title the vendee may have. The vendee cannot retain his property and has only a claim for damages.

 Relying upon New York Investors, the Court of Appeals for the Third Circuit held in Philadelphia Penn Worsted Co. that the doctrine of equitable conversion does not give the vendee with an equitable ownership a right superior to that of the trustee, who may, using the authority of section 70(b), reject the contract upon which the vendee's right is based. The vendee in Philadelphia Penn Worsted had agreed to purchase real estate at a public auction. The arrangement provided for a down payment with the balance of the
purchase price to be paid in cash, and delivery of a deed and possession at the time of settlement. This contract was held to be executory and subject to rejection by the seller's trustee.\(^3\)

The First Circuit adopted a similar approach to section 70(b) in *Gulf Petroleum, S.A. v. Collazo*.\(^3\) Gulf had negotiated a purchase and sale agreement with Puerto Rico Broilers, Inc., for land to be used as a site for a filling station. Under this arrangement, Gulf's installment payments were not to be credited to the purchase price until the closing. The funds were to be held in escrow until closing and were to be returned to Gulf if the closing did not take place for any reason other than the purchaser's default. Gulf had made two of the required three payments when Broilers was adjudicated bankrupt. Because the closing had not occurred when bankruptcy intervened, the court held that the contract was still executory, and Broilers' trustee was empowered to reject it under section 70(b). Although Gulf had no lien upon the bankrupt's land prior to the time both parties fulfilled their contractual obligations, they were held to be entitled to a return of the money paid because the trustee could not reject the escrow provisions of the contract. But the court disallowed Gulf's efforts to: (1) exclude the land from the sale of Broilers' assets; and (2) compel the trustee to convey it to Gulf upon tender of the final payment.\(^3\)

Thus, the courts have found no basis within the Bankruptcy Act and its underlying policies on which to deny the trustee the right to reject a land sale contract, despite the fact that the vendee is willing and able to perform.

### III. Current Protection for the Land Sale Vendee

Because the vendor's trustee in bankruptcy may reject the contract under section 70(b) of the Bankruptcy Act, the land sale vendee may lose his property and even the payments he has made. Despite the severity of this threat, there is little the vendee can do to protect himself. The vendee has no remedy which is certain to be effective. Indeed, there are only a few legal theories which might offer him some protection.

First, the vendee could argue that he should be entitled to the traditional breach of contract remedies of specific performance, rescission and damages. Second, if he does not have a legal lien on

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\(^{34}\) Id. at 665.

\(^{35}\) 316 F.2d 257 (1st Cir. 1963).

\(^{36}\) Id. at 257, 260.
his payments, the vendee could try to convince the bankruptcy court to enforce an equitable lien by analogizing to non-bankruptcy cases. Third, depending upon the state in which his land is located, the vendee may also argue that the applicable state law converts his land sale contract into a mortgage. Finally, the Interstate Land Sales Full Disclosure Act may offer some assistance by requiring the vendor to disclose certain information concerning his financial position. However, the value of each of these remedies is questionable, because they may be disallowed in bankruptcy court, and even if allowed, because they may fail to afford complete protection. This section will discuss these remedies and their inadequacies.

A. Contract Remedies

If the ordinary contract remedies of damages, rescission, and specific performance were available to the vendee, he would be afforded substantial, or even complete protection. Section 70(b), however, probably makes the latter two of these remedies inapplicable in bankruptcy court. It is undeniable that the land sale contract requires the vendor to transfer title to the vendee upon receipt of the total purchase price, and that refusal to transfer is a breach of the contract outside of bankruptcy. Section 70(b), however, gives the vendor’s trustee in bankruptcy the right to reject the contract, which would appear to preclude reliance on either of these two traditional remedies. Moreover, if only the section 103 damage action were allowed, and a damage judgment could be obtained, it is unlikely that the assets of the bankrupt’s estate could satisfy it in full. And even if the damage judgment were paid in full, payment would probably not be equivalent to holding the property, because of the uniqueness of the land and the buyer’s lost investment opportunity.

38 See notes 23-34 supra & accompanying text. 11 U.S.C. §§ 103 (a) (9), 103 (c) (1970) specifically allow an action for damages.
39 See Lee, Remedies for Breach of the Installment Land Contract, 19 U. MIAMI L. REV. 550, 567-74 (1965). Where a vendee has breached, the vendor has the following remedies: suit at law for damages; retention of payments as liquidated damages; retention of deposit as an alternative performance; a vendor’s lien; foreclosure by judicial sale; strict foreclosure of purchaser’s contract rights; forfeiture of purchaser’s payments; obtaining possession and quieting title. Id. at 550-67.
40 Id. at 570. See Kitchen v. Herring, 42 N.C. 178 (1851).
41 In County of Lincoln v. Fischer, 216 Ore. 421, 339 P.2d 1084 (1959), the purchaser, upon proper payment, was entitled to specific performance where the vendor, the county, had delayed for over a full year after the first installment was due before attempting to declare a forfeiture, but the vendor continued to receive taxes paid by the
Rescission, like damages, would probably be inadequate even if it were available. The assets of the bankrupt's estate would not provide full restitution and the vendee would be unable to retain the property. Since most vendees would want to retain the property, specific performance would seem the only complete contract remedy. Yet the vendee cannot seek specific performance until he has made the last payment and the vendor has failed to perform. Consequently, when the vendor's bankruptcy intervenes before the vendee can perform, the specific performance remedy is probably made unavailable by section 70(b).

B. Liens in Bankruptcy

Some land sale contracts give the vendee a legal lien which might provide for the return of the vendee's payments in the event of the vendor's bankruptcy. A legal lien in the case of a lease was given effect by a bankruptcy court in Cohen v. East Netherland Holding Co.

In Cohen, East Netherland, the lessee and builder of the property in question, had negotiated an unrecorded lease which required the lessor to pay for the value of the buildings constructed in the event of the lessor's default. Under the lease and the applicable state law, the lessee was entitled to remain in possession until that value was paid. The lessor became bankrupt and his trustee rejected the unexpired portion of the lease and complied with the saving clause of section 70(b): "Unless a lease of real property expressly otherwise provides, a rejection of the lease or of any covenant therein by the trustee of the lessor shall not deprive the lessee of his estate." The lease provision was held to be a legal purchaser. The market value of the property in question had soared from $500 to approximately $50,000.

42 Lee, supra note 39, at 570. See Luette v. Bank of Italy, 42 F.2d 9 (9th Cir. 1930).

43 Few courts have yet spoken to the availability of specific performance. Where the question was raised, courts held this remedy unavailable as a matter of law. See, e.g., In re New York Investors Mutual Group, Inc., 143 F. Supp. 51 (S.D.N.Y. 1956).

44 258 F.2d 14 (2d Cir. 1958).


46 11 U.S.C. § 110(b) (1970). If this saving clause applied to vendees, as well as lessees, the vendee would, of course, be fully protected. See notes 69-84 infra & accompanying text.

This provision of section 70(b) is an "equitable safeguard for an innocent party
lien binding on the trustee in bankruptcy. Thus, by consensual agreement, the lessee became empowered to retain possession of the property, after the trustee had rejected, until the appraised value was paid.\textsuperscript{47} In so doing the investment value which the lessee would otherwise have lost was restored. Thus, the bankruptcy court’s recognition of legal liens should allow the lessee to regain the payments he has made, assuming that the bankrupt’s estate has sufficient assets to pay the lien. A legal lien will not, however, enable the vendee to retain possession of his land, absent a saving clause governing land sale contracts.

But in practice, many land sale vendees do not have legal liens. Alternatively, a vendee without a legal lien can argue that he should have an equitable lien for his payments. In non-bankruptcy situations, many state courts have recognized equitable liens when the vendor has breached the contract.\textsuperscript{48} For example, an Ohio court in \textit{Cleveland Trust v. Bouse}, which involved a purchaser who had intervened in a mortgage foreclosure proceeding, held that, “[w]here an executory contract for the sale of real property is breached by the vendor, the purchaser is entitled to an equitable lien for the amount he has paid on the purchase price.”\textsuperscript{49} Later, expanding upon \textit{Bouse}, \textit{Wayne Building and Loan Co. v. Yarborough} held that the vendee’s equitable lien in the land does not depend upon his possession.\textsuperscript{50} Although the equitable lien theory has not yet been raised in a bankruptcy court, it offers a direction for courts willing to analogize between a vendor who has breached and a vendor’s trustee who has rejected. But even if a buyer were successful in exercising an equitable lien, he would only receive his

\begin{footnotes}
\item[47] In Spruell v. Blythe, 215 Md. 117, 137 A.2d 183 (1957), the Maryland Supreme Court reached this point in a non-bankruptcy case involving a land vendee. It held that the vendee was entitled not only to a decree for compensation, but also to a lien upon the house and lot to secure payment from the vendor who had breached.

\item[48] The vendee’s lien is similar to that of the vendor for unpaid purchase money. \textit{See} National Indem. Co. v. Banks, 376 F.2d 533, 534 (5th Cir. 1967).

\item[49] 163 Ohio St. 392, 397, 127 N.E.2d 7, 10 (1955). There is as much justice in providing the vendee with a lien device for installments he has paid as in providing the vendor a right to foreclose in order to get payments he has been promised by the contract. \textit{King}, \textit{Survey of Ohio Law-Equity}, 7 CASE W. RES. L. REV. 282, 284 (1956). The \textit{Bouse} court, however, did not decide the priorities between a mortgage lien and an equitable lien when the proceeds of sale were inadequate to satisfy both. \textit{Comment}, 25 U. CIN. L. REV. 170 (1956).

\item[50] 111 Ohio St. 2d 195, 228 N.E.2d 841 (1967).
\end{footnotes}
payments and would have no option to complete the contract and obtain title to the land.  

If the equitable lien were used as a remedy in the bankruptcy situation, there are certain technical problems which could limit its value.  

For example, the Bankruptcy Act states:

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\text{[t]he recognition of equitable liens where available means of perfecting legal liens have not been employed is hereby declared to be contrary to the policy of [section 60(a)(6)] ... [p]rovided, however, [t]hat, where the debtor's own interest is only equitable, he can perfect a transfer thereof by any means appropriate fully to transfer an interest of that character ...}
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If the vendee does not have a legal lien where one could have been obtained, this provision might result in his being denied an equitable lien as well.

C. Conversion of the Land Sale Installment Contract into a Mortgage

In some states the distinction between the land sale contract and the mortgage has been eliminated, particularly when the vendee has substantially performed his obligations under the contract. This conversion of land sale contracts to mortgages has been effected both judicially and legislatively in non-bankruptcy situations, and although the state courts cannot override federal bankruptcy law, the bankruptcy courts may accept a state's definition of what constitutes a mortgage. If the conversion has occurred prior to bankruptcy and is given effect by the bankruptcy court, then the trustee is confronted with a contract which he cannot reject.

In Mid-State Investor's Corp. v. O'Steen, a Florida non-bankruptcy case, the court interpreted a land sale contract as a mortgage. As part of a loan transaction to purchase a home, the vendee in Mid-State had assigned his deed to the vendor and received an unrecorded installment contract for the deed. The contract provided for forfeiture and reposssession upon default, and when the vendee defaulted, the vendor repossessed the house. The

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51 The right of a vendee who has a lien for purchase money paid was held to take priority over a tax lien against the seller in State Fidelity Federal Savings & Loan Ass'n v. Wehrly, 263 N.E.2d 801 (Ohio C.P. 1970).


vendee subsequently brought an action for trespass in which the court held that the contract was a mortgage and that the vendor had no right to repossess upon the vendee's default. The general Florida rule underlying this decision is that "[a]ll conveyances... with the intention of securing the payment of money... shall be deemed and held mortgages, and shall be subject to the same rules of foreclosure... as are prescribed in relation to mortgages." If this rationale were permitted in bankruptcy court, the vendee would become a mortgagor, immune from rejection of the contract by the vendor's trustee.

Some courts, although not going to the extent of the Mid-State decision, have been reluctant to strictly enforce the provisions of a land sale contract when the purchaser has made a substantial number of payments. For example, in Rothenberg v. Pollman, the purchasers obtained relief in a forfeiture action, even though they were in default on one installment and the contract provided that time was of the essence. The Michigan court of appeals held that forfeiture was unreasonable and the vendees were entitled to specific performance where the amount in default was only $1500 principal plus $225 interest, of a purchase price of $40,000, and some of the purchasers had attempted to pay their share of the delinquent payment. The inequity of allowing a vendor to reclaim land while retaining the vendee's payments has also prompted the Iowa courts to avoid unreasonable forfeitures. They have done so by interpreting the vendor's acceptance of part payment as a waiver of his right to immediate forfeiture. These cases, although not holding


58 Id. at 849, 851. Similarly, in Land Development, Inc. v. Padgett, 369 P.2d 888 (Alaska 1962), the purchasers had been in possession of the realty in question for three years prior to their default, and they had paid about two-thirds of the purchase price. The court held that enforcement of forfeiture would be inequitable; "it would cause a loss to the buyers all out of proportion to any injury that might be sustained by the seller." Id. at 889. See also Dependabilt Homes v. White, 117 N.E.2d 706 (Ohio Ct. App. 1951).

For the contrary view, that the vendor is entitled to rescission without tendering back the payments made when the purchaser has failed to make the monthly payments agreed upon, see Miami Investment Corp. v. Baker, 109 Ohio App. 354, 165 N.E.2d 690 (1959).


60 But waiver of one default does not amount to a waiver for subsequent defaults. See Cassiday v. Adamson, 208 Iowa 417, 421, 224 N.W. 508, 510 (1929).
that the land sale contract is the same as a mortgage, have reached
the same result as did Mid-State and would provide the vendee the
same protection if followed in bankruptcy court.

In addition to the judicial efforts to protect the vendee, several
state legislatures have enacted statutory safeguards which, under
certain circumstances, effectively convert the installment contract in-
to a mortgage. A Maryland statute provides that a purchase-money
mortgage shall entirely supersede the land installment contract
when 40 percent of the original cash price has been paid. 61 In
Ohio, the applicable provision reads:

If the vendee of a land installment contract has paid in ac-
cordance with the terms of the contract for a period of five years or
more from the date of the first payment or has paid toward the pur-
chase price a total sum equal to or in excess of twenty percent
thereof, the vendor may recover possession of his property only by
use of a foreclosure proceeding and judicial sale of the foreclosed
property . . . 62

As with the Maryland law, the Ohio statute appears to treat the in-
stallment contract like a mortgage if there has been substantial per-
formance as defined by the statute. California has created another
approach by providing for prepayments of the balance due on real
property sales contracts. 63 When the prepayments have been fully
made, title passes. This provision could protect the vendee who
prepays the balance of the contract, if he does so before the date of
bankruptcy.

Thus, once the vendee has reached the point at which his land
sale contract is converted into a mortgage, 64 or the contract is pre-
paid, he would presumably be safe from rejection by the vendor’s
trustee in bankruptcy. But just as with the non-bankruptcy case law,
it remains for these statutory provisions to be tested in bankruptcy
court.

61 When 40% or more of the original cash price of the property shall have
been paid, the vendee shall have the right (if no earlier period be fixed by
the contract) to demand a conveyance of the premises mentioned in the con-
tract, on the condition that he execute a purchase money mortgage to the
vendor, or to a mortgagee procured by the vendee. MD. CODE ANN. art. 21,
§ 112(7) (1966).


63 "A buyer shall be entitled to prepay all or any part of the balance due on any
real property sales contract with respect to the sale of land which has been subdivided
into a residential lot or lots which contain a dwelling for not more than four hundred
families." CAL. CIV. CODE § 2985.6 (West 1968).

64 This may also happen when the installment contract is used as an interim device.
The vendor retains title until the vendee has paid enough, under contract terms, to
transform the transaction into an executed sale, in which the remaining indebtedness is
secured by a trust deed. Warren, supra note 13, at 609.
D. The Interstate Land Sales Full Disclosure Act

The reporting requirement of the Interstate Land Sales Full Disclosure Act may operate as a protective device and give the vendee enough knowledge about his investment to enable him to avoid the problems that might arise if his vendor takes bankruptcy. The Act provides that the vendor must furnish the vendee with a property report, stating, \textit{inter alia}, the consequences to the vendee in the event that: (1) the vendor becomes bankrupt; (2) the vendor's blanket mortgage is foreclosed; or (3) the vendor defaults on any lien obligation.\textsuperscript{65} In addition, the vendor must state whether the vendee's down payment and installment payments will be placed in escrow.\textsuperscript{66} If the vendor fails to furnish a property report to the vendee within 48 hours before the signing of the contract, the vendee may cancel and obtain a refund of payments. If the vendor does provide a report, but it is one that contains "an untrue statement of a material fact" or omits "to state a material fact," the vendee may bring an action for damages.\textsuperscript{67} Of course, if the vendor is bankrupt, an action for damages is not guaranteed to permit the vendee a return of his payments.

Although laudable as a remedy for fraudulent practices in interstate land sales, the foregoing provisions, in their current form, will not help the vendee when the vendor has entered bankruptcy. It is not a regulatory statute. As the Act's sponsor, Senator Williams, pointed out: "The only purpose of this legislation is to give the purchaser the necessary information upon which he can make his own investment decision."\textsuperscript{68}

In Summary, it is evident that there are no tested legal theories

\footnotesize{\textsuperscript{65} 24 C.F.R. § 1710.110, §§ 4, 5 (1971).\textsuperscript{66} Id. at § 1710.110, § 8 (1971).\textsuperscript{67} Housing and Urban Development Act of 1968, Pub. L. No. 90-448, tit. XIV § 1418, 82 Stat. 590.\textsuperscript{68} S. REP. NO. 1123, 90th Cong., 2d Sess. (1968). The Department of Housing and Urban Development admits:

The law is designed to afford the prospective buyer a full and fair disclosure of the facts about a subdivision offering. But, if the buyer ignores or fails to read and understand the property report, the consumer protection aspects of the law are virtually negated. The law will light the threshold but not unlock the door. U.S. DEPT. OF HOUSING AND URBAN DEVELOPMENT, CONSUMER PROTECTION: INTERSTATE LAND SALES, HUD-15-F (2) (Aug. 1970).

For a copy of this pamphlet, send to: Office of Interstate Land Sales Registration, U.S. Dept. of Housing & Urban Development, Washington, D.C. 20411.}
which the vendee can use to protect himself fully against the rejection of the contract by the vendor's trustee in bankruptcy. Several arguments are available, such as the lien or conversion theory, but it is uncertain whether the bankruptcy court would accept them. Consequently, in order to ensure that the vendee be legally protected, further legislative and judicial remedies should be contemplated.

IV. PROPOSED REMEDIES

Of the proposals to be considered, the most effective remedy would be congressional amendment of section 70(b) of the Bankruptcy Act. This would offer complete protection to the vendee and provide uniformity among the states. Alternatives to amendment of the Act are increased state regulation, more extensive use of the Interstate Land Sales Full Disclosure Act, requiring placement of payments and title in escrow, and bonding of the vendor. But none of these alternatives would provide the total solution which amendment offers.

A. Amendment of the Bankruptcy Act

To protect the vendee in a land sale contract when the vendor's trustee in bankruptcy rejects, section 70(b) should be amended to include the following proviso: "provided, however, that the trustee of a vendor in an executory contract for the sale of land shall not reject such contract where the vendee is continuing to meet the obligations of the contract." The purpose of the proposed amendment is to prevent the trustee from rejecting an executory land contract unless the vendee has breached. The vendee would thus be permitted to retain possession of the land and complete his performance; the vendee would lose his right to possession and to continue performance only if he were in breach of the contract. Moreover, these rights would become available to the vendee once he had begun complying with the contract terms and there would be no need for the bankruptcy court to determine whether the vendee had substantially performed at the time of the vendor's bankruptcy.

69 The amendment would not create administrative problems for the trustee. Even if the contract had several years remaining, the trustee would be able to sell this asset — the right to receive payments from the vendee — at a discount and distribute the resulting proceeds to creditors.

Assumption of an executory contract, unlike rejection, must be passed upon by the court because it involves the continuation of liabilities which constitute an expense to the bankrupt's estate. 4A COLLIER, supra note 6, § 70.43(5), at 529.
The vendee's right to possession, contingent upon his tendering payment in accordance with the contract, provides him with protections similar to those of a mortgagor.\(^7\)

The proposed amendment would have to overcome a number of objections. Initially, creditors would argue that the trustee should be able to reject an executory contract in order to allow the trustee to negotiate a better price for the land and eventually to give greater satisfaction to the estate's creditors.\(^7\) Supporters of the amendment would contend that a different rationale applies where the vendor, normally a creditor, is the bankrupt. First, the contract is no longer executory as to the vendor — except for his conveying the title when the vendee completes performance — and therefore should be free from the trustee's power of rejection. Second, an already profitable contract is not a burden on the estate. Third, equity favors the vendee who is willing to meet his contract obligations. Allowing a greater profit than originally contemplated simply to benefit the creditors, at the expense of a non-breaching vendee, is unjust.\(^7\)

But the most compelling justification for the amendment lies in its economic consequences. The amendment would no longer allow the vendee to be used as a resource by the trustee to increase the bankrupt's estate, and the cost of the bankruptcy would be completely borne by commercial creditors. This would increase the creditors' incentive to deal only with sound vendors and would entirely remove this "policing" function from the vendees, who occupy the poorest position to exercise such control.\(^7\) Moreover, the commercial creditors are capable of distributing the risks of a vendor's bankruptcy, but the vendees are not.\(^7\)

The creditors can simply pass on

\(^{70}\) Whether the vendee should have an equity of redemption like the mortgagor's is a separate question. It is not unreasonable to include it, although one can argue that the vendee should be bound to the terms of the contract regarding timely payment.

\(^{71}\) See 4A COLLIER, supra note 6, ¶ 70.43 (2), at 521-25. The thrust of the entire Bankruptcy Act is to enable the trustee to marshal assets of the bankrupt debtor for the benefit of the creditors. To accomplish this purpose the trustee is free to assume only those liabilities which involve profit to the estate and which the estate can afford to administer.

\(^{72}\) It can be argued that the vendee, particularly where he is a consumer, is entitled to a more lenient application of a bankruptcy statute written for the needs of commercial creditors.

\(^{73}\) Normally the vendee would not deal with land vendors as extensively as might a creditor. Consequently, the vendee is at a disadvantage in keeping track of the vendor's financial integrity. When the vendee is a consumer, it is unrealistic to assume he would have any significant impact as a financial "policeman."

\(^{74}\) Only if a vendee were widely engaged in purchasing land could he begin to distribute the risks of a vendor's bankruptcy in a smooth fashion. But a vendee dealing on this scale might not even use land sale installment contracts. With the small scale
the increased costs of vendor bankruptcy by raising the cost of credit.\textsuperscript{75} Most likely, the vendees would ultimately pay for most of this increase in the cost of credit. But they would be paying as a group, and therefore the risks of bankruptcy would be distributed evenly and rationally — rather than falling completely on a small and arbitrary group of vendees.

Against these attractive economics, one could only argue that the proposal interferes with the normal role of the bankruptcy trustee.\textsuperscript{76} The trustee may have several alternative ways of performing his function of maximizing the assets of the bankrupt's estate. These alternatives may or may not require available cash. But if cash is required, then the trustee's inability to reject an executory land sale contract and sell the land for cash at a higher price may hinder the trustee's disposition of the estate's other assets. Especially in a reorganization proceeding, it may be best to reject executory land sale contracts. The ultimate consideration in a reorganization is to preserve the business, and the funds available to accomplish this might be available only by rejecting the land sale contracts and selling the land for its market value.\textsuperscript{77}

To counter the argument that the amendment would impede the trustee's proper function, the supporters of the proposal must rely primarily on the beneficial economic consequences that would result from its enactment. In addition, regardless of the economic effects of the amendment, it is still a questionable practice to penalize the vendee in order to provide an occasional added impetus for a successful reorganization. The vendee in our situation is not in breach

purchaser, and particularly with the consumer, the present law allows no feasible way to distribute these risks.

There is another way that risks might be reallocated. As in the securities industry, self-insurance by the vendors could become prevalent if the vendors' need for financial stability increased sufficiently.

\textsuperscript{76} This possibility may be unduly pessimistic. If the creditors were prompted by the amendment to refuse to deal with the more unstable vendors, the number of bankruptcies might decrease, allowing the creditors to make the same rate of return without increasing the cost of credit. This same result could be achieved by stricter legal control over the vendor's finances.

\textsuperscript{77} The trustee's function is to assume or reject an executory contract. If he takes no action, the contract is deemed to be rejected under section 70(b) of the Act. Situations occur in which the trustee might take other actions. For example, if the vendee is in default, the vendor's trustee would enforce or abandon the bankrupt's claim. 4A Collier, \textit{supra} note 6, \textsection 70.43 (2), at 522.

\textsuperscript{77} The later amendments to the Bankruptcy Act were based on the theory that business should be preserved where possible. H.R. 8046, 75th Cong., 3rd Sess. 8680 (1938). In order to "preserve" the business, it is quite possible that the trustee would choose to assume executory land sale contracts. In this manner, the business might be received better by future vendees and stand a greater chance of a successful reorganization.
of the contract and it is unfair to him to use his funds as the basis for reviving the vendor.\footnote{78}

Even if passed, there is a potential barrier that could limit the amendment's effectiveness. The purpose of the amendment could be undercut if the parties agreed to a contract clause which required termination of the agreement upon the vendor's bankruptcy. Section 70(b) permits enforcement of termination clauses for leases, and the bankruptcy courts have given effect to such claims.\footnote{79} A similar position with regard to land sale contracts could render the amendment meaningless if this type of clause proliferated.\footnote{80} But courts could reasonably refuse to enforce a termination clause in the land sale contract. First, the termination clause could be held ineffective as contrary to the policy of the proposed amendment.\footnote{81} Second, the vendee wants to continue the contract, unlike the lessee who wants to be free from the obligations of a burdensome lease.\footnote{82} Moreover, although the Bankruptcy Act permits lease termination clauses, it also provides that the lessor's trustee cannot deprive the lessee of his estate.\footnote{83} In Cohen, "estate" meant possession until the lessee received payment on his lien. By analogy, the vendee who has relied upon possession under the contract should also have an "estate" — \textit{i.e.}, the right to continue possession as long as he performs his obligations.\footnote{84}  

\footnote{78}{The imbalance of the equities is particularly severe where only a few additional reorganizations would be successful because the vendee's contract was rejected and the land resold. But even if one does find these arguments against the proposed amendment convincing, there are possible compromise positions that would be somewhat less inequitable. For example, the vendee could be allowed to obtain title to the land by paying the current appraisal value, minus the full amount of the payments already made (adjusted for the cost of credit). This approach would not satisfy the arguments either for or against the amendment, but simply represents a possible "political" compromise.}

\footnote{79}{J. MacLachlan, \textsc{Handbook of the Law of Bankruptcy} 173-74 (1956).}

\footnote{80}{It is conceivable that the creditors would require such clauses as a condition to extending credit.}

\footnote{81}{In the case of a lease, the Act allows termination clauses because both parties may wish to be freed upon bankruptcy. But there is no reason why the vendor's bankruptcy should affect a vendee's desire to own the land in question.}

\footnote{82}{J. MacLachlan, \textsc{supra} note 79, at 174.}

\footnote{83}{See notes 44-46 \textsc{supra} \& accompanying text.}

\footnote{84}{The rationale for the lease provision in section 70(b) was given by the court in \textit{In re Freeman}, 49 F. Supp. 163, 165 (S.D. Ga. 1943): In case of sale by the trustee, a purchaser assured of a reasonable rent for a fixed term will be satisfied, and, meanwhile, a tenant (who is an innocent party) who may have made his business plans on the assumption he would occupy the premises for the term is not treated inequitably.}
B. Increased Regulation by the States

In the absence of an amendment to section 70(b) of the Bankruptcy Act, the states can play a more active role in correcting the inequity to land sale vendees when the vendor files for bankruptcy. Although state law cannot supersede the federal Bankruptcy Act, a state can affect the outcome in bankruptcy court by controlling the law regarding the vesting of title to property. A state can achieve a salutary result by converting the land sale contract into a mortgage by new legislation. Ohio law, for example, appears to convert the land contract into a mortgage when the vendee has paid in accordance with the terms of contract for five years or has paid more than 20 percent of the purchase price. If the bankruptcy court followed the conversion statute, the trustee would be powerless to reject absent a breach by the vendee.

In addition to conversion statutes, states could provide protection to a vendee by legislating controls to create a more financially solvent vendor who would be less likely to take bankruptcy. For example, Ohio prohibits the vendor's own mortgage from exceeding the balance due on the vendee's contract without the latter's consent. This statute should discourage potential developers from entering the business unless they can secure reasonable mortgages and adequate financial backing.

In addition to providing this kind of indirect financial regulation, a state could legislate more directly and prohibit a company

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86 OHIO REV. CODE § 5313.07 (Page Supp. 1969). The statute also provides the vendee in default with a thirty day grace period before the vendor can bring forfeiture proceedings. OHIO REV. CODE §§ 5313.05-06 (Page Supp. 1969). Although this statutory grace period appears to give the vendee a thirty day equity of redemption, the vendor's trustee in bankruptcy can still reject the contract.
87 OHIO REV. CODE § 5313.02 (Page Supp. 1969) provides:
(A) . . . The contract shall contain at least the following provisions . . .
(B) No vendor shall hold a mortgage on property sold by a land installment contract in an amount greater than the balance due under such contract, except a mortgage which covers real property in addition to the property which is the subject of the contract where the vendor has made written disclosure to the vendee of the amount of such mortgage and the release price, if any, attributable to the property in question.
No vendor shall place a mortgage on the property in an amount greater than the balance due on the contract without the consent of the vendee.
from selling land by installment contracts if it is under-financed or uses questionable business practices. For example, Ohio has declared that a vendor's dealing in "grossly unfair terms" violates the Interstate Land Sales Full Disclosure Act's antifraud provisions. And if the vendor fails to furnish the division of securities "such other information as the division requires," (i.e., as to the vendor's financial condition), the state might be able to deny the vendor a license, as well as bring the other enforcement mechanisms to bear. Also, under Ohio law, if a practice works "material prejudice" to the vendee, a court of common pleas may appoint a receiver with the power to "sell, convey and assign such property, and to hold and dispose of proceeds." 

Florida has authorized its Land Sales Board to issue cease and desist orders for violations of the Florida Uniform Land Sales Practices Law. Purchasers are accorded civil remedies when the subdivider disposes of land in violation of the Act, and vendors face criminal penalties for willful violations. New York's protective approach creates a trust that segregates the vendee's payments from the vendor's other assets. The funds in the trust are applied toward clearance of title to the land to be conveyed to the purchaser. The vendee is protected if bankruptcy occurs because the vendor's trustee cannot reach the payments placed in trust and must allow the vendee to perform. This approach would expand upon the Interstate Land Sales Full Disclosure Act, which seeks to limit fraudulent land sales but does nothing to correct the problem caused by good faith, but under-financed developers.

C. Requiring Escrow Agreements Under State Law and the Disclosure Act

State laws could also be modified to require the interstate vendor to make escrow arrangements a condition of doing business (i.e., ob-

80 OHIO REV. CODE § 1707.33(D) (Page 1953).
81 OHIO REV. CODE § 1707.33(B)(10) (Page 1953).
82 OHIO REV. CODE § 1707.27 (Page 1953).
84 FLA. LAWS ch. 67-229, §§1-35 (1967). The statute was formerly titled the Florida Installment Land Sales Law, which had authorized the earlier Florida Installment Land Sales Board. See generally Boyer, Real Property Law 22 U. MIAMI L. REV. 278, 280 (1967).
86 N.Y. REAL PROP. LAW, art. 9-A, § 338 (4) (McKinney 1968).
87 Id.
taining a license) in the state where the vendee resides. Escrowed the payments would at least protect the installments of the vendee that had already been paid.

Already, the Interstate Act implicitly appreciates the protection which escrowed offers the vendee, for escrowed is part of the method in which the vendor may obtain an exemption from the Act.\(^7\) The exemption is available and the time of sale is considered the effective date of the conveyance if: (1) the contract of sale requires delivery of a deed to the purchaser within 120 days following the signing of the sale contract; and (2) any earnest money deposit or other payment on account of the purchase price, made by the purchaser prior to the effective date of the conveyance, is placed in an escrow account.\(^8\) Although this provision is optional, similar conditions requiring the vendor to convey title and place the vendee’s payments in escrow would offer the vendee valuable safety in his transaction with the vendor. The purchaser would note such arrangement in the property report, and title would remain with the vendee. Payments would be made to a bank in the vendee’s state.\(^9\)

While it has been held that the vendor’s trustee cannot reject an executory land contract and simultaneously retain funds deposited in escrow,\(^10\) whether placement of title in escrow gives the vendee the right to continue performance is an undecided issue.\(^11\) Regardless of the bankruptcy court’s interpretation of that issue, escrowed funds would force the vendor to obtain other funds to finance his mortgage and would prevent the under-capitalized developer from entering the market place. More importantly, the vendee who performs would have protection for his payments, and possibly for title as well.

D. Bonding Requirements for Land Sale Vendors

Bonding is the least desirable solution, but one which would provide the vendee with some protection.\(^12\) Vendors could be re-

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\(^8\) Id. at § 1710.10(j) (2) (ii).

\(^9\) This escrow device, known as an "impound account," can be utilized in Ohio. OHIO REV. CODE § 1707.33 (E) (Page 1953).


\(^11\) Escrow and trust law would seem to dictate that when a title is placed in escrow it is no longer a part of the vendor’s estate, and consequently if the vendor takes bankruptcy the vendee should still be entitled to continue performance.

\(^12\) Performance bonds have been required for chartered air carriers since January
quired to obtain surety bonds to guarantee performance of the contract. But unfortunately, "performance" would mean only a return of the total payments made by the vendee when bankruptcy intervened.

Like an escrow arrangement, bonding insurance creates a fund outside the assets of the vendor's estate, so that the vendee can still recover his payments if bankruptcy occurs, even though the estate may be penniless. The vendor's general creditors might argue that they should be entitled to a share of such a fund since it arises out of an executory contract with the vendor, but in many situations it will be the vendee who has paid for the bonding. Although the cost of bonding would likely be passed on to the vendee, when balanced against the alternative risks it becomes a price worth paying.

V. Conclusion

Today the basic problem is that the land sale contract, absent a trust arrangement or a remedial statute, is executory. Unlike a mortgage, it may be rejected by the vendor's trustee in bankruptcy. This is inequitable because the contract is no longer executory as to the bankrupt vendor. Moreover, the vendee, whether commercial or consumer, is least able to "police" the vendors and is in no position to distribute the costs of the vendor's bankruptcy. The vendee who continues his payments should have the right to obtain full title to the property.

The current heavy-saturation advertising campaigns of many land developers — aimed at unsophisticated people seeking lots for recreation or retirement — have created a need for relief beyond mere rescission for fraud. The need exists for legally binding devices to enable the vendee to complete performance and obtain title.

Other creditors of the vendor may raise the objection that once the Bankruptcy Act has been amended as proposed, such legislation may be carried too far and lead to a general diminution of the trustee's function. But the proposed legislation seems reasonable, and, overall, it should be a beneficial force both in keeping under-financed vendors out of the market and in distributing the effects of bankruptcy in a rational manner. The intent is not to close down commercial vendors or the land development business. Far from

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1971, after bankrupt carriers stranded passengers in Europe. The tour operator is now required to furnish a surety bond for twice the amount of the charter price of the air transportation supplied in connection with the tour. This requirement is specified in the Civil Aeronautics Board regulations governing charter trips. 14 C.F.R. § 378.16(a) (1971). See id. at § 378.16(b) for alternatives to bonding.
it — if the vendee can go forward on his land sale contract knowing that he will be protected even from the vendor's bankruptcy, both the commercial vendor and the consumer land sale business would benefit.

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