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## SUMMARY

Whenever a real estate transaction involves financing, a Bond for Deed/Trust Agreement should be considered as a alternative methods of financing.

If the existing mortgage loan(s) are attractive, but are thought to be “non-assumable”, remember that the Louisiana Bond for Deed/Trust Agreement allows you to legally avoid the “due on sale” clause. Under a Bond for Deed/Trust Agreement the purchaser can take over the “non-assumable” loan, and you can still “close the deal”.

Additionally, whenever there is owner-financing, the Seller should consider using the Bond for Deed/Trust Agreement in the event of a default by the Purchaser, the forty-five day notice and the ease of cancellation with the Bond for Deed/Trust Agreement are much quicker and much less expensive than a judicial foreclosure proceeding to regain title.

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The Louisiana Real Estate Commission has certified him as an instructor for its continuing education requirements. He is a member of the Louisiana Bar Association, Jefferson Parish Bar Association and past member of the House of Delegates, Louisiana State Bar.

A major portion of his practice is devoted to real estate and he has closed several hundred Bond for Deed/Trust Agreement Contracts.

This booklet is designed to provide general information in regard to the subject matter covered. It is distributed with the understanding that it should not be utilized as a substitute for professional legal or accounting advice in specific situations. If legal advice or other expert assistance is required, the service of a professional should be sought.

**The Louisiana BOND FOR DEED/TRUST AGREEMENT Contract**  
*by Richard E. Regan and Richard J. Regan*

The "Bond for Deed/Trust Agreement" contract would be more easily understood if it were known simply as a "Contract for Deed" .

A "Bond for Deed/Trust Agreement" is quite simply an Agreement to Purchase, or a contract for the sale of real property, almost invariably including an Occupancy Agreement.

**APPLICABILITY**

It is suggested that such a "Bond for Deed/Trust Agreement" contract should be considered for use by a Seller, Buyer, Broker or Agent whenever:

1. The purchaser cannot qualify to obtain a new loan or to assume the existing loan, but the seller is satisfied with the purchaser's credit.
2. The property does not qualify for a new loan, but the purchaser is satisfied with the price and condition of the property.
3. The required "closing costs" to obtain a new mortgage loan are prohibitive.
4. Permission to assume is conditioned upon payment of an unreasonable transfer fee (such as 1% or 2% of the loan balance) and/or in an increase in the interest rate on the existing loan.
5. The "due on sale" clause in a mortgage (or the La. statutory "due on sale" found in R.S. 6:833) is used by the lender to prohibit any assumption of the existing loan(s).
6. The seller desires to maintain the security of retaining title and eliminating the legal expense and delays of a judicial foreclosure in the event of a default by the purchaser. This is particularly beneficial if the seller finances a portion of the purchase price.
7. The seller agrees to allow the purchaser to "assume" or take over responsibility for the mortgage payments, but requires that the purchaser must refinance and pay off the existing mortgage loan within a specified period of time (such as within five years).
8. Any combination of the above.

## LEGAL BASIS

An understanding of the "Bond for Deed" requires a review not only of the applicable statutory provisions, but also the various State and Federal judicial decisions interpreting and applying the statutes.

The "Bond for Deed" contract is authorized and governed by ACT No. 169 enacted by the Louisiana Legislature in 1934. This Act is found in the Louisiana Revised Statutes, Title 9, Sections 2941 through 2947. A brief review of the individual statutory provisions and the applicable court decisions should dispel the current myths and fears regarding the use of "Bond for Deed" when confronted with the "non-assumable" mortgage loan.

### **R.S. 9:2941. "Bond for Deed" defined.**

A bond for deed is a contract to sell real property, in which the purchase price is to be paid by the buyer to the seller in installments and in which the seller after payment of a stipulated sum agrees to deliver title to the buyer.

#### **Notes of Decisions**

Trichel v. Home Ins. Co. (La. Sup. Ct. 1924) 99 So. 403  
Lindhardt v. Marrero Land and Improvement, App. 1962, 137 So.2d 387  
Gray v. James, App. 1987, 503 So.2d 598

**Comment:** These cases establish that any agreement, irrespective of its title, which provides that the purchase price for real property is to be paid in monthly installments and that title is to be conveyed after the payment of all stipulated installments, is a "Bond for Deed" and not an act of sale.

### **R.S.9:2942. Unlawful to sell encumbered real property by Bond for Deed without guarantee to release on payment.**

It shall be unlawful to sell by Bond for Deed contract, any real property which is encumbered by mortgage or privilege without first obtaining a written guarantee from the mortgage and privilege holders to release the property upon payment by the buyer of a stipulated mortgage release price, with which agreement the secured notes shall be identified. The agreement shall be recorded in the mortgage records of the parish where the property is situated before any part of the property is offered for sale under Bond for Deed contracts. The provisions of this Part likewise shall apply to any property offered for sale by Bond for Deed contract which may be subsequently mortgaged or encumbered by a privilege.

#### **Notes of Decisions**

First Federal Savings & Loan v. Botello, 725 Fed 2d 350 (1984)  
Scott v. Apgar, (La.Sup.Ct. 1959) 113 So.2d 457

**Comment:** These cases clearly establish that neither the “written guarantee” nor any type of consent of permission from the mortgage holder(s) is required, provided the purchaser is made aware of the underlying mortgage(s) and provision is made in the Bond for Deed contract to insure that the payments made by the purchaser are applied to payment of the underlying mortgage(s).

The Botello case is especially significant. After the Savings and Loan refused their request for the sale of the property on an assumption, the buyer and seller executed a Bond for Deed contract. The S&L then filed a foreclosure action claiming a violation of their “due on sale” clause.

The Federal Fifth Circuit Court of Appeal made an extensive review of Louisiana law, cited numerous Louisiana cases, and concluded that the contract to sell (or Bond for Deed) clearly does not violate the “due on sale” clause. Accordingly, the decision of the Federal District Court dismissing the plaintiff’s foreclosure action was affirmed by the United States Court of Appeal.

**R.S. 9:2943. Method of Payment.**

All payments by the buyers under Bond for Deed contract of property then or thereafter burdened with a mortgage or privilege, shall be made to some bank authorized to do business in this state, which shall have been designated as the escrow agent for all parties interested in the contract. The payments shall be distributed by the escrow agent between the seller and the holder of the mortgage or privilege, in such proportion as the secured obligation shall bear to the purchase price in order to insure the buyer on unencumbered title when all payments have been made as provided in the Bond for Deed contract.

**Notes of Decisions**

St. Landry Loan Co. V. Etienne, App. 1969, 227 So.2d 599.

**Comment:** This case holds that a failure to designate a bank as an escrow agent does not invalidate a Bond for Deed contract explaining that the purpose of the escrow agent is to assure a proper apportionment of the buyer’s payments between the seller and the mortgagee(s). Buyer and Seller should employ a commercial escrow agent experienced in handling Bond for Deed/Trust Agreement contracts. The escrow agent’s services include the all important functions of prompt forwarding of mortgage payments, immediate notice in the event of a default in payments and proper reporting of interest as required by the Internal Revenue Service.

**R.S. 9:2944. Timely payment of installments precludes foreclosure; change of description upon foreclosure.**

The payments due by buyers under Bond for Deed contracts, shall preclude the holder of any secured notes from foreclosure, but the failure of the buyers to make payments as they fall due, shall secure to the holder of the notes the right to foreclose when the notes become due and are unpaid. In the event of a foreclosure under such circumstances, the description as contained in

the act of mortgage may be changed so as to leave unaffected those lots or tracts of land on which payments have been kept up and so as to effect and adjudicate under the foreclosure only such lots as may be in default of payments and other lots not sold under Bond for Deed contracts.

**Comment:** This section is self-explanatory. It protects the buyer and prohibits foreclosure by the mortgage holder provided the buyer makes timely payment of the installments as required in the Bond for Deed/Trust Agreement contract.

#### **R.S. 9:2945. Cancellation of Bond for Deed upon default.**

If the buyer under a Bond for Deed contract shall fail to make the payments in accordance with its terms and conditions, the seller, at his option, may have the Bond for Deed cancelled by proper registry in the conveyance records, provided he has first caused the escrow agent to serve notice upon the buyer, by registered mail at his last known address, that unless payment is made as provided in the Bond for Deed, within forty-five (45) days from the mailing of the notice, the Bond for Deed shall be cancelled. Where there is no mortgage or privilege existing upon the property, and the buyer shall be in default, the seller shall exercise the right of cancellation shall not exceed the legal rate per hundred words fixed for conveyance registries.

#### **Notes of Decisions**

Lindhardt v. Marrero Land and Improvement, App. 1962, 137 So.2d 387  
Williams v. Dixie Land Co., La.Sup.Ct. 1957, 93 So.2d 185

**Comment:** These cases hold that the forty-five day notice of default is mandatory.

In practice, the forty-five day notice can be sent either by registered or certified mail and, if provided in the contract, may be served either by the seller or by the escrow agent.

Frequently, buyer and seller agree to sign a mutual cancellation and mutual release. This can be done at any time and is similar in practical effect to the "dation en paiement" or "deed in lieu of foreclosure".

There have been a number of cases involving the amount to be forfeited by the buyer in the event of default. In the recent case of Gray v. James, La. App. 1987, 503 So.2d 598, the court prohibited forfeiture in an amount found to be "inequitable and unreasonable".

In our Bond for Deed/Trust Agreement contracts, it is specifically provided that the buyer must forfeit an amount equal to the fair reasonable rental value, compensation for removing the property from the market, reimbursement of broker's commission, closing fee, costs, transaction taxes, and Federal and State income taxes.

**R.S. 9:2946. Unlawful to require mortgage notes when property encumbered; act of sale.**

It shall be unlawful for any seller in a Bond for Deed contract to require promissory notes to represent the purchase price or any portion thereof, if the property should be encumbered with a mortgage or privilege. Upon the payment to the escrow agent of the sum necessary to release the property, the seller shall execute a deed to the buyer and may then exact one or more mortgage notes to represent any portion of the unpaid purchase price. Should the property not be encumbered with a mortgage privilege, and a note has been executed to represent all or a portion of the price under the bond for deed contract, when the buyer shall become entitled to demand a deed, the seller shall execute an authentic sale and the notary passing it shall require the production of the note or notes and shall cancel them at the time of passing the sale.

**Comment:** The seller does not need promissory notes, as the Bond for Deed/Trust Agreement contract makes provisions for the payments required by the purchaser and the application of all payments to the payment of the underlying mortgage(s) and/or payments to the seller. Our contracts also provide for late charges, specific performance, attorney's fees, insurance, repairs, termite contract, etc.

**R.S. 9:2947. Penalty for violations.**

Any person who sells by Bond for Deed contract any real property encumbered by mortgage or privilege without first obtaining and recording the guarantee required by R. S. 9:2942, shall be fined not more than one thousand dollars, or imprisoned for not more than six months, or both.

Any seller in a Bond for Deed contract of property encumbered with a mortgage or privilege, who requires promissory notes to represent the purchase price or any portion thereof, shall be fined not more than one thousand dollars, or imprisoned for not more than six months, or both.

**Notes of Decisions**

Scott v. Apgar, (La.Sup.Ct. 1959) 113 So.2d 457  
First Federal Savings & Loan v. Botello, 725 Fed. 2d 350 (1984)

**Comment:** In the Scott case the Louisiana Supreme Court determines that the written guarantee required by R.S. 9:2942 is solely for the protection of the purchaser. Accordingly, there is no criminal violation provided the parties have substantially complied with statutory law or court decisions, particularly with respect to provisions for payment of the underlying mortgage(s) and appointment of an escrow agent.

Specifically, in the Botello case (725 Fed.2d 350), not only was there no written guarantee, but the mortgage holder had refused to give its consent to an assumption. Nevertheless, the buyer and seller executed a Bond for Deed contract and the mortgage holder's challenge to the Bond for Deed contract was dismissed with not even the suggestion that there had been any criminal violation. Again, these cases establish that both the Federal and State courts approve the use of the Bond for Deed.

## PRACTICAL CONSIDERATIONS

The practical effects of executing a Bond for Deed/Trust Agreement contract are very similar to an "assumption" or a sale "subject to" the underlying mortgage(s). The principal difference is that title is not yet transferred.

1. You may write an Agreement to Execute a Bond for Deed/Trust Agreement on a standard Agreement To Purchase/Sell form with the simple, but necessary modification that the parties agree to purchase/sell under a Bond for Deed/Trust Agreement contract.

2. Preferably, you should use an Addendum Form which has been tailored to provide for a Bond for Deed/Trust Agreement contract. A suggested form for your use is supplied with this booklet.

3. After an explanation of the "Bond for Deed/Trust Agreement" and the fact that the Seller will convey title only after the purchase price is paid, you prepare your agreement which provides:

Price of \$\_\_\_\_\_ Dollars on term of \$\_\_\_\_\_ cash and approximate balance of \$\_\_\_\_\_ under La. Bond for Deed/Trust Agreement contract at \$\_\_\_\_\_ per month for \_\_\_\_\_ months or years. The remaining part of the Agreement is written just like an Assumption contract.

4. There can be existing 1<sup>st</sup>., 2<sup>nd</sup>., etc. mortgages.

5. The Seller can owner finance all, or a portion, of his equity.

6. The Seller can "Wrap" around existing mortgages.

NOTE: a "wrap" is not a Bond for Deed/Trust Agreement and will NOT by itself solve the problem of a "due on sale" clause.

7. The real estate commission is paid at the closing of the Bond for Deed/Trust Agreement contract.

8. ESCROW AGENT: The law requires the use of a third party escrow agent for the protection of all parties. The designated escrow agent is responsible for the distribution of all payments, notices to all parties in the event of late payment or non-payment, and sending out the proper interest notices required by the I.R.S. The law permits the parties to use any mutually agreeable third party. However due to the legal responsibilities involved, we suggest the parties employ the services of an experienced escrow agent.



## FREQUENT QUESTIONS

1. **Assignment:** The Bond for Deed/Trust Agreement contract is assignable to a third party. Typically such an Assignment is made by the Purchaser to a third party. Typically such an Assignment is made by the Purchaser to a new Purchaser who takes over the rights and responsibilities of the original Purchaser.
2. **Bankruptcy:** In the event the Seller files a bankruptcy action, the Purchaser is protected by the Bankruptcy Code, 11 U.S.C., Sec. 365 (i) and the law as applied in the case of *In Re Smith*, 71 B.R. 754 (Bankruptcy M.D. La.)
3. **Death:** The death of a Seller or Buyer does not affect the validity of a Bond for Deed/Trust Agreement. As a "heritable contract" under La. Civil Code Articles 1765 & 1984, it is effective by or against the heirs or estate of a decedent..
4. **Enforceability:** In the event of default by either party, the other party may sue for "Specific Performance". Additionally the Seller may have the Bond for Deed/Trust Agreement cancelled in accordance with the provisions of R.S. 9:2945 as explained above. In such event, **the Seller need not file a foreclosure suit to reacquire title of the property.**
5. **Homestead Exemption:** The Homestead Exemption is not available in most Louisiana Parishes.
6. **Income Tax Consequences:** The I.R.S. treats a Bond for Deed/Trust Agreement the same as a Sale. Accordingly, the determination of gain or loss by the Seller and deductions for interest or depreciation expense by the Purchaser is treated the same as if there had been an ordinary sale. The case law on this point is found in :
  - (1) *CIR v BAERTSCHI*, 412 F.2d 494 (6 Cir. 1969)
  - (2) *DITTMERS v CIR*, 430 F.2d 1019 (6 Cir. 1970)
  - (3) *WAYNE v CIR*, 518 F.2d 655 (10 Cir. 1975)
  - (4) *HELVERING v F & F LAZARUS*, 60 SUP. Ct. 290 (1939)
7. **Occupancy:** Along with the responsibility for repairs, maintenance, etc., is transferred to the Purchaser at the closing of the Bond for Deed/Trust Agreement contract.
8. **Power of Attorney:** Our Bond for Deed/Trust Agreement contract provides that the Seller give a power of attorney to the named Escrow Agent empowering the Escrow Agent to transfer title to the subject property in accordance with the provisions of the contract. This protects the Purchaser in the event the Seller has moved away or it is otherwise inconvenient for the Seller to appear at Act of Sale after the Purchaser has made all payments.
9. **Property Insurance:** Is carried by the Seller or Purchaser in the names of all parties - Seller, Purchaser, and Mortgagee(s).

10. **Recordation:** The Bond for Deed contract is recorded in both the conveyance and mortgage records. Additionally, we include a special mortgage in favor of the Purchaser to protect the Purchaser's rights in the event of a subsequently arising encumbrance, such as a judgment or an I.R.S. tax lien. The rights of the Purchaser are superior to subsequently recorded inscriptions. The Trust Agreement is secured by a Multiple Indebtedness Mortgage filed in the mortgage records.

11. **Title Insurance:** Is available to insure the validity of the Seller's title that is to be conveyed to the purchaser under the Bond for Deed/Trust Agreement-subject to the express condition that the Purchaser pay the amounts contracted for in the Bond for Deed/Trust Agreement.

12. **Title Transfer:** The Purchaser can take title in his own name at any time by paying the balance due on the Bond for Deed/Trust Agreement. Mostly commonly this occurs by refinancing (if interest rates go down) or reapplying to qualify for an assumption of the existing mortgage.

### EXAMPLE No. 1

Smith agrees to sell to Jones under a Bond for Deed/Trust Agreement.

Purchase price:	\$100,000.00
Cash portion: (paid at closing of Bond for Deed/Trust Agreement)	<u>\$ 20,000.00</u>

Balance owed to Mortgage Company:	\$ 80,000.0
(Mortgage rate 7% per annum for 27 years remaining)	

Jones agrees to pay monthly the amount necessary to keep current principal, interest, taxes and insurance (plus escrow agent's service charge).

Whenever Jones pays off the \$80,000.00 mortgage balance, title is transferred to Jones. Jones may continue monthly payments over the 27 years remaining or prepay the balance at anytime, normally by refinancing if rates decrease.

### EXAMPLE No. 2

Smith and Jones agree at a price of \$100,000.00. Jones has only \$15,000.00 cash to put down and Smith has \$20,000.00 equity. (mortgage balance of \$80,000.00 with payments of \$900.00 month).

Smith agrees to owner finance the remaining \$5000.00 at 10% interest for five years with a monthly payment of \$106.00.

In this example, Jones would pay \$15,000.00 at closing and the Bond for Deed/Trust Agreement would require Jones to pay a total monthly payment of \$1006.00 for the first five years, thereafter reducing to \$900.00/month.

very month, for the first five years, the Escrow Agent would forward \$900.00 per month to the mortgage holder and \$106.00 per month to Smith. Thereafter the payments reduce to \$900.00 per month.

Alternatively, the parties can provide for a "balloon" payment at the end of two years, five years, ten years, depending on the amount financed by the owner, and the maximum monthly payment that the purchaser can afford.

### **EXAMPLE No. 3**

Smith can offer a "wraparound" at 9% per annum. If Jones puts down \$20,000.00. Smith can owner finance (by "wraparound") \$80,000.00 at 9% per annum interest for 30 years, (with or without a "balloon").

If Jones only puts \$15,000.00 down, Smith can still do a "wraparound" on the remaining \$85,000.00 at a rate and term agreed upon.

When using a "wraparound", the payments to the mortgage holder are still made by the Escrow Agent and not by the Seller.