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## Vendor and Purchaser - Real Estate Contracts - The Future of the Real Estate Contract in New Mexico: Huckins v. Ritter

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VENDOR AND PURCHASER—REAL ESTATE CONTRACTS—  
The Future of the Real Estate Contract in New Mexico: *Huckins v. Ritter*

I. INTRODUCTION

The real estate contract is a contract for the purchase of land. It often is used in lieu of a mortgage.<sup>1</sup> Real estate contracts generally are enforceable in New Mexico.<sup>2</sup> New Mexico courts, however, always have noted that an exception will be made to the general rule of enforceability if enforcement would "shock the conscience of the court."<sup>3</sup> In *Huckins v. Ritter*,<sup>4</sup> the New Mexico Supreme Court refused to enforce the forfeiture provision of a real estate contract upon the purchaser's default, holding that a forfeiture would shock the conscience of the court.<sup>5</sup>

The real estate contract used in *Huckins* contained a forfeiture provision similar to those found in many real estate contracts. Ordinarily, such provisions provide that, upon default by the purchaser, the vendor is entitled to repossess the property and to retain all payments made on the contract prior to the default.<sup>6</sup> *Huckins*, in light of other recent New Mexico cases, makes it clear that the court will make an exception to the general rule of enforceability of such provisions in order to protect buyers in some situations.<sup>7</sup> Like the cases preceeding it, however, *Huckins* fails to enunciate any specific test for determining when a forfeiture clause will not be enforced.

This Note will review prior real estate contract cases in light of *Huckins* in order to ascertain guidelines for future cases. It will discuss the use of the real estate contract for the purchase of real property as an alternative to the mortgage and the trust deed in the context of the history of the real estate contract in New Mexico. This Note also includes suggestions for the future use of real estate contracts in light of the *Huckins* decision.

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1. Comment, *Comparison of California Mortgages, Trust Deeds and Land Sale Contracts*, 7 UCLA L. Rev. 83, 95 (1960); see also *infra*, notes 20-32 and accompanying text.

2. See *Eiferle v. Toppino*, 90 N.M. 469, 565 P.2d 340 (1977); *Bishop v. Beecher*, 67 N.M. 339, 355 P.2d 277 (1960).

3. See *Hale v. Whitlock*, 92 N.M. 657, 593 P.2d 754 (1979); *Eiferle v. Toppino*, 90 N.M. 469, 565 P.2d 340 (1977); *Bishop v. Beecher*, 67 N.M. 339, 355 P.2d 277 (1960).

4. 99 N.M. 560, 661 P.2d 52 (1983).

5. *Id.* at 562, 661 P.2d at 54.

6. See *Nelson & Whitman, The Installment Land Contract—A National Viewpoint*, 1977 B.Y.U. L. Rev. 541, 542.

7. *Huckins*, 99 N.M. at 562, 661 P.2d at 54. For a detailed discussion of these cases, written prior to the *Huckins* decision, see Note, *The Real Estate Contract in New Mexico: Eiferle v. Toppino*, 8 N.M.L. Rev. 247 (1978).

## II. STATEMENT OF THE CASE

On July 28, 1981, Robert and Sylvie Huckins entered into a real estate contract with Nancy Ritter for the purchase and sale of residential property in Ruidoso, New Mexico.<sup>8</sup> The Huckins' made a \$45,000 down payment on the total purchase price of \$155,000, and assumed an underlying real estate note in the amount of \$40,725.73.<sup>9</sup> The remaining balance, approximately \$70,000, was due and payable on October 15, 1981, three months after the contract was signed.<sup>10</sup> The Huckins' were unable to make the \$70,000 payment on October 15th, and on October 30th, Ritter notified the Huckins' that if the amount due was not paid within fifteen days, she intended to exercise her right to retain all sums previously paid under the contract.<sup>11</sup> On November 30th, the Huckins' filed an action to enjoin Ritter from terminating the contract or, alternatively, to provide for the return of a portion of the down payment.<sup>12</sup> Ritter then agreed to extend the time for payment under the contract to January 10, 1982. The Huckins' failed to make the payment on January 10, and on February 25, Ritter terminated the contract.<sup>13</sup>

In June of 1982, the trial court entered an order in the action filed by the Huckins'. It ruled in favor of Ritter, upholding the forfeiture provision. On appeal, the New Mexico Supreme Court reversed the trial court, finding that the case fell within the exception to the general rule of enforceability of forfeiture provisions.<sup>14</sup> The court held that the plaintiffs were entitled to a return of the down payment, less a reasonable rental payment for the period they occupied the property and the amount of any diminution to the property that may have occurred during the plaintiffs' occupancy.<sup>15</sup>

## III. DISCUSSION

The supreme court addressed two issues in *Huckins v. Ritter*. The first issue, a procedural challenge to the appellants' right to appeal, was decided in favor of the Huckins' and is not discussed in this Note.<sup>16</sup> The

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8. *Huckins*, 99 N.M. at 561, 661 P.2d at 53. The terms of the real estate contract used in this case were similar to terms generally found in such contracts. A typical real estate contract states that time is of the essence, has an acceleration clause, and provides for forfeiture of the vendee's rights in the event of a breach by the vendee. Comment, *supra* note 1, at 83.

9. *Huckins*, 99 N.M. at 561, 661 P.2d at 53.

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.*

14. *Id.*

15. *Id.* at 562, 661 P.2d at 54.

16. *Id.* Ritter argued that the supreme court should refuse to consider the Huckins' argument on appeal because of the Huckins' failure specifically to challenge certain findings of fact, as required

second issue involved the substantive question of the enforceability of the forfeiture clause of the contract. The court held that to allow the seller to retain the \$45,000 down payment and to regain possession of the property, as provided by the terms of the contract, would be an unwarranted forfeiture.<sup>17</sup> The court relied on earlier New Mexico cases which have recognized an exception to the general rule that the forfeiture terms of real estate contracts are enforceable.<sup>18</sup> Courts apply this exception when enforcement would result in a forfeiture or unfairness "which shocks the conscience of the court."<sup>19</sup> The court, relying strictly on the specific facts of the case, gave little explanation for its refusal to enforce the forfeiture provision, and provided no general analysis or guidelines for future real estate contract disputes.

### A. Real Estate Contracts, Mortgages, and Deeds of Trust

The real estate contract often is used as an alternative to mortgages and deeds of trust in the sale of real property.<sup>20</sup> To understand the attractiveness of the real estate contract to vendors and purchasers, it is important to understand the differences among real estate contracts, mortgages, and deeds of trust. One of the most important conceptual differences among these three security devices involves legal title. When a mortgage is used, the legal title typically lies with the debtor-mortgagor.<sup>21</sup> When a deed of trust is used, the legal title passes to a third party, the trustee.<sup>22</sup> In contrast, when the property is purchased through the use of

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by N.M. R. Civ. App. 9(m). According to Ritter, the plaintiffs should have been bound by the findings of fact because they never properly attacked them on appeal. The lower court findings were that: (1) the Huckins' owed Ritter the sum of \$69,274.65 and were unable to pay the sum by the October deadline; (2) time was of the essence in the real estate contract; (3) 15 days after written demand for payment had been made and had not been satisfied, Ritter was entitled to her election of remedies; and (4) the Huckins' did not offer any evidence that the real estate contract did not properly reflect the parties' intentions. The supreme court refused to accept Ritter's argument, holding that the transcripts and briefs in the case were sufficient to present the essential question for review, notwithstanding a technical violation of the rules. *Huckins*, 99 N.M. at 561, 661 P.2d at 53.

17. *Huckins*, 99 N.M. at 562, 661 P.2d at 54.

18. One of the most recent exceptions to the general rule was made in *Eiferle v. Toppino*, 90 N.M. 469, 565 P.2d 340 (1977). The court in *Eiferle* refused to enforce a forfeiture on a real estate contract that occurred when the purchasers did not pay a \$25 fee when they sent a payment to cure a pending default. See *infra* notes 56-72 and accompanying text.

19. *Huckins*, 99 N.M. at 562, 661 P.2d at 54; *Eiferle*, 90 N.M. at 470, 565 P.2d at 341.

20. See *Hetland, The California Land Contract*, 48 Cal. L. Rev. 729 (1960); *Gerdes, Installment Land Contracts: Legislative Protection of Defaulting Purchasers*, 52 Harv. L. Rev. 129 (1938).

21. Comment, *supra* note 1, at 83. At common law, the mortgage operated as a conveyance of legal title to the mortgagee, but subject to defeasance upon payment of the debt. Although this theory still applies in some states, in most jurisdictions the mortgagee has only a lien on the land, and title passes to the mortgagor. R. Boyer, *Survey of the Law of Property* 499 (3rd ed. 1981). In New Mexico, the mortgagor retains the legal title, while the mortgagee has a lien on the property. *Griffith v. Humble*, 46 N.M. 113, 122 P.2d 134 (1942).

22. R. Boyer, *supra* note 21, at 511-12.

a real estate contract, the vendor retains the legal title until all payments have been made on the contract.<sup>23</sup>

Another important difference is the method of repossession of the property when a purchaser fails to make the payments due. When a mortgage is utilized, foreclosure occurs upon default by the mortgagee.<sup>24</sup> Mortgage foreclosures are regulated by statute, and involve lengthy and costly judicial proceedings.<sup>25</sup> Following judicial foreclosure, most states allow a statutory period of redemption during which the mortgagor may cure the default and redeem the property.<sup>26</sup> The cost of the foreclosure and the statutory right of redemption are problems creditors attempt to avoid through the use of the deed of trust and the real estate contract.

In response to the problems inherent in mortgages, some states have statutorily created the deed of trust as a device for the sale of real property.<sup>27</sup> New Mexico, however, does not have a deed of trust act. A deed of trust in New Mexico is subject to the same statutory provisions as a mortgage.<sup>28</sup> Use of a deed of trust in New Mexico, therefore, does not offer the same advantages as it does in other states.

In contrast to the default procedures of the mortgage and the deed of trust, when a purchaser under a real estate contract defaults, the seller may bring an action under general contract theories.<sup>29</sup> If a forfeiture clause similar to the one in *Huckins* is contained in a real estate contract, it typically is enforceable.<sup>30</sup> Upon default, enforcement of the forfeiture

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23. Comment, *supra* note 1, at 95.

24. R. Boyer, *supra* note 21, at 500-01. Some deed of trust statutes also allow the vendor to chose either foreclosure or forfeiture upon default by the purchaser. See, e.g., Ariz. Rev. Stat. §§ 33-801 to -821 (Supp. 1972) (discussed *infra* note 27).

25. See Gose, *The Trust Deed Act in Washington*, 41 Wash. L. Rev. 94 (1966). See generally N.M. Stat. Ann. §§ 48-7-1 to -10 (1978) (statutory regulation of mortgages in New Mexico).

26. Comment, *supra* note 1, at 88. New Mexico has a one year redemption period. N.M. Stat. Ann. § 39-5-20 (1978).

27. Lawyer, *The Deed of Trust: Arizona's Alternative to the Real Property Mortgage*, 15 Ariz. L. Rev. 194 (1973); R. Boyer, *supra* note 21, at 511; Gose, *supra* note 25, at 94.

For example, Arizona enacted the Deed of Trust Act in 1971. Ariz. Rev. Stat. Ann. §§ 33-801 to -821 (Supp. 1972). Upon default of the purchaser under a deed of trust in Arizona, the seller typically has two options: he can either foreclose under mortgage foreclosure proceedings, in which case the deed of trust is treated like a mortgage, or he can foreclose pursuant to the Trust Deed Act. *Id.*; st33-807(A); Lawyer, *supra*, at 204. Such foreclosure typically involves a sale of the property by the trustee. If the creditor chooses judicial foreclosure, he encounters the same problems involved with mortgage foreclosures. In comparison, foreclosure pursuant to the Trust Deed Act does not allow any redemption period and does not involve a lengthy court proceeding. The Act, however, gives the purchaser a 90 day reinstatement period prior to the trustee's sale during which the purchaser has the opportunity to cure his default. Lawyer, *supra*, at 199-200. This action most commonly is taken with a trust deed. Foreclosure under a deed of trust in Arizona, therefore, typically is more advantageous to the seller than foreclosure pursuant to a mortgage.

28. N.M. Stat. Ann. §§ 47-1-39 to -41 (1978).

29. Note, *Reforming the Vendor's Remedies for Breach of Installment Land Sale Contracts*, 47 S. Cal. L. Rev. 191, 199 (1973).

30. See *Eiferle v. Toppino*, 90 N.M. 469, 565 P.2d 340 (1977); *Bishop v. Beecher*, 67 N.M. 339, 355 P.2d 277 (1960).

clause is less time consuming than foreclosure proceedings under a mortgage.<sup>31</sup>

The purchaser's interest under a real estate contract is easily eliminated in comparison to judicial foreclosure and trustees' sales.<sup>32</sup> The seller in *Huckins* attempted to take advantage of this simple procedure for default. The court refused to allow the forfeiture, however, and the advantage of quick and inexpensive forfeiture under the real estate contract was lost in this case.

### B. History of the Real Estate Contract in New Mexico

As early as 1936, the New Mexico Supreme Court recognized that in the case of a contract for sale of land before conveyance, the vendor has the legal title to the land.<sup>33</sup> Although the vendee has possession of the land, the only method by which the vendee can prejudice that title is by paying the purchase price specified in the contract.<sup>34</sup>

One of the first New Mexico cases to address the issue of whether the forfeiture provisions of a real estate contract are enforceable was *Bishop v. Beecher*.<sup>35</sup> In *Bishop*, the purchasers entered into a real estate contract for the purchase of a house.<sup>36</sup> By the terms of the contract, the purchasers assumed an existing mortgage given by the vendors.<sup>37</sup> Against the assertion that real estate contracts should be considered equitable mortgages, giving a right of redemption to the vendee, the court upheld the forfeiture provisions of the contract. The court found that the property involved had a value in excess of \$12,000, and that the purchasers had retained possession and use at a cost of less than \$60 per month for almost six years prior to the default.<sup>38</sup> The court likened the payments to rent, and held that a forfeiture under these circumstances was not inequitable.<sup>39</sup>

The *Bishop* court, however, laid the foundation for an exception to the general rule of enforceability of forfeiture provisions. The court noted that the forfeiture provision will be enforced "absent unfairness which shocks the conscience of the court."<sup>40</sup> This recognition marked the first step in the development of the exception to the general rule of enforceability of forfeiture provisions.

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31. Comment, *supra* note 1, at 97. If the contract has been recorded, the vendor will have to bring a suit to quiet title; however, this is no more involved than a foreclosure proceeding. *Id.*

32. *Id.*

33. *Dunken v. Guess*, 40 N.M. 156, 56 P.2d 1123 (1936).

34. *Id.* at 159, 56 P.2d at 1125.

35. 67 N.M. 339, 355 P.2d 277 (1960).

36. *Id.* at 340, 355 P.2d at 277.

37. *Id.* The contract was similar to the one used in *Huckins*. See *supra* note 8.

38. 67 N.M. at 343, 355 P.2d at 279.

39. *Id.*

40. *Id.* at 343, 355 P.2d at 280.

Three years after *Bishop*, the court in *Davies v. Boyd*<sup>41</sup> held that, where a contract can be given two possible constructions, courts will adopt the construction that avoids a forfeiture.<sup>42</sup> *Davies* involved a written contract for the purchase of real estate. The purchase price of the property was \$17,500, of which \$8,000 represented a promissory note payable two years from the date of the contract.<sup>43</sup> The promissory note was secured by a mortgage upon the buyers' other property.<sup>44</sup> The remainder of the purchase price was payable at \$100 per month including interest. Within a few months, the purchasers defaulted on the monthly payments.<sup>45</sup> The court allowed the seller to repossess the property and retain the monthly payments previously tendered, as provided by the contract.<sup>46</sup> The seller, however, was not permitted to recover the amount due under the promissory note.<sup>47</sup>

The seller maintained that he was entitled to the amount due under the note because it was agreed upon in lieu of a down payment.<sup>48</sup> The court refused to accept this interpretation, explaining that the seller, having declared a forfeiture and electing to rescind the contract, could not as a matter of law recover on a note that represented an unpaid part of the purchase price.<sup>49</sup> In allowing the forfeiture, the court relied on *Bishop*, stating that "[A] provision for forfeiture of installment payments made prior to default, *which approximate rent*, will be approved, at least where reasonable notice of default is required by the contract."<sup>50</sup>

In 1979, the court decided *Hale v. Whitlock*,<sup>51</sup> another case involving the sale of real property under a real estate contract. Prior to default, the

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41. 73 N.M. 85, 385 P.2d 950 (1963).

42. *Id.* at 89, 385 P.2d at 952 (Moise, J., concurring specially).

An example of the court's ability to avoid a forfeiture is seen in *Ott v. Keller*, 90 N.M. 1, 558 P.2d 613 (Ct. App. 1976). In *Ott*, a real estate contract was used for the purchase of a house. The contract provided for forfeiture if the purchasers defaulted on payments and remained in default for 15 days after written demand for payments. When the purchasers failed to make a monthly payment four months after entering into the contract, the seller mailed a notice of default, which allowed the purchaser to cure the default by making the payment within 15 days from the effective date of the notice. The notice was mailed on February 4, 1976. On February 20, the sellers withdrew the papers from the escrow agent, effecting a forfeiture, and refused to accept the monthly payment offered by the purchasers that afternoon.

The court refused to enforce the forfeiture provision, interpreting the "effective date of the notice of default" to be the day after it was mailed, making the latest date for curing the default February 20th. *Id.* at 4, 558 P.2d at 617. Although the court refused to enforce the forfeiture, the opinion contains no reference to unfairness which shocks the conscience of the court.

43. 73 N.M. at 87, 385 P.2d at 950.

44. *Id.*

45. *Id.*

46. *Id.* at 88-89, 385 P.2d at 950-51.

47. *Id.*

48. *Id.* at 87, 385 P.2d at 951.

49. *Id.* at 89, 385 P.2d at 952.

50. *Id.* at 88, 385 P.2d at 951 (emphasis added).

51. 92 N.M. 657, 593 P.2d 754 (1979).

purchasers continually failed to make some of the monthly payments on time for several years. Eleven years after the parties entered into the real estate contract, the original seller assigned her interest in the contract. The purchasers were not notified that strict performance would be required by the assignee. After demanding that the purchasers make twenty-five delinquent payments totalling \$1,675, the assignee brought an action to declare the contract in default. The supreme court held that the trial court properly exercised its equity jurisdiction in granting the purchasers additional time to pay off the entire balance due on the contract.<sup>52</sup> Emphasizing that the seller had not objected to the late payments, the court concluded that the purchasers were reasonable in believing that the seller would not insist upon prompt payment of the monthly installments.<sup>53</sup> The court recognized that real estate contracts are enforceable in New Mexico and that the vendor may terminate the contract upon default, regain possession of the property, and retain payments made.<sup>54</sup> It held, however, "that there are exceptions to this rule, and that under certain circumstances, the contract and acts of the parties should be construed if at all possible to avoid a forfeiture."<sup>55</sup>

Another real estate contract case decided in the 1970's was *Eiferle v. Toppino*,<sup>56</sup> where the facts followed the same pattern as earlier real estate contract cases. The contract provided for a total payment of \$23,500. The purchasers made a down payment of \$3,000 and assumed a mortgage of approximately \$17,000 given to Prudential Insurance Company.<sup>57</sup> The purchasers also agreed to pay the seller's equity balance in the house, totalling approximately \$3,000, in monthly installments of \$30 or more to a designated escrow agent.<sup>58</sup>

In March of 1975, five years after entering into the contract, Prudential returned one of the purchasers' monthly mortgage payments because the bank had dishonored the check.<sup>59</sup> Prudential sent a letter with the returned check threatening to initiate foreclosure proceedings.<sup>60</sup> In the letter, the purchasers were given an opportunity to pay all existing delinquencies by sending the sum of \$573.89 no later than March 31, 1975.<sup>61</sup> Prudential sent a copy of the letter to the seller.<sup>62</sup>

The purchasers sent a cashier's check to Prudential in the amount

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52. *Id.* at 658, 593 P.2d at 755.

53. *Id.* at 657, 593 P.2d at 754.

54. *Id.* at 657-58, 593 P.2d at 754-55.

55. *Id.* at 658, 593 P.2d at 755.

56. 90 N.M. 469, 565 P.2d 340.

57. *Id.* at 469, 565 P.2d at 340.

58. *Id.*

59. *Id.* at 470, 565 P.2d at 341.

60. *Id.*

61. *Id.*

62. *Id.*

requested.<sup>63</sup> The company received the payment on or before April 1, 1975.<sup>64</sup> Meanwhile, on March 28, 1975, the seller sent a demand letter to the purchasers, claiming the deficiency in the mortgage payment owed to Prudential constituted a default.<sup>65</sup> The purchasers received this letter on March 29, 1975.<sup>66</sup> Although Prudential applied the cashier's check to the mortgage, the escrow agent refused to accept the payment owed to the seller unless the purchasers also paid \$25, which the contract required to cover the costs of the demand letter.<sup>67</sup> The \$25 was not paid, and the seller withdrew the escrow papers, filed an affidavit of default and forfeiture, and filed a special warranty deed.<sup>68</sup> Title to the property was thus conveyed back to the seller.

The purchaser brought an action seeking a declaration of the rights of the parties under the real estate contract. The supreme court held that the terms of the contract would not be enforced because, under the specific facts of the case, enforcement would shock the conscience of the court.<sup>69</sup> Again the court noted that real estate contracts generally are enforceable in New Mexico,<sup>70</sup> but it also recognized that there is an exception to the general rule.<sup>71</sup> In *Eiferle*, the court specifically found, given the facts involved, that the purchasers met the demands made by Prudential. Under the particular facts of the case, the court held that a forfeiture would result in "unfairness which shocks the conscience of the court."<sup>72</sup>

In each of the above cases, the court relied upon specific facts to determine whether the forfeiture clause in the real estate contract would be enforced. The court mentioned the test of unconscionability in each case, but failed to define it. The only guidelines given come from the cases where the court refused to enforce the forfeiture clause of the contract; the "guidelines" are the specific facts in each case. While it appears that the court is reaching equitable results in these cases, purchasers and sellers have little assurance that a specific real estate contract will be enforceable following these decisions.

### C. *Huckins v. Ritter*

*Huckins v. Ritter* followed the same analytical approach as *Eiferle*. In refusing to uphold the forfeiture in *Huckins*, the court focused on the fact that the purchasers had possession of the property for only a brief time,

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63. *Id.*

64. *Id.*

65. *Id.*

66. *Id.*

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

that the down payment was nearly one-third of the purchase price of the house, and that the market value at the time of the forfeiture was equal to the original sale price.<sup>73</sup> These facts appear to have been the sole basis for the determination of unconscionability which led to the court's refusal to uphold the forfeiture provision in the contract.

It is significant that the down payment made in *Huckins* constituted nearly one-third of the total purchase price of \$155,000.<sup>74</sup> When little or no down payment is made on a real estate contract and payments made prior to the default are substantially equivalent to the rental value of the property, it is not difficult to equate the loss from a forfeiture with rental payments, and to conclude that there is no hardship for the purchaser. In contrast, in a situation such as the *Huckins* case forfeiture results in a substantial loss to the buyer with a windfall for the seller. This is because the seller retains the large down payment in addition to the amount of money paid under the contract. These payments combined usually exceed the fair rental value of the property.

The court's emphasis on the brief period of occupancy and the lack of change in market price also is significant. It clearly indicates that the court will consider all aspects of each situation to determine what is fair, rather than considering only whether the forfeiture would be unfair to the purchasers. A different result may have been reached if one of these factors did not exist, even in light of the large down payment. In fact, the court has recently stated that a high down payment alone will not cause a forfeiture clause to be unconscionable.<sup>75</sup>

In light of the facts of the case, the result in *Huckins* hardly can be criticized. The lack of specific guidelines or analysis in *Huckins* and previous cases, however, makes it difficult to predict the result of future defaults.<sup>76</sup>

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73. 90 N.M. at 562, 661 P.2d at 54.

74. *Id.* While the amount of the down payment is important, a large down payment will not automatically trigger the exception to enforceability of a forfeiture clause. *Manzano Industries, Inc. v. Mathis*, \_\_\_ N.M. \_\_\_, 678 P.2d 1179 (1984); see *infra* note 77.

75. *Manzano*, \_\_\_ N.M. at \_\_\_, 678 P.2d at 1180; see *infra* note 77.

76. *Less than one year after Huckins* was decided, the supreme court decided *Cape v. Mullins*, 100 N.M. 525, 673 P.2d 502 (1983). In this case, the purchaser defaulted on a real estate contract after making six monthly payments totalling approximately \$2,500. The down payment on the contract was \$5,000. *Id.* at 526-27, 673 P.2d at 503-04. The main issue on appeal was whether the district court erred in not ordering a reinstatement of the real estate contract. *Id.* at 527, 673 P.2d at 504. The supreme court held that the trial court did not err because the facts of the case did not support an exception to the general rule of enforceability of forfeiture provisions in real estate contracts. *Id.* at 528, 673 P.2d at 505. The court relied heavily upon the facts of the case, and stated that "the legitimate use of real estate contracts as a worthy financing method in New Mexico would be jeopardized, should [the parties] be denied the rights for which they contracted." *Id.*

The *Cape* decision should have little effect on the development of the law because the court relied heavily on the unique facts involved and applied the same general language as earlier cases. The decision, however, does support the conclusion that forfeiture provisions in real estate contracts will be enforced when the payments forfeited can be equated to the fair rental value of the property.

#### D. The Utility of the Real Estate Contract After *Huckins*

Although the New Mexico Supreme Court has not provided any clear-cut rules for real estate contract disputes,<sup>77</sup> it is clear that forfeiture provisions in real estate contracts will be allowed in the future where the payments forfeited can be likened to rent. It is also clear that forfeiture provisions in real estate contracts will not be enforced in situations similar to *Huckins* and *Eiferle*.

It appears that the court is applying traditional notions of contract law in these cases. At the same time, it is using equitable remedies to provide greater protection for the defaulting purchaser. The reason for this method of analysis can be explained by several factors. First, penalty provisions are not favored,<sup>78</sup> and forfeiture provisions often look more like penalties than liquidated damage clauses because they do not state a specific sum of money to be forfeited upon default.<sup>79</sup> Second, when payments are made

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77. The lack of guidelines is illustrated by two other cases involving real estate contract defaults decided by the New Mexico Supreme Court since *Huckins* and *Cape: Manzano Industries Inc. v. Mathis*, \_\_\_ N.M. \_\_\_, 678 P.2d 1179 (1984) and *Martinez v. Martinez*, \_\_\_ N.M. \_\_\_, 678 P.2d 1163 (1984).

In *Martinez*, the court held that the right of the seller to declare a forfeiture under a real estate contract may be exercised only after giving the purchaser reasonable notice of the default. The court defined "reasonable time" as not less than 30 days. \_\_\_ N.M. at \_\_\_, 678 P.2d at 1167-68. The *Martinez* court refused to enforce the forfeiture provision of the contract, because the purchaser was given less than 30 days notice of the default. While the court did not uphold the forfeiture provision, the case was remanded with instructions that the sellers be allowed to forfeit the contract and demand that the purchaser reconvey her interest should she fail to cure the default within 30 days. *Id.* at \_\_\_, 678 P.2d at 1168. The court relied on language from previous cases, basing its holding on the finding that a forfeiture would shock the conscience of the court, because the purchaser was not given adequate notice. *Id.* at \_\_\_, 678 P.2d at 1167-68. The lack of a 30 day notice of default is the most specific reason for refusing to enforce a forfeiture provision seen in any real estate contract case to this date.

The most recent real estate contract case decided by the supreme court is *Manzano Industries*. The court upheld the forfeiture clause of the real estate contract involved. \_\_\_ N.M. at \_\_\_, 678 P.2d at 1180. Again, the court considered all of the circumstances of the case, and noted in particular that the purchasers had failed to meet all of their obligations under the contract. These obligations were: 1) to make timely monthly payments; 2) to keep the premises in good repair; 3) to keep the premises insured; and 4) to pay taxes on the property. *Id.* Although a substantial down payment was made on the contract, the court refused to allow this factor to trigger the exception to enforceability. The court specifically stated: "We refuse to hold that the forfeiture of a large down payment will, in every case, shock the conscience of the court. The size of the forfeited down payment is only one of the factors the trial court should consider." *Id.* Although the court did not enumerate other factors, it is apparent that the facts mentioned above were of utmost importance for the court's holding.

78. Corbin, *The Right of a Defaulting Vendee to Restitution of Instalments Paid*, 40 Yale L.J. 1013, 1016 (1931).

79. Liquidated damages typically bear a reasonable relationship to the actual damage caused by a breach, and contract provisions for liquidated damages generally are enforceable. In contrast, a penalty is a type of punishment for the breach, and it bears no relation to the actual damages incurred. A penalty may easily result in unjust enrichment of the non-breaching party, and generally is unenforceable. Lee, *Remedies For Breach of the Installment Land Contract*, 19 U. Miami L. Rev. 550, 552 (1965). The problem lies in the fact that there is no general rule for determining whether a provision is a penalty or liquidated damages. Most courts look to the facts of the case, the intent of the parties, and the construction of the contract to make this determination. *Id.*

on a regular basis under a real estate contract, the amount of the forfeiture increases as the purchaser performs under the terms of the contract.<sup>80</sup> This result means that the penalty for the breach increases in inverse proportion to the seriousness of the breach. Third, the actual injury suffered by a seller upon a purchaser's default can be difficult to determine, due to possible depreciation or appreciation of the land, improvements made on the land by the purchaser, and changes in the real estate market. For these reasons, it is difficult for the court to apply general contract rules to each case in a consistent manner.

In determining whether a forfeiture clause will be enforced upon a purchaser's default, the test appears to be whether the total amount paid by the purchaser, including monthly payments made prior to the default and any down payment, can be equated to the fair rental value of the property during the period of possession by the purchaser. A court also should consider any diminution in the value of the property in making the fair rental value determination.<sup>81</sup> When the payments made are extremely disproportionate to the fair rental value during the purchaser's possession, a court should not uphold the forfeiture provision of the contract. Instead, a court should demand that the seller return the amount of the payments tendered, less the fair rental value of the property and any diminution in the value of the property during the purchaser's possession. This appears to be similar to allowing the seller to obtain reliance damages, although the New Mexico courts have never defined the remedy in these terms. The supreme court, however, has left open the possibility of resorting to "fairness" and equity in cases which are difficult to decide due to particularly unique circumstances.

#### *E. Possible Reforms for the Use of the Real Estate Contract in New Mexico*

The advantages offered to vendors through the use of the real estate contract, such as simple, inexpensive forfeiture upon default, may disappear as a result of courts' efforts to protect purchasers from unconscionable contract terms. In turn, the loss of advantages to vendors could lead to the disappearance of the real estate contract in New Mexico. For this reason, it is important that New Mexico develop a predictable method of handling future defaults under these contracts.

The goal of any reform of the use of the real estate contract must be to preserve as many of the advantages of real estate contracts as possible

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80. See Corbin, *supra* note 78, at 1029. For example, if one defaults on a real estate contract after making only one monthly payment, the most one stands to lose is the amount of that payment and the down payment, if any. In comparison, if one defaults after making monthly payments for several years, one stands to lose a great deal more, even though the breach is less significant.

81. See *Huckins*, 99 N.M. at 562, 661 P.2d at 54.

while protecting the purchaser against unjust forfeiture.<sup>82</sup> The reform also must permit the contract to operate under clear and recognized standards so that both vendors and purchasers will know the effect of a breach without resort to judicial resolution.

Several states have developed legislative and judicial reforms aimed at solving the problems involved in the use of real estate contracts.<sup>83</sup> The California courts have de-emphasized the contract aspects of real estate contracts in favor of protections similar to those given to mortgagors.<sup>84</sup> Other states have adopted the statutory deed of trust as an alternative security device to the traditional mortgage.<sup>85</sup> In New Mexico, however, the deed of trust is indistinguishable from a mortgage, and subject to the same statutory conditions.<sup>86</sup>

The New Mexico Supreme Court has consistently stated that public policy supports the use of real estate contracts in New Mexico.<sup>87</sup> The court has stated that its refusal to enforce forfeiture provisions "when fairness and legal principles dictate that [it] should not" does not undermine the market for real estate contracts.<sup>88</sup> It is apparent from *Huckins* and the cases decided more recently that drastic judicial reforms are not forthcoming.<sup>89</sup> In addition, the court has yet to suggest that legislative reforms would be appropriate.

A possible legislative reform would be to enact a statute regulating forfeitures by allowing the purchaser upon default to recover an amount equal to the total principle payments made under the real estate contract, less the fair rental value of the property while in the possession of the purchasers.<sup>90</sup> Another possibility would be the enactment of a detailed statute regulating all aspects of the real estate contract.<sup>91</sup>

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82. Lee, *Defaulting Purchaser's Right to Restitution Under the Installment Land Contract*, 20 U. Miami L. Rev. 1, 19 (1965).

83. For example, Maryland enacted a statute designed to prevent forfeitures in certain cases. See Md. Real Property Code Ann. §§ 10-101 to -110 (1981). California also has attempted to protect purchasers from unconscionable forfeitures. See Note, *supra* note 29; *Barkis v. Scott*, 34 Cal. 2d 116, 208 P.2d 367 (1979).

84. See Note, *supra* note 29, at 199.

85. See Gose, *supra* note 25, at 104.

86. See N.M. Stat. Ann. § 48-7-7 (1978); *id.*

§§ 47-1-39 to -41.

87. *E.g.*, *Manzano Industries, Inc. v. Mathis*, \_\_\_ N.M. \_\_\_, 678 P.2d 1179 (1984); *Martinez v. Martinez*, N.M. \_\_\_, 678 P.2d 1163 (1984).

88. *Martinez*, \_\_\_ N.M. at \_\_\_, 678 P.2d at 1167.

89. See *Manzano Industries*, \_\_\_ N.M. \_\_\_, 678 P.2d 1179 (1984); *Martinez v. Martinez*, \_\_\_ N.M. \_\_\_, 678 P.2d 1163 (1984) *Cape v. Mullins*, 100 N.M. 525, 673 P.2d 502 (1983).

90. This, in effect, would codify what the court apparently is doing in situations similar to the situation presented in *Huckins*. Such a statute would have to recognize, and make exceptions for, situations in which the default was made in bad faith in order to protect sellers from purchasers who decide they no longer wish to be a party to the contract for reasons other than inability to pay. Such a statute may remove any incentives for sellers to use real estate contracts because sellers would stand to gain little upon a purchaser's default. On the other hand, this type of statute would provide both vendors and purchasers with clear and concise guidelines upon default under a real estate contract.

91. Such a statute has been suggested by Professor Richard H. Lee. See Lee, *supra* note 82, at

A more radical remedy would be to enact the Uniform Land Transactions Act (ULTA)<sup>92</sup> in New Mexico. The purposes of the ULTA are: 1) to simplify, clarify, and modernize real estate transaction law; 2) to promote interstate flow of funds for real estate transactions; 3) to protect consumers against unreasonable risk; and 4) to achieve uniform real estate laws among the states.<sup>93</sup> The scope of the ULTA includes all contractual real estate transfers, including transfers for security and transfers of limited interests, such as leases and easements.<sup>94</sup>

The ULTA provides predictable methods for handling forfeitures and determining damages upon the breach of a real estate contract. Although the ULTA has not been adopted by any state as of this writing,<sup>95</sup> it should be carefully considered as a viable solution to the problems currently facing the real estate business.

#### IV. CONCLUSION

It may indeed be true, as the New Mexico Supreme Court claims, that the supreme court's occasional refusal to enforce forfeiture provisions in real estate contracts has not effected the viability of the real estate contract

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21-24. The most important aspect of the statute suggested by Professor Lee is that it prohibits any provision in real estate contracts for forfeiture of any payments made exceeding 10% of the purchase price. The statute also requires that restitution be made to the purchaser upon default of all payments in excess of the amount of money stipulated as liquidated damages. *Id.* at 22.

These two provisions appear to solve the recurring problems caused by defaults on real estate contracts. First, the 10% allowance for liquidated damages provides some incentive for the seller to use a real estate contract instead of a conventional mortgage because the provision would allow the seller to retain more money upon default than the seller could retain as reliance damages in some situations. At the same time, the purchaser is protected by the provision that requires restitution in excess of the specified amount of liquidated damages. Finally, the statute makes express provision for foreclosure, including required grace periods upon the purchaser's default. This provision provides the simplicity lacking in mortgage foreclosures, while also providing certainty for both the buyer and the seller upon default.

92. Uniform Land Transactions Act (National Conference of Commissioners on Uniform State Laws)(1978). No state has yet enacted the ULTA. National Conference of Commissioners on Uniform State Laws, Uniform Laws Annotated Directory of Acts-Tables Index (Master ed. 1983).

93. Uniform Land Transactions Act § 1-102.

94. Uniform Land Transactions Act, Article Two.

Several provisions of the ULTA are of particular interest. Section 1-311, for example, allows the court, upon finding that a contract or contract clause was unconscionable at the time the contract was entered into, to refuse to enforce the contract, or to limit the application of any unconscionable clause to avoid an unconscionable result. In addition, Part Five of Section Two of the ULTA provides specific remedies for the seller upon the purchaser's breach. Uniform Land Transactions Act § 2-504.

Perhaps the section of greatest interest is section 2-516, which allows liquidated damages to be fixed by agreement, "but only in an amount that is not unreasonable in the light of the anticipated or actual harm caused by the breach." *Id.* This section explicitly states that a provision for unreasonably large liquidated damages is void. In addition, if the buyer breaches, the buyer is entitled to restitution of any amount by which the sum of his payments exceeds the amount of liquidated damages to which the seller is entitled. *Id.* This provision could solve the problem of unconscionable forfeitures while also providing enough incentive for the seller to use a real estate contract because it appears to put a reasonable, but not prohibitive, limit on the amount of money a seller can expect to receive upon a buyer's default.

95. See *supra*, note 92.

in New Mexico. A problem, however, lies in the uncertainty which the court has created by refusing to lay specific guidelines for the future. Apparently, the court believes that concepts of "fairness" and equity will provide adequate guidelines for those who enter into real estate contracts. On one hand, the lack of specifics is necessary, and in fact beneficial, due to the unique situations involved in individual real estate contract defaults. Common sense would appear to be the best guide for predicting whether a forfeiture provision will be enforced after *Huckins*.

On the other hand, the lack of specific guidelines creates uncertainty among potential parties to a real estate contract, and may result in a flood of litigation in the future. It seems likely that many defaulting purchasers will go to court in an attempt to prevent sellers from enforcing forfeiture provisions. This will effectively eliminate the advantage of the real estate contract to the seller, and could lead to the disappearance of the real estate contract in New Mexico.

For the buyers and sellers in the real estate market who believe in the ability of the New Mexico courts to make proper decisions based on "fairness" and equity, the *Huckins* decision will pose few problems. For those seeking more specific guidelines, however, the use of a real estate contract may not be a viable method for the sale of land. After *Huckins*, the only certainty is that forfeiture provisions in real estate contracts will be enforced unless such enforcement would "shock the conscience of the court." Exactly what this means depends upon the court's interpretation of individual situations as they arise in future litigation.

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