

THE BORDER

by MARY ALICE ROBBINS

Low-income Texans living along the Texas-Mexico border or in major urban areas around the state can realize the American dream of home ownership, with less chance they'll lose their money, under a new state law designed to stop abuses in the contract-for-deed system.

"Along the Texas-Mexico border, contracts for deed helped create

an unregulated market for very low-cost and substandard dwellings and are among the reasons substandard housing in the form of colonias flourished in the region," says state Sen. Eddie Lucio, D-Brownsville, Senate sponsor of H.B. 1823.

Housing advocates for low-income Texans pushed for the bill to remedy what they say were problems in the contract-for-deed system. John Henneberger, the co-director of the Texas Low-Income Housing Information Service in Austin, says the Legislature passed contract-for-deed reforms in 1995 and 2001, but there are still flaws in the system. "I hope it will in essence be the final thing that clears up the abuses on contracts for deed," Henneberger says of the new law.

Along the border, particularly in poor communities, people commonly use contracts for deed to purchase residential property. Henneberger says that, in the late-1970s and 1980s, the border experienced a rapid population growth. Land developers began creating colonias, he says, and the developers turned to contract-for-deed arrangements to make sales. Sellers financed the sales and wanted to be able to re-claim the property quickly and easily if the buyer defaulted, Henneberger says.

Henneberger adds that the colonia developments were comprised of substandard housing for which traditional lenders would not provide loans. The American dream of homeownership in colonias has turned into a nightmare for many of these people. Colonias often lack basic services, such as drinking water, sewers and paved roads,

says Kathryn Youker, staff attorney for Texas RioGrande Legal Aid (TRGLA) in Weslaco.

Unlike home buyers using standard mortgages, people who buy residential property under a contract for deed don't receive deeds to the property until they pay off the loan. The seller holds the deed until the buyer makes the final payment.

Robert Doggett, TRGLA staff attorney in Austin

and manager of the legal aid program's foreclosure defense team, predicts the new law, which takes effect on Sept. 1, will have a huge impact. That's because the law makes it possible for buyers with contracts for deed to convert their loans to traditional mortgages.

H.B. 1823 amended Subchapter D, Chapter 5 of the Property Code, by adding §5.081. Section 5.081 gives a buyer the right, "at any time and without paying penalties or charges of any kind," to convert the buyer's interest in property under a contract for deed to a standard mortgage with the same terms. Under

that provision, the buyer executes a promissory note to the seller, and the seller conveys title to the buyer.

"Probably thousands of people who are trying to obtain title to property will realize that goal," Doggett says.

But Mark McPherson, chairman of the State Bar of Texas Real Estate, Probate and Trust Section, says the new law swings the pendulum too far to

the buyers' side.

"In the process of correcting abuses . . . we pulled out a bludgeon and beat to death those provisions," says McPherson, a principal in McPherson & Associates in Dallas.

McPherson says the law's conversion provision could dry up the loan market for low-income home buyers, because sellers will face increased expenses and the potential for greater risk with a standard mortgage.

Doggett says contract-for-deed arrangements — which are common in the border region — have been rife with problems over the years. In some cases, Doggett says, buyers have been unaware of liens against the property until a bank forecloses on the property because the seller has defaulted on a loan. In other cases, he says, sellers have not platted properties properly, making it impossible



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for the buyers to connect to city utility services. And some buyers who have paid the full amount owed on their homes don't receive the deeds, he says.

Youker says some buyers who pay off their loans are unable to obtain their deeds because they cannot find the sellers. "They just disappear," she says.

Without a deed, a buyer can't sell the property or transfer the property to an heir, Youker says.

Virginia Goldman, head organizer for the Houston chapter of the Association of Community Organizations for Reform Now (ACORN), says the group made passage of H.B. 1823 its top priority this year. Goldman says people who buy property under contracts for deed are renters in the sense that the insurance and the taxes on their properties are not in their names. They can't claim homestead exemptions, and if an insurer pays a claim for damage to the property, they may not receive the money even though they paid the premiums, she says.

"They have all the responsibilities of home ownership, but they don't get the benefits," Goldman says.

H.B. 1823

Under the new law, the seller must execute a deed and convey to the buyer recorded legal title of the property within 10 days after the buyer provides a promissory note for the balance owed on the property. The law requires that, if the seller decides not to provide the deed within the 10-day period, the seller must provide the buyer a written explanation that legally justifies that decision, or face monetary penalties.

McPherson says the change in the Property Code flips contracts for deed into very different transactions with different risks for the sellers. "This boils down to whether sellers will be willing to sell to low-income people," he says.

Houston solo Richard Spencer, chairman of the Texas College of Real Estate Lawyers, says sellers finance home sales for less creditworthy buyers, because the sellers can handle the transactions with contracts for deed. Sellers may not want to convey title to a property until the loan is

paid in full, because they face a more expensive process if they have to go through a lengthy foreclosure when a buyer defaults on a loan, Spencer says.

Sanford Weiner, a real estate partner in Houston's Vinson & Elkins, says sellers often use a contract for deed, because there is a high default rate early on in such transactions. The contract for deed makes it easier for the seller to oust a defaulted purchaser, because the seller does not have to go through the foreclosure process, says Weiner, a member of a V&E team that has been working pro bono with ACORN on contract-for-deed matters.

Allan Van Fleet of Houston, another V&E partner involved in the pro bono project with ACORN, says current law does not give buyers a right to convert a contract for deed. "Many of the contracts we saw prohibited [buyers] from paying off the contract early," Van Fleet says.

Doggett says sellers who will sell property to low-income buyers only with contracts for deed may never have intended to sell the property. Doggett says some low-income buyers learn after they get into contract-for-deed arrangements that they don't have enough money to buy a property and lose the money they've invested.

"Allowing these rip-offs to continue is no favor to poor people," Doggett says.

McPherson sees another problem with the new law. He says it provides for forms promulgated by the Texas Real Estate Commission (TREC) to be used for converting contracts, but the commission has no such forms and no plans to develop the forms.

"The reference to the Texas Real Estate Commission [in H.B. 1823] was not well thought through," McPherson says.

Loretta DeHay, TREC's general counsel, was on vacation last week and did not return an e-mail requesting comment on the situation with the forms before presstime on Aug. 11.

Doggett says he's hopeful that TREC will promulgate the forms but that anyone can draft a form for use in these transactions. It's not going to be a problem, he says.

McPherson says he believes the cure the Legislature provided is worse than the problems. But Doggett and other advocates for low-income home buyers say the new law will cure many of the problems that the buyers have faced with contracts for deed.

One Family

Youker recently represented a couple in a contract-for-deed dispute. Julian and Argentina Olague sued the people from whom the Olagues bought their home, filing *Olague v. Balli* last year in Hidalgo County's 389th District Court. In their original petition, the Olagues asserted claims for breach of contract, statutory fraud and violations of the Texas Deceptive Trade Practices-Consumer Protection Act against Adolfo and Pearl Balli.

As alleged in the petition, the Olagues agreed in 1993 to pay the Ballis \$18,500 for the property, located in a colonia outside of Weslaco, in Hidalgo County on the border, and made a \$3,000 down payment. The Olagues asserted in the petition that they paid all the monthly payments of \$204.83, which included 10 percent interest.

In the petition, the Olagues alleged they paid the Ballis the full amount agreed to under the contract by July 2002 but that the Ballis continued to accept monthly payments for the property through Dec. 1, 2003, resulting in an overpayment of more than \$3,800. The Olagues further alleged that the Ballis did not provide or record a warranty deed granting them title to the property.

Because the deed was never recorded in the Olagues' name, the Olagues' tax payments were not recorded properly, and they faced the possible loss of their home, Youker says.

"It was a big mess," Youker says. "This is what you get when you don't work with a bank."

Youker says the parties reached a settlement in June. The Ballis paid the Olagues almost \$5,000 to settle the suit, she says.

Weslaco solo Phil Harris, attorney for the Ballis, says his clients deny all of the Olagues' allegations but agreed

to a settlement to end the litigation for the least amount of cost. "They just wanted to get rid of this lawsuit," Harris says.

Youker says she is negotiating with the Hidalgo County Tax Office to get the Olagues credit for the money they paid in for taxes on the property.

The new law also offers relief to contract-for-deed home buyers whose properties are not properly platted. H.B. 1823 adds §5.083 to the Property Code, giving buyers the right to rescind a contract for deed and get back all the money they paid for the property and any improvements, if the property is not platted properly.

"This one is the time bomb," says Sanford, the V&E real estate partner.

Sanford says cities may be inundated with requests for plats, putting a strain on the limited resources of cities' planning departments. Sellers also could face high costs to comply with platting requirements, Sanford says. If a seller doesn't comply within 90 days after receiving a platting request, the purchaser can rescind the contract and is entitled to every cent that the purchaser ever paid for the property, including amounts paid for insurance and taxes and the value of any improvements made, he says.

"If everyone who has a right to rescind rescinds, you will have a rush of demands on sellers who may not have the resources to pay," Sanford adds.

Sanford says buyers of property are the ones who suffer the consequences if property is not platted properly, because they're unable to connect to city utilities or obtain city building permits if their homes are destroyed and they need to rebuild.

H.B. 1823 also provides new protections for those who buy property under contracts of deed after Sept. 1. Under §5.085 of the Property Code, a seller can't convey property

using an executory contract, such as a contract for deed, in most instances if there are liens or other encumbrances against the property. If a buyer agrees to purchase property that is encumbered, the seller must provide the buyer full information on the lien, including the name and address of the lien holder and the balance left on the note.

Virginia Goldman says people who buy property under contracts for deed are like renters: Insurance and taxes on their properties are not in their names.

Youker says buyers can lose their homes when sellers default on liens against the property and a mortgage company forecloses. Buyers often don't know there is a lien, she says.

"The buyer is just left homeless," Youker says. "All they can do is to try to sue the seller, and usually the seller doesn't have any money."

The new law also defines a lease with an option to buy as an executory conveyance and applies many of the contract-for-deed protections to such options.

Doggett says, for example, the seller must give a person leasing property with an option to buy 30 days' notice of a default. The law also prohibits the seller from including a provision in the lease contract that requires forfeit of the option if the person is late in making a payment, he says.

Notes Doggett, "These options cost a lot of money." 