A landowner needed money. His land was fairly worth $100,000, so the landowner tried to borrow $60,000 from a lender on the security of the land. The lender agreed, but only if the landowner would convey the land to the lender outright by warranty deed, with the lender agreeing orally to reconvey to the owner once the loan was paid according to its terms. The landowner agreed, conveyed the land to the lender by warranty deed, and received $60,000 cash from the lender. The lender promptly and properly recorded the landowner's deed.

Now, the landowner has defaulted on repayment with $55,000 still due on the loan. The landowner is still in possession.

Which of the following best states the parties' rights in the land?

A. The attempted security arrangement is null as an unknown creature to the law, so the lender has only a personal right to $55,000 from the landowner.

B. The landowner, having defaulted, has no further rights in the land, so the lender may obtain summary eviction.

C. The lender may bring whatever foreclosure proceeding is appropriate under the laws of the jurisdiction.

D. The lender's oral agreement to reconvey is invalid under the statute of frauds, so the lender owns the land outright.

Explanation:

Mortgage alternatives

Absolute deed	Debtor gives deed to creditor with intent to secure loan (ie, equitable mortgage)
Deed of trust	Debtor gives deed of trust to third-party trustee as collateral for debt, & creditor can instruct trustee to foreclose upon default
Installment land contract	Debtor agrees to buy land through installment payments & gets immediate possession, but seller keeps legal title until paid in full
Sale-leaseback	Seller leases property from buyer immediately after sale, & seller's rental payments function as repayments on loan
Equitable vendor's lien	Seller finances buyer's purchase with equitable vendor's lien when seller transfers title to buyer but purchase price not fully paid

A **mortgage** is a lien against real property that is given to secure a debt and is often memorialized in two documents:

Mortgage deed – a writing that conveys an interest in the real property to secure the debt

Promissory note – a formal "IOU" in which the borrower promises to repay the debt according to the listed terms (eg, interest rate, payment schedule, acceleration clause)

But an **equitable mortgage** can be established by an **absolute deed** (or other alternative means) that was **intended to secure a debt**. As a result, the deed recipient (like any other lender) may bring a **foreclosure action** if the debtor defaults on repaying the loan.

Here, the landowner conveyed his land to the lender *outright* by warranty deed. And since the lender agreed to reconvey the land once the loan was paid, the deed was intended to secure the landowner's debt. As a result, the deed will be treated as an equitable mortgage (ie, an absolute deed) **(Choice A)**. This means that the lender can bring an appropriate foreclosure proceeding to recover the $55,000 still due on the loan.

(Choice B) A summary eviction is a legal procedure that allows a landlord to quickly remove a tenant from leased property without the formalities of a full trial. But it does not allow a lender (mortgagee) to remove a borrower (mortgagor) from mortgaged land.

(Choice D) A mortgage is subject to the statute of frauds, so it must be in writing, signed by the parties against whom it is to be enforced, and contain all essential terms. Therefore, the lender's *oral* agreement to reconvey the land is invalid under this statute. But the *written* warranty deed is valid under the statute, and extrinsic evidence (eg, the oral agreement) can be used to show the parties' intent to create a mortgage.

Educational objective:

A mortgage is typically evidenced by a mortgage deed and a promissory note. But an equitable mortgage can also be created when an absolute deed is made with the intent that it secure a debt.

References

Restatement (Third) of Prop.: Mortgages § 3.2 (Am. Law Inst. 1997) (absolute deed as mortgage).