

**Commonwealth of Kentucky**  
**Court of Appeals**

NO. 2012-CA-001655-MR  
AND  
NO. 2012-CA-001834-MR

JOE S. WATKINS

APPELLANT

v. APPEALS FROM BOURBON CIRCUIT COURT  
HONORABLE PAUL F. ISAACS, JUDGE  
ACTION NO. 11-CI-00211

RICHARD STIPP EADS AND  
DEANNA EADS

APPELLEES

OPINION  
REVERSING AND REMANDING

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BEFORE: LAMBERT, TAYLOR, AND VANMETER, JUDGES.

TAYLOR, JUDGE: Joe S. Watkins brings Appeal No. 2012-CA-001655-MR and

Appeal No. 2012-CA-001834-MR from orders of the Bourbon Circuit Court

entered August 30, 2012, and October 2, 2012, respectively, quieting title to certain

real property in favor of Richard Stipp Eads and Deanna Eads (collectively referred to as “the Eads”) and awarding the Eads damages. We reverse and remand Appeal Nos. 2012-CA-001655-MR and 2012-CA-001834-MR.<sup>1</sup>

The facts giving rise to this appeal are largely undisputed. On September 24, 1998, Joe (Jody) S. Watkins entered into an installment land sale contract with Elizabeth Stipp Eads<sup>2</sup> for the purchase of residential property owned by Elizabeth located at 531 Main Street, Paris, Kentucky. Although not documented in the record, Elizabeth subsequently conveyed her interest in the property to Richard and Deanna Eads.<sup>3</sup> The contract stated a total purchase price of \$125,000 with a down payment of \$5,000 to be paid upon execution of the contract. The \$120,000 balance was to accrue interest at the rate of 9.5 percent per annum, simple interest, and was to be paid in 180 equal monthly installments of \$1,253.07. Watkins was also responsible for paying the *ad valorem* taxes on the

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<sup>1</sup> Appeal No. 2012-CA-001655-MR was taken from a judgment entered by the circuit court on August 30, 2012, that granted a summary judgment holding that Joe S. Watkins had waived his right to a foreclosure sale under the installment land sale contract (contract), and awarded damages under the contract. On its face, this appeal was interlocutory. However, before the issue was addressed by this Court, Appeal No. 2012-CA-001834-MR was filed from a final judgment entered on October 2, 2012. For judicial economy and expediency, this Court has consolidated the appeals for disposition hereof.

<sup>2</sup> When the contract was executed in 1998, Joe (Jody) S. Watkins, Jr., was married to Pam Watkins. Pam Watkins died after execution of the contract, but before the underlying civil action was filed. The Watkins’ daughter, Jody Lynn Oliver, was also identified in the contract as a purchaser of the property but never signed the contract. Oliver subsequently conveyed by quitclaim deed any interest she may have acquired in the property to Joe S. Watkins.

<sup>3</sup> Elizabeth Stipp Eads is the mother of Richard Stipp Eads. Elizabeth transferred her interest in the subject real property to her son, Richard Stipp Eads and his wife, Deanna Eads. Reference is made to “Deed Book 262, Page 519” regarding this transfer but the deed was not introduced into evidence or made part of the record on appeal.

property conveyed under the contract. The contract further provided that in the event of default, the Eads could declare the total balance due, and if such balance was not paid within ten days, the contract could be terminated. The contract also contained the following forfeiture clause which is the genesis of this appeal:

[I]n the event that the amount then owing is not paid within ten (10) days after demand therefore, Seller may terminate this agreement and all payments made by Purchaser hereunder and the value of any repairs and/or improvements made by Purchaser may be retained to the benefit of the Seller as fixed and liquidated damages for non performance by Purchaser of this agreement and as rent and compensation for use and occupancy of said property by Purchaser, as Purchaser specifically waives their right to a foreclosure sale of the property.

However, if the above remedy of Seller, upon default by Purchaser, is determined to be unenforceable by a court of competent jurisdiction, then in that event Seller may, at his option, declare all of the unpaid purchase money herein, the interest due thereon and all other amounts due hereunder to be immediately due and payable without further notice of demand to Purchaser, and Seller may thereupon institute proceedings to collect the same as if Seller had a purchase money lien on said property, pursuant to the holding and guidelines of *Sebastian v. Floyd, Ky.*, 585 S.W.2d 381 (1979), and Purchaser agrees to pay all costs thereof, including reasonable attorney's fees.

It is undisputed that Watkins eventually defaulted under the terms of the contract. On June 4, 2010, the Eads sent Watkins a letter notifying him the contract would be terminated in ten days unless all arrearages (payments, taxes, and interest) were paid in full. There is a dispute between the parties as to the actual amount owed including interest. The arrearages were not paid;

consequently, the Eads filed a complaint in Bourbon Circuit Court in June of 2011. Therein, the Eads alleged that Watkins was in default under the terms of the contract, and that per the contract's forfeiture clause, Watkins forfeited any right to a foreclosure sale or recoupment of payments made thereunder.

Watkins filed an answer and counterclaim, asserting that he had not forfeited the right to a foreclosure sale and was entitled to recoupment of payments made under the land contract. Specifically, Watkins argued that a foreclosure sale of the real property was legally mandated and that he was entitled to receive approximately \$86,984.72 from the proceeds of the sale of the real property.

By opinion and order entered April 17, 2012, the circuit court granted summary judgment in favor of the Eads. The circuit court determined that Watkins was in default, had forfeited his right to a foreclosure sale per the contract, and waived any payments made under the land contract. The circuit court then conducted a hearing to determine the amount of damages owed by Watkins to the Eads. By order entered August 30, 2012, the circuit court determined the amount of damages to be \$311,381.38 and awarded same to the Eads. A final judgment upon transfer of the property to the Eads per court order, with credit thereon for the value of the property determined by the circuit court at \$130,000, was entered October 2, 2012. These appeals follow.

#### I. THE FORFEITURE CLAUSE

Watkins contends the circuit court erred by concluding that the forfeiture clause in the contract was enforceable and that he waived his right to a foreclosure

sale of the real property. Watkins relies upon *Sebastian v. Floyd*, 585 S.W.2d 381 (Ky. 1979), for the proposition that a forfeiture clause in an installment land contract is *per se* invalid. The Eads respond that Watkins voluntarily waived his right to a foreclosure sale of the real property under the contract and, therefore, *Sebastian*, 585 S.W.2d 318, is inapposite. The circuit court concluded Watkins' waived his right to a judicial foreclosure sale.

Summary judgment is proper where there exists no material issue of fact and movant is entitled to judgment as a matter of law. Kentucky Rules of Civil Procedure 56; *Steelvest, Inc. v. Scansteel Service Center, Inc.*, 807 S.W.2d 476 (Ky. 1991). In this case, we are concerned with an issue at law – validity of the forfeiture clause in the parties' installment land contract. Our review of issues of law proceeds *de novo*. *Ceasars Riverboat Casino, LLC v. Beach*, 336 S.W.3d 51 (Ky. 2011).

Installment land sale contracts, also commonly referred to as contracts and bond for deed, are recognized as valid and enforceable contracts to finance the purchase of real property. *Sebastian*, 585 S.W.2d 381. These contracts are common in owner-financed transactions. Upon execution of an installment land sale contract, legal title to the real property remains with the seller, and equitable title to the real property passes to the purchaser. *Id.* However, Kentucky law is clear that upon default by the purchaser in an installment land contract, the purchaser does not “forfeit” his interest in the real property and, most importantly,

a purported forfeiture clause stating otherwise is considered void and unenforceable. *Sebastian*, 585 S.W.2d 381.

This Court recently revisited *Sebastian* in *Slone v. Calhoun*, 386 S.W.3d 745 (Ky. App. 2012). As noted in *Slone*, *Sebastian* remains the controlling precedent in Kentucky regarding installment land sale contracts. Under the *Sebastian* rule, a real estate purchaser, who defaults under an installment land sale contract, still retains an equitable interest in the real property and further possesses redemption rights therein pursuant to Kentucky Revised Statutes (KRS) 426.530. The Kentucky Supreme Court held in *Sebastian* that the forfeiture provision in an installment land sale contract that provided for the forfeiture of the buyers' payment upon the buyers' default was invalid and otherwise not enforceable in Kentucky. The Supreme Court noted that there was no practical distinction between a land sale contract and a purchase money mortgage. The Court made the following observation regarding this issue:

There is no practical distinction between the land sale contract and a purchase money mortgage, in which the seller conveys legal title to the buyer but retains a lien on the property to secure payment. The significant feature of each device is the seller's financing the buyer's purchase of the property, using the property as collateral for the loan.

Where the purchaser of property has given a mortgage and subsequently defaults on his payments, his entire interest in the property is not forfeited. The mortgagor has the right to redeem the property by paying the full debt plus interest and expenses incurred by the creditor due to default. In order to cut off the mortgagor's right to

redeem, the mortgagee must request a court to sell the property at public auction. *See* Lewis, Reeves, How the Doctrine of Equitable Conversion Affects Land Sale Contract Forfeitures, 3 Real Estate Law Journal 249, 253 (1974). *See also* [KRS 426.005](#), [426.525](#). From the proceeds of the sale, the mortgagee recovers the amount owed him on the mortgage, as well as the expenses of bringing suit; the mortgagor is entitled to the balance, if any.

*Sebastian*, 585 S.W.2d at 383.

Effectively, grantors who finance the sale of real property are treated like banks or mortgage institutions that finance real estate transactions and retain mortgages against the property to secure the payment of the indebtedness owed. This public policy is consistent with the legislative mandate that “strict foreclosure” in Kentucky has been abolished, regardless of the method of financing. KRS 426.525. Prior to passage of this statute at common law, a lien holder could unilaterally take possession and control of mortgaged property, thereby eliminating any equity of the mortgagor or owner of the property, as well as extinguishing statutory redemption rights provided for in KRS 426.530. *Sebastian* extended the policy of strict foreclosure prohibition to installment land sale contracts.

The forfeiture clause at issue in this case clearly violates the holding in *Sebastian* and *Slone* and also contravenes KRS 426.525 and KRS 426.530. The forfeiture clause in Watkins’ contract is void and of no effect. The circuit court erred as a matter of law in enforcing the same.

We would further note that the circuit court's conclusion that the contract states that "he [Watkins] is waiving his rights that were established by *Sebastian v. Floyd* . . . ." is also erroneous on its face for two reasons. First, the contract does not contain any language whatsoever regarding the waiver of "*Sebastian* rights." Second, had the contract expressly waived any "rights" from *Sebastian*, this waiver would also have been void on its face. We must emphasize that *Sebastian* did not create "rights" that are subject to waiver. Rather, *Sebastian* established and applied the long-standing law in Kentucky that strict foreclosure is prohibited in any real estate financing transaction, including owner-financed transactions that utilize installment land sale contracts. Until the Supreme Court directs otherwise, any attempt to waive the protections afforded by *Sebastian* are void as a matter of law and the only judicial remedy available to address the alleged breach of an installment land sale contract is a judicial sale of the property. *Sebastian*, 585 S.W.2d 381.

Under the authority of *Sebastian*, 585 S.W.2d 381, a forfeiture clause in an installment land contract is void and will not be given legal effect in this Commonwealth. *See also Slone*, 386 S.W.3d 745.

## II. DAMAGES

Also on appeal is the award by the circuit court of \$311,381.38 in damages to the Eads. Upon entry of judgment, the circuit court ordered the master commissioner to prepare and deliver to the Eads a deed conveying Watkins' interest therein. When this was completed, the circuit court ordered that the

\$311,381.38 judgment would be credited by \$130,000, representing the value of the real estate conveyed as determined by the court, although no appraisals were ordered.

In computing the \$311,381.39 total damage award, the circuit court concluded that \$239,719.88 was owed by Watkins for unpaid *ad valorem* taxes, interest, and principal due under the contract. The circuit court also awarded \$60,796.50 to the Eads as damages for Watkins' removal of fixtures attached to the real property and awarded \$10,865 in attorney's fees to the Eads. We are of the opinion that the circuit court's damage award was erroneous as a matter of law.

First, upon our review of the record we cannot determine exactly how the circuit court established the judgment amount. Other than unsupported testimony by Eads, there is no documented computation or analysis establishing the amount owed, except for an "updated" amortization schedule introduced at the hearing on damages. This document does reflect that Watkins paid a total of \$162,299.96 during the term of the contract. However, the court's August 31, 2012, order makes no reference to these payments or how they were credited. On remand, the circuit court should go through the same or similar analysis and require supporting documentation, evidence, and, if necessary, testimony on how the balance owed was determined, as the court would do in any routine bank foreclosure proceeding. In other words, a detailed accounting should be required, reflecting all payments made and the correct assessment of interest on the unpaid principal, as discussed below.

Additionally, as concerns the assessment of damages to the property in the amount of \$60,756.50 against Watkins, we conclude that KRS 382.350<sup>4</sup> applies to the facts herein. This statute was not addressed by the circuit court in assessing damages. Under KRS 382.350, if Watkins removed or destroyed any fixtures appurtenant to the real property, the Eads are entitled to the “reasonable market value” of such fixtures; however, the sum of indebtedness owed by Watkins would be reduced by said amount. Additionally, we would note that the testimony submitted at the hearing on damages to the property was hearsay at best, and otherwise does not support any award of damages in this case.

### III. INTEREST AND ATTORNEY’S FEES

Upon review of the record and judgment in this case, we cannot determine how interest was calculated or what amount of interest was assessed prior to entry of judgment on unpaid principal amounts. The assessment of interest is expressly controlled by the contract, wherein Paragraph B reads:

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<sup>4</sup> Kentucky Revised Statutes 382.350 reads:

Any person who, with actual or constructive notice of a recorded real property mortgage or vendor's lien, and without the written consent of the record holder thereof, purchases, severs or removes from the land covered by the mortgage or lien, any standing timber, buildings, minerals, or improvements in the nature of fixtures real, covered by and included in the mortgage or lien, and who converts such property to his own use, shall take such property subject to the mortgage or vendor's liens, and the respective priorities thereof, and shall be liable to the holders of the mortgages or liens for a return of such property or for the reasonable market value thereof at the time of the purchase or severance or removal and conversion thereof at the option of the holder of the mortgage or lien. But no holder of a mortgage or a vendor's lien shall recover more than the amount of the indebtedness secured by his mortgage or vendor's lien, and any amount recovered by the holder of the mortgage or vendor's lien shall be credited on the indebtedness secured thereby.

B. The balance of said purchase price . . . shall bear the interest at the rate of 9.5% per annum, simple interest from the execution date of May 1, 1998[,] until paid . . . .

This express provision limits interest on the unpaid balance of this contract to “simple interest.” Simple interest is interest computed solely on principal debt.

*McWilliams v. Northwestern Mutual Life Ins. Co.*, 147 S.W.2d 79 (Ky. 1941).

Simple interest excludes compounding or interest on interest from accruing. See *Black’s Law Dictionary* 817 (7th ed.1999). Given the amount of the judgment and that Eads testified to the accrual of interest on unpaid interest in his computations, we must conclude that the judgment reflects compounded interest therein, which is contrary to the terms of the contract and thus in error as a matter of law. On remand, interest may be computed on principal debt only and may not be compounded and incorporated into principal debt in computing the amount owed. Once the actual amount owed is determined, less credit for all payments made, the property should then be sold at a judicial sale in accordance with applicable law.

As for attorney’s fees, the installment land contract specifically provides for attorney’s fees to the sellers if the sellers “[i]nstitute[s] proceedings to collect the same as if seller had a purchase money lien on said property, pursuant to the holding and guidelines of *Sebastian v. Floyd*, 585 S.W.2d 381 (Ky. 1979), and purchaser agrees to pay all costs thereof, including reasonable attorney fees.” The record is clear that the sellers (the Eads) have not initiated to date a proceeding to seek a judicial sale of the property as required by *Sebastian*, 585 S.W.2d 381.

Seeking the enforcement of a forfeiture clause is not equivalent to proceeding to

collect on a lien claim, including a judicial sale. Consequently, the Eads are not entitled to attorney's fees of \$10,865 at this time, in accordance with the agreement between the parties.

Finally, the Commissioner's Deed, prepared and recorded in the Office of the Bourbon County Clerk prior to this appeal, pursuant to the circuit court's order of October 2, 2012, is hereby rescinded, and of no force and effect.

Upon remand and entry of judgment, the circuit court shall direct that a judicial sale of the real property be conducted in accordance with applicable law, and from the proceeds, the Eads are entitled to recover the balance owed under the land contract as determined by the circuit court in accordance with this opinion.<sup>5</sup> Any remaining balance will be paid to Watkins.

For the foregoing reasons, Appeal Nos. 2012-CA-001655-MR and 2012-CA-001834-MR are reversed and remanded for proceedings consistent with this opinion.

ALL CONCUR.

BRIEFS FOR APPELLANT:

Jerry Anderson  
Barbara Anderson  
Lexington, Kentucky

BRIEF FOR APPELLEES:

Henry C. Prewitt  
Paris, Kentucky

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<sup>5</sup> We find no error in the circuit court's award of ad valorem taxes to the Eads that were paid by the Eads and were obligations owed by Watkins under the contract.