



1982

## Property Law—Mortgages—Validity of Due-on-Sale Clauses in Instruments of Federally Chartered Savings and Loans Upheld

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### Recommended Citation

David G. Paul, *Property Law—Mortgages—Validity of Due-on-Sale Clauses in Instruments of Federally Chartered Savings and Loans Upheld*, 5 U. ARK. LITTLE ROCK L. REV. 569 (1982).

Available at: <https://lawrepository.ualr.edu/lawreview/vol5/iss4/5>

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PROPERTY LAW—MORTGAGES—VALIDITY OF DUE-ON-SALE CLAUSES IN INSTRUMENTS OF FEDERALLY CHARTERED SAVINGS AND LOANS UPHELD. *Fidelity Federal Savings & Loan Association v. de la Cuesta*, 102 S. Ct. 3014 (1982).

Appellant, a California federal savings and loan association chartered by the Federal Home Loan Bank Board, executed deeds of trust to secure certain real estate loans. Each of these instruments contained a “due-on-sale” clause which provided that if the mortgaged property were sold without the prior consent of the lender, the principal and interest would automatically become due and payable.<sup>1</sup> The appellees were individuals who had purchased these properties from the mortgagors without the prior consent of the appellant. After learning of the conveyances, the appellant expressed a willingness to allow the transfers, but only if the appellees agreed to an increase in the mortgage interest rates to reflect current market rates, a common practice in the industry. When the appellees refused to agree to this condition, the appellant accelerated the loans and began non-judicial foreclosures of the mortgaged properties.

The appellees sought injunctive and declaratory relief in the Superior Court of Orange County. The appellees contended that the California Supreme Court decision in *Wellenkamp v. Bank of America*<sup>2</sup> precluded the appellant from exercising the due-on-sale clauses unless it could demonstrate that the transfers would impair the lender’s security or otherwise increase the risk of default. The Superior Court consolidated the cases and granted the appellant’s motion for summary judgment holding that federal savings and loan associations are regulated by the federal government and, therefore, *Wellenkamp* was not controlling. The California Court of Appeals reversed, however, stating that Congress had not expressed the requisite intent to preempt state law concerning due-on-sale clauses and that mortgage and real property law had traditionally

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1. An example of a typical due-on-sale clause is as follows: “Upon the sale or transfer of the premises described herein, or any part thereof, the whole of said principal sum and the interest thereon shall, at the option of the Mortgagee, become immediately due and payable.” 8A. J. RABKIN & M. JOHNSON, CURRENT LEGAL FORMS § 21.70 (1982).

2. 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978) (required a demonstration by the lender that his security had been impaired by the transfer before allowing enforcement of due-on-sale clauses).

been controlled by state law.<sup>3</sup> The United States Supreme Court reversed the decision of the California Court of Appeals, holding that the Federal Home Loan Bank Board's regulation preempted state law in this area and that due-on-sale clauses could be accelerated at will by federally chartered savings and loan associations. *Fidelity Federal Savings & Loan Association v. de la Cuesta*, 102 S. Ct. 3014 (1982).

Although the due-on-sale clause has been widely used only in the last twenty years, early cases upheld other devices giving the grantor the power to restrict future use and alienation of the property.<sup>4</sup> Restrictive clauses in mortgages which provided for the acceleration of principal and interest if the property ceased to be used for particular purposes,<sup>5</sup> and acceleration clauses activated by the mortgagor's failure to pay any installments, taxes, or assessments against the property<sup>6</sup> have generally been held to be valid restraints on alienation. Nevertheless, even during this early period, the courts were not unyielding to the demands of equity when the mortgagor's default could be excused in the eyes of the court.<sup>7</sup>

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3. *de la Cuesta v. Fidelity Fed. Sav. & Loan Ass'n*, 121 Cal. App. 3d 328, 175 Cal. Rptr. 467 (1981).

4. One of the earliest restraints took the form of an oath requiring the grantees of the Abbott of Gloucester not to sell, mortgage, or otherwise transfer the property to any other "religious house without the consent of the monks." Bonanno, *Due on Sale and Prepayment Clauses in Real Estate Financing in Times of Fluctuating Interest Rates—Legal Issues and Alternatives*, 6 U.S.F.L. REV. 267, 271 n.11 (1972). Another form of restraint exercised by the grantor has been the right of re-entry for the breach of a condition subsequent, a restraint generally upheld by the courts. 4 G.W. THOMPSON, THOMPSON ON REAL PROPERTY § 1979, at 388 (1979).

5. In *Board of Church Erection Fund v. First Presbyterian Church*, 19 Wash. 455, 53 P. 671 (1898), the Washington Supreme Court upheld the validity of an acceleration clause contingent upon the failure to use the mortgaged property as a "house of worship" and rejected the mortgagor's contention that the clause was a restraint on alienation and based upon religious beliefs.

In a suit to enforce a materialman's lien on a church building, the Mississippi Supreme Court interpreted another acceleration clause similar to that in *First Presbyterian Church. Planters' Lumber Co. v. Griffin Chapel M.E. Church*, 157 Miss. 714, 128 So. 76 (1930).

6. The mortgagor in *Lewis v. Culbertson*, 124 Conn. 333, 199 A. 642 (1938), failed to pay an insurance premium. Under a state statute incorporated into the mortgage agreement, the mortgagee had the right of reimbursement for any payment he made to protect his secured interests. Although this clause did not explicitly give the mortgagee the right to automatic foreclosure upon the payment of the premium, the court allowed foreclosure after the mortgagor failed to reimburse the mortgagee for such payments.

7. Construing an early example of a due-on-sale clause, the Iowa court relieved the mortgagor of the burdensome clause by basing its decision on mutual mistake. *Merriam v. Leeper*, 192 Iowa 587, 185 N.W. 134 (1921). "It is a general rule in equity that a party to a written contract may not escape the obligations thereof by merely showing that he failed to read the same," but he can be relieved if he can show his failure to read was due to "some

Initially, the California Supreme Court upheld the validity of the due-on-sale clause, finding that the clause was a reasonable restraint upon alienation.<sup>8</sup> Likewise, the California Court of Appeals expressed its view that these types of clauses were valid exercises of contractual power which are necessary to protect the lender's security.<sup>9</sup> Then, in *La Sala v. American Savings and Loan Association*,<sup>10</sup> the California Supreme Court refused to allow the automatic enforcement of a due-on-encumbrance clause. Similar to the due-on-sale clause, this restriction would accelerate the principal and interest if the mortgagor executed a junior mortgage on the secured property. Explaining that automatic enforcement of the clause would be an unreasonable restraint on alienation, the court held that the lender could enforce a due-on-encumbrance clause only if it were reasonably necessary to protect the mortgagee's security.<sup>11</sup> However, the court stated that the decision did not affect the validity of the due-on-sale clause stating that such clauses were enforceable provisions.<sup>12</sup> Finally, the California Supreme Court in *Tucker v. Lassen Savings and Loan Association*<sup>13</sup> applied the rationale of *La Sala* and held that a due-on-sale clause could not be enforced automatically after the mortgagor entered into an installment contract for the sale of the property. In the court's view, the due-on-sale

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artifice or fraudulent connivance instrumental in such prevention." *Id.* at 593, 185 N.W. at 137. The court emphasized the circumstances surrounding the execution of the mortgage and noted the hint of possible fraudulent inducement by the mortgagee's agent.

8. *Coast Bank v. Minderhout*, 61 Cal. 2d 311, 392 P.2d 265, 38 Cal. Rptr. 505 (1964).

9. *Cherry v. Home Sav. & Loan Ass'n*, 276 Cal. App. 2d 574, 81 Cal. Rptr. 135, 138-39 (1969). Most notable was the court's observation that the clause did not prevent the sale of the property, but only provided the option to accelerate upon the purchaser's refusal to accept a higher interest rate. In the court's view, "[s]uch refusal [by the mortgagee to accept the new purchaser without an interest rate increase] demonstrated no lack of good faith or fair dealing," and "[n]either [the mortgagor nor the new purchasers], all of whom were aware of the terms, can complain." *Id.*

10. 5 Cal. 3d 864, 489 P.2d 1113, 97 Cal. Rptr. 849 (1971).

11. *Id.* at 881, 489 P.2d at 1124, 97 Cal. Rptr. at 860.

12. The court distinguished a due-on-sale clause by noting the effect of a sale of the property as opposed to executing a junior mortgage.

A sale of the property usually divests the vendor of any interest in that property, and involves the transfer of possession, with responsibility for maintenance and upkeep, to the vendee. A junior encumbrance, on the other hand, does not terminate the borrower's interests in the property, and rarely involves a transfer of possession.

*Id.* at 880, 489 P.2d at 1123, 97 Cal. Rptr. at 859. The court also noted that the operation of a due-on-sale clause would not seriously impair the right of alienation since "the sale terms can, and usually will, provide for payment of the prior trust deed." *Id.* at 880 n.17, 489 P.2d at 1123 n.17, 97 Cal. Rptr. at 859 n.17.

13. 12 Cal. 3d 629, 526 P.2d 1169, 116 Cal. Rptr. 633 (1974).

clause in this instance would be an unreasonable restraint on alienation, and although the mortgagor would no longer have possession, the potential "dangers of waste and depreciation" did not "justify the *blanket* restraint on alienation."<sup>14</sup> Only upon a demonstration that the conveyance created "a threat to one of [the lender's] legitimate interests" could enforcement be justified.<sup>15</sup> This decision controlled until 1978, when the California Supreme Court decided *Wellenkamp v. Bank of America*.<sup>16</sup> In *Wellenkamp*, the court clarified its position that enforcement of a due-on-sale clause upon an "outright" sale could be activated only upon a showing of impairment of security or an increase in the risk of default.<sup>17</sup>

Sensing possible financial problems for federal savings and loan associations in states like California where due-on-sale clauses were not automatically enforceable,<sup>18</sup> the Federal Home Loan Bank

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14. *Id.* at 638, 526 P.2d at 1174, 116 Cal. Rptr. at 638 (emphasis in original).

15. *Id.* at 639, 526 P.2d at 1175, 116 Cal. Rptr. at 639.

16. 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978).

17. *Id.* at 948-51, 582 P.2d at 973-75, 148 Cal. Rptr. at 382-84. The court noted that its earlier decisions of *La Sala v. American Sav. and Loan Ass'n*, 5 Cal. 3d 864, 489 P.2d 1113, 97 Cal. Rptr. 849 (1971), and *Tucker v. Lassen Sav. & Loan Ass'n*, 12 Cal. 3d 629, 526 P.2d 1169, 116 Cal. Rptr. 633 (1974), were based upon the reasoning that the restraint on alienation of an acceleration upon an outright sale would be minimal. However, the court's use of the term "outright sale" had been used only to include sales when the mortgagor would receive full payment from the new purchaser. As the court pointed out, however, this situation is often not the case as the high cost of new financing may effectively prevent the buyer from substituting a new loan for the one being accelerated. By preventing the new buyer from buying the mortgagor's equity and assuming the old loan, the mortgagee is placing an unreasonable restraint on alienation. Therefore, the court expanded its definition of outright sale to include any transfer by sale of the legal title.

18. Basically, the decisions of various state courts fall into three categories. One group requires impairment of security and/or an increased risk of default before the loan can be accelerated. These states seem to reflect the minority viewpoint. *Patton v. First Fed. Sav. & Loan Ass'n*, 118 Ariz. 473, 578 P.2d 152 (1978); *Tucker v. Pulaski Fed. Sav. & Loan Ass'n*, 252 Ark. 849, 481 S.W.2d 725 (1972); *Wellenkamp v. Bank of America*, 21 Cal. 3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978); *Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n*, 73 Mich. App. 163, 250 N.W.2d 804 (1977); *State ex rel Bingaman v. Valley Sav. & Loan Ass'n*, 97 N.M. 8, 636 P.2d 279 (1981); *Bellingham First Fed. Sav. & Loan Ass'n v. Garrison*, 87 Wash. 2d 437, 553 P.2d 1090 (1976).

The second category consists of those states allowing automatic enforcement. *Provident Fed. Sav. & Loan Ass'n v. Realty Centre, Ltd.*, 101 Ill. App. 3d 277, 428 N.E.2d 170 (1981); *Chapman v. Ford*, 246 Md. 42, 227 A.2d 26 (1967); *Dunham v. Ware Sav. Bank*, 423 N.E.2d 998 (Mass. 1981); *Holiday Acres No. 3 v. Midwest Fed. Sav. & Loan Ass'n*, 308 N.W.2d 471 (Minn. 1981); *First Commercial Title, Inc. v. Holmes*, 92 Nev. 363, 550 P.2d 1271 (1976); *Century Fed. Sav. & Loan Ass'n v. Van Glahn*, 144 N.J. Super. 48, 364 A.2d 558 (1976); *Ceravolo v. Buckner*, 111 Misc. 2d 676, 444 N.Y.S.2d 861 (1981); *People's Sav. Ass'n v. Standard Indus., Inc.*, 22 Ohio App. 2d 35, 257 N.E.2d 406 (1970); *Ministers & Missionaries Benefit Bd. of the Am. Baptist Churches v. Goldsworthy*, 253 Pa. Super. 321, 385 A.2d 358 (1978); *Gunther v. White*, 489 S.W.2d 529 (Tenn. 1973); *Sonny Arnold, Inc. v. Sentry Sav. Ass'n*, 615 S.W.2d 333 (Tex. Civ. App. 1981); *Walker Bank & Trust Co. v. Neilson*, 26 Utah

Board promulgated regulations that allowed member institutions to include due-on-sale clauses in their loan instruments.<sup>19</sup> Noting that the majority of state court decisions had upheld the validity of the clauses, the Board viewed such action as necessary to secure the financial stability of federal savings and loan associations.<sup>20</sup>

After the adoption of these regulations, various suits followed in which federal savings and loan associations sought to establish the enforceability of due-on-sale clauses in their mortgage instruments. In *Glendale Federal Savings & Loan Association v. Fox*<sup>21</sup> the United States District Court for the Central District of California found a clear congressional intent to preempt state regulation of the operation of federal savings and loan associations. The court recognized that the Home Owners' Loan Act of 1933 (HOLA)<sup>22</sup> authorized the Federal Home Loan Bank Board to promulgate those regulations necessary to insure the safe and stable operation of federal savings and loans<sup>23</sup> and that the regulation of due-on-sale

2d 383, 490 P.2d 328 (1971); *Mutual Fed. Sav. & Loan Ass'n v. Wisconsin Wire Works*, 71 Wis. 2d 531, 239 N.W.2d 20 (1976).

The third category contains those states which allow automatic enforcement but specifically note that equity may intervene when the acceleration clause would be unconscionable or inequitable. *Tierce, II v. APS Co.*, 382 So. 2d 485 (Ala. 1979); *Malouff v. Midland Fed. Sav. & Loan Ass'n*, 181 Colo. 294, 509 P.2d 1240 (1973); *Occidental Sav. & Loan Ass'n v. Venco Partnership*, 206 Neb. 469, 293 N.W.2d 843 (1980); *Mills v. Nashua Fed. Sav. & Loan Ass'n*, 121 N.H. 722, 433 A.2d 1312 (1981); *Crockett v. First Fed. Sav. & Loan Ass'n*, 289 N.C. 620, 224 S.E.2d 580 (1976); *Continental Fed. Sav. and Loan Ass'n v. Fetter*, 564 P.2d 1013 (Okla. 1977).

19. Adopted in 1976, the regulation noted that:

An association continues to have the power to include, as a matter of contract between it and the borrower, a provision in its loan instrument whereby the association may, at its option, declare immediately due and payable sums secured by the association's security instrument if all or any part of the real property securing the loan is sold or transferred by the borrower without the association's prior written consent.

12 C.F.R. § 545.8-3(f) (1982).

20. 41 Fed. Reg. 6283, 6285 (1976). The Board outlined four reasons why its decision was necessary. 1) The financial stability of member institutions would be jeopardized by the assumption of the loan by the new purchaser; 2) Eliminating the due-on-sale clause would substantially reduce cash flow and net income of member institutions; 3) The sale of the association's home loans on the secondary market would be severely hampered without the clause; 4) Prohibiting the use of the clause would cause "economic hardship" on the majority of home sellers while benefiting only a small number. *Id.*

21. 459 F. Supp. 903 (C.D. Cal. 1978).

22. 12 U.S.C. §§ 1421-1470 (1976 & Supp. IV 1980).

23. The purpose of HOLA as stated by Congress is:

In order to provide local mutual thrift institutions in which people may invest their funds and in order to provide for the financing of homes, the Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, operation, and regulation of associations to be

clauses in instruments of federal savings and loans was entirely within the regulatory power of the Board.<sup>24</sup> Other federal court decisions that followed *Glendale* reached essentially the same conclusion.<sup>25</sup>

Although it did not have an opportunity to decide the validity of the due-on-sale clause until 1972,<sup>26</sup> the Arkansas Supreme Court generally sustained the validity of acceleration clauses contingent upon the mortgagor's failure to pay an installment, tax, or insurance payment.<sup>27</sup> Yet, in *Johnson v. Guaranty Bank & Trust Co.*,<sup>28</sup> the Arkansas Supreme Court, while sustaining an acceleration clause, noted that equity would shield the mortgagor from the harsh effects of an acceleration clause in those instances in which the mortgagee's conduct would render enforcement of the clause inequitable.<sup>29</sup>

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known as "Federal Savings and Loan Associations," and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home financing institutions in the United States.

12 U.S.C. § 1464(a)(1) (1976).

24. The court in *Glendale* stated:

The language, history, structure and purpose of the Home Owner's Loan Act evidence a clear Congressional intent to delegate to the Bank Board complete authority to regulate federal savings and loan associations and to preempt state regulation. Whenever the Bank Board pursuant to that plenary authority, promulgates a regulation governing an aspect of the operation of federal savings and loan associations, that regulation governs exclusively and preempts any attempt by a state to regulate in that area.

*Glendale Fed. Sav. & Loan Ass'n v. Fox*, 459 F. Supp. 903, 910 (C.D. Cal. 1978).

25. See, e.g., *First Fed. Sav. & Loan Ass'n v. Myrick*, 533 F. Supp. 1041 (W.D. Ark. 1982); *Price v. Florida Fed. Sav. and Loan Ass'n*, 524 F. Supp. 175 (M.D. Fla. 1981); *First Fed. Sav. & Loan Ass'n v. Peterson*, 516 F. Supp. 732 (N.D. Fla. 1981); *Conference of Fed. Sav. & Loan Ass'ns v. Stein*, 495 F. Supp. 12 (E.D. Cal. 1979); *Bailey v. First Fed. Sav. & Loan Ass'n*, 467 F. Supp. 1139 (C.D. Ill. 1979).

However, the Fourth Circuit Court of Appeals in *Williams v. First Fed. Sav. and Loan Ass'n*, 651 F.2d 910 (4th Cir. 1981), avoided the preemption question by holding that due-on-sale clauses were valid restraints on alienation. The court noted the possible preemption of any state law regulating the enforcement of due-on-sale clauses in instruments of federal savings and loan institutions. Choosing to avoid the preemption question, the court held that due-on-sale clauses do not contravene Virginia law. Barring any inequitable circumstances which would render the clause unenforceable, the court believed that lenders should be able to rely on the clause and stated that "[t]here is nothing inherently unfair or unreasonable in such a rule." *Id.* at 927.

26. *Tucker v. Pulaski Fed. Sav. & Loan Ass'n*, 252 Ark. 849, 481 S.W.2d 725 (1972).

27. *Hume v. Indiana Nat. Life Ins. Co.*, 155 Ark. 466, 245 S.W. 19 (1922) (court upheld an acceleration clause contingent on the failure of the mortgagor to pay taxes on the property); *Mooney v. Tyler*, 68 Ark. 314, 57 S.W. 1105 (1900) (an acceleration clause contingent on the mortgagor's failure to make an insurance payment was upheld); *Farnsworth v. Hoover*, 66 Ark. 367, 50 S.W. 865 (1899) (court upheld on acceleration clause contingent on the mortgagor's failure to pay an interest installment).

28. 177 Ark. 770, 9 S.W.2d 3 (1928).

29. *Id.* at 773, 9 S.W.2d at 5. The court upheld a provision for acceleration of the debt

These decisions controlled until 1972 when the Arkansas Supreme Court decided *Tucker v. Pulaski Federal Savings & Loan Association*.<sup>30</sup> In dealing with the due-on-sale clause for the first time, the court held that a clause which provided for acceleration of the principal and interest upon the sale of the property could not be exercised unless there existed "legitimate grounds for refusal to accept a transfer to a particular individual or concern."<sup>31</sup> While the court clearly prohibited arbitrary enforcement, the basis for the court's decision in *Tucker* is not clear.<sup>32</sup> The court failed to specify what constituted "legitimate grounds" for acceleration, although it seemed to emphasize the mortgagee's failure to demonstrate impairment of security.<sup>33</sup> The validity of the *Tucker* decision, however, was cast in doubt by *First Federal Savings & Loan Association v. Myrick*.<sup>34</sup> This decision by the United States District Court for the Western District of Arkansas followed the rationale of earlier federal court decisions

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upon the failure of the mortgagor to pay any note, interest installment, taxes or special assessments. However, the court did specify certain equitable grounds upon which it could relieve the mortgagor: if the acceleration clause is waived by the mortgagee; if the mortgagor's default is the result of accident or mistake; or if the acceleration clause is procured by fraud or some other inequitable conduct of the lender.

In *Harrell v. Perkins*, 216 Ark. 579, 226 S.W.2d 803 (1950), the court barred the enforcement of the acceleration clause basing its decision upon the equitable powers of the court. Concluding that the actions of the mortgagee had caused the mortgagor's default, the court held that the acceleration would be unconscionable. Similarly, the court later ruled that an acceleration upon a 48-hour delay in payment would be an inequitable acceleration. See the supplemental opinion in *Seay v. Davis*, 246 Ark. 201, 438 S.W.2d 479, *reh'g denied*, 246 Ark. 627, 438 S.W.2d 479 (1969).

30. 252 Ark. 849, 481 S.W.2d 725 (1972).

31. *Id.* at 855, 481 S.W.2d at 729. Specifically, the court noted the reasoning in *Baltimore Life Ins. Co. v. Harn*, 15 Ariz. App. 78, 486 P.2d 190 (1971), and quoted extensively from it:

Absent an allegation that the purpose of the clause is in some respect being circumvented or that the mortgagee's security is jeopardized, a plaintiff cannot be entitled to equitable relief. Otherwise the equitable powers of the trial court would be invoked to impose an extreme penalty on a mortgagor with no showing that he has violated the substance of the agreement, that is, that he would not make a conveyance that would impair the security.

*Tucker v. Pulaski Fed. Sav. & Loan Ass'n*, 252 Ark. 849, 854, 481 S.W.2d 725, 729 (1972) (quoting *Baltimore Life Ins. Co. v. Harn*, 15 Ariz. App. 78, 486 P.2d 190, 193 (1971)).

32. As one commentator noted, "it is not altogether clear whether the court was basing its decision upon the requirement that restraints be reasonable or upon its equitable powers to deny foreclosure. . . ." Finch, *Due-On-Sale Clauses in Debt Instruments: Reconciling Legal Doctrine and Market Realities*, 98 BANKING L.J. 300, 304 (1981).

33. In quoting from *Baltimore Life Ins. Co. v. Harn*, the court emphasized the language used by the Arizona court that "[a]t no place in the pleading does an allegation appear that the plaintiff's security is in any way jeopardized." 252 Ark. at 855, 481 S.W.2d at 729 (quoting *Baltimore Life Ins. Co. v. Harn*, 15 Ariz. App. 78, 486 P.2d 190, 193 (1971)).

34. 533 F. Supp. 1041 (W.D. Ark. 1982).

and held that due-on-sale clauses were enforceable by Arkansas federal savings and loan institutions.

The United States Supreme Court in *Fidelity Federal Savings and Loan Association v. de la Cuesta*<sup>35</sup> settled the question whether the Federal Home Loan Bank Board's regulations permitting federally-chartered savings and loan institutions to enforce due-on-sale clauses preempted state law in the area. The Court recognized that federal preemption may be evidenced by an express statement of congressional intent to preempt state law, or it may be implied when the regulatory scheme reasonably precludes any supplemental action by the states.<sup>36</sup> Preemptive intent can also be found if state law directly opposes the intended congressional purposes or otherwise conflicts with federal law.<sup>37</sup> The Court also noted that federal regulations have the same preemptive effect as federal law if the regulations are reasonably promulgated and are consistent with the authorizing statute.<sup>38</sup> To afford the regulation allowing due-on-sale clauses preemptive status the Court had to determine whether the regulation was within the scope of the authorizing statute, the Home Owners' Loan Act of 1933 (HOLA).<sup>39</sup> The Court noted that HOLA was a response by Congress to the unstable banking conditions created by the great depression and was enacted to provide stable and secure savings institutions.<sup>40</sup> The congressional intent was to prescribe regulations which reflected "accepted" and "sound" banking practices for the savings institutions and not merely an adoption of local practices.<sup>41</sup> In short, the Federal Home Loan Bank Board was not bound by state law.<sup>42</sup> The Board's desire that enforcement of the clauses be governed by federal law is stated clearly in the regulation,<sup>43</sup> and the Court held that federal savings and loan associations are authorized to enforce the clauses without a showing of impair-

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35. 102 S. Ct. 3014 (1982).

36. *Id.* at 3022.

37. *Id.*

38. *Id.* at 3022-23.

39. 12 U.S.C. §§ 1461-1470 (1976 & Supp. IV 1980).

40. 102 S. Ct. at 3025-26.

41. [T]he Board is authorized, under such rules and regulations as it may prescribe, to provide for the organization, incorporation, examination, *operation*, and *regulation* of associations to be known as 'Federal Savings and Loan Associations' or 'Federal mutual savings banks' . . . , and to issue charters therefor, giving primary consideration to the best practices of local mutual thrift and home-financing institutions in the United States.

*Id.* at 3026 (quoting § 5(a) of HOLA) (emphasis in original).

42. 102 S. Ct. at 3024-25.

43. "Due-on-sale practices of Federal associations shall be governed exclusively by the

ment of security, a requirement of the *Wellenkamp* doctrine.<sup>44</sup>

The question unresolved by *Fidelity Federal* is whether states may continue to restrict enforcement of due-on-sale clauses by mortgagees other than federally chartered savings and loan institutions. Even though *Fidelity Federal* was limited to the Federal Home Loan Bank Board's regulations, the decision could apply to similar regulations promulgated by other federal banking authorities.<sup>45</sup> Subject only to the limits of the agency's authorizing statute,<sup>46</sup> the regulations of these other federal banking authorities could very well preempt state law governing due-on-sale clauses.

The question also remains whether *Fidelity Federal* will have

Board's regulations in preemption of and without regard to any limitations imposed by state law on either their inclusion [sic] or exercise. . . ." 12 C.F.R. § 556.9(f)(2) (1982).

44. 102 S. Ct. at 3030-31.

45. The banking industry is a virtual labyrinth of intertwining federal and state regulatory and statutory controls. Banks and savings and loans can choose to be either federally or state chartered. State-chartered institutions can come under federal regulatory authority by electing to insure their assets under the Federal Depository Insurance Corporation or the Federal Savings and Loan Insurance Corporation. The overall perspective is complicated further by the election of state banks to become members of the Federal Reserve System, thus subjecting themselves to the regulatory authority of the Board of Governors. In short, "[t]he dual banking system . . . is not a simplistic system of supervision by two separate authorities; it is a system in which federal regulation operates side by side with state regulation." 1 W. SCHLICHTING, T. RICE & J. COOPER, *BANKING LAW* § 2.03 (1982).

The Comptroller of the Currency, the regulatory authority which controls national banks, is currently considering a proposed regulation allowing the inclusion and enforcement of due-on-sale clauses in instruments of national banks. 47 Fed. Reg. 18476 (1982). The Comptroller has also drafted a proposed regulation allowing a national bank to prohibit assumption of an outstanding loan by a new purchaser. 47 Fed. Reg. 23944, 23948 (1982) (to be codified at 12 C.F.R. § 29.6). This regulation expressly provides for preemption of state law.

The staff of the Board of Governors of the Federal Reserve System is also planning to revise its official commentary to Regulation Z (Truth in Lending) "to clarify that a due-on-sale clause is not considered a demand feature requiring disclosure." 47 Fed. Reg. 20603, 20606 (1982).

The National Credit Union Administration has also amended its regulations to require federal credit unions to include due-on-sale clauses in their long-term mortgage instruments. 12 C.F.R. § 701.21-6(d) (1982).

Subsequent to the *Fidelity Federal* decision, Congress passed the Garn-St. Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469 (1982), which answered many of the questions posed in the text. In short, the act allows the enforcement of a "due-on-sale" clause by the "lender," defining "lender" as "a person or government agency making a real property loan or any assignee or transferee, in whole or in part, of such a person or agency." Pub. L. 97-320, § 341(a)(2), 96 Stat. at 1505.

46. The purposes and objectives of HOLA, *supra* note 23, played a key role in the Court's decision. Under the authority of HOLA, the Board's concern is that of insuring the continued and stable financial operations of federal savings and loans. The authorizing statutes of other federal banking authorities face the same careful review to determine whether their regulatory measures have the same preemptive effect over state law.

any effect on the enforcement of due-on-sale clauses by state chartered institutions. Unless subject to the control of a federal banking authority governed by *Fidelity Federal*, the decision would not prevent the continued application of *Tucker* to Arkansas' state chartered institutions. This imbalance would create an obvious economic advantage in favor of federally chartered counterparts and could be viewed as an incentive for state institutions to obtain a federal charter.<sup>47</sup> Additional relief exists for Arkansas institutions since state statutes allow the state agencies which regulate state banks and savings and loans to confer "business practices" enjoyed by federal institutions upon state chartered institutions.<sup>48</sup>

Looking beyond the enforcement questions presented by *Fidelity Federal*, one must consider the possible effects of the decision on the real estate market served by lending institutions. While an argument exists that preventing the assumption of low interest loans by home buyers could have a serious effect on the already depressed real estate market,<sup>49</sup> lending institutions are quick to point out detrimental consequences on home financing caused by the inability of lenders to enforce due-on-sale clauses.<sup>50</sup> For the most part, the wis-

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47. Specifically, 12 U.S.C. § 1464(i) (1976 & Supp. IV 1980) and 12 C.F.R. § 543.9 (1982) outline the procedure for the conversion of state savings and loans into federal institutions. Under 12 U.S.C. § 35 (1976), state banks can convert into a national banking association.

48. Under Arkansas law, the Savings and Loan Association Board has the power to allow state-chartered institutions to "[a]dopt any business practice, procedure, method of system authorized for a Federal Association doing business in this State." ARK. STAT. ANN. § 67-1858 (1980). Similarly, the State Bank Commissioner, with the approval of the State Banking Board, can "authorize state banks to engage in any banking activities in which said banks could engage were they acting as national banks at the time such authority is granted." ARK. STAT. ANN. § 67-501.1(o) (1980). The Arkansas State Savings and Loan Association Board did adopt regulations allowing state savings and loan associations to offer any form of mortgage which is authorized for federal associations. These regulations were used as the basis of the Arkansas Supreme Court's decision in *Schulte v. Benton Savings and Loan Association*, No. 83-74 (Ark. May 31, 1983), which held that state savings and loan associations were no longer bound by *Tucker v. Pulaski Federal Savings & Loan Ass'n*, 252 Ark. 849, 481 S.W.2d 725 (1972) and that state associations could enforce the due-on-sale clause without a showing of impairment of security.

49. Many individuals in the real estate industry view the *Fidelity Federal* decision as a further burden on the real estate market. Since some home buyers are unable to afford the current market rates, real estate sales will decline and/or the seller will be forced to reduce his asking price to accommodate the new buyer who is unable to assume the seller's mortgage. Andrew, *Assumable-Mortgages Ruling Seen Further Hurting Market*, Wall St. J., June 30, 1982, at 25, col. 1.

50. As one author points out, the detrimental effects of the inability to maintain mortgages at current market rates outweigh any benefit received by the few home buyers who assume low interest mortgages. The increased costs to the lender, created by rising interest rates and the assumption of low interest mortgages by buyers, can pose a severe reduction in

dom of the Board's regulation is yet to be seen, and as the *Fidelity Federal* decision indicates, any change in the due-on-sale regulations must come not from the courts but from the agency itself. Yet, in light of the Board's express purpose and primary interest in protecting the interests and security of member institutions, any move in that direction by the Board may be slow in coming.

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the lender's return on real estate investments. This reduction in the lender's return would also result in lower rates offered depositors by lending institutions. In addition, new borrowers who are unable to assume existing mortgages will find increased interest rates as lenders attempt to recover lost profits from low interest mortgages. Yet another adverse effect on borrowers could be the replacement of long term loans with loans amortized over periods of less than ten years, a measure which will find some borrowers unable to pay the increased monthly payments. Finch, *Due-On-Sale Clauses in Debt Instruments: Reconciling Legal Doctrine and Market Realities*, 98 *BANKING L.J.* 300, 338-40 (1981).

