REAL ESTATE CONTRACTS-DUE-ON-SALE CLAUSES DO NOT VIOLATE PUBLIC POLICY AND ARE VALID AND ENFORCEABLE SUBJECT TO STATUTORY LIMITATIONS IN IOWA. — *Martin v. Peoples Mutual Savings and Loan Association* (Iowa 1982).

On September 9, 1979, James and Georgeann Martin purchased a residential property from Brian and Kathleen Jorgensen.[1] The Jorgensens had purchased the home in April, 1978, with financing secured in part by a first mortgage from Peoples Mutual Savings and Loan (Peoples Mutual),[2] an Iowa chartered financial institution.[3] The Jorgensens' mortgage included a provision known as a "due-on-sale clause" which provided that, if the borrower sold or transferred the property without the lender's prior written consent, the lender could declare all sums owed the lender immediately due and payable.[4] The mortgage agreement further stated that, if the lender agreed to the transfer, the mortgage could only be assumed at a rate of interest set by the lender.[5]

The Martins sought to assume the obligations under the Jorgensens' mortgage with Peoples Mutual.[6] The lender approved assumption of the mortgage at an interest rate of eleven per cent, rather than the lesser rate demanded in the original mortgage agreement.[7] The Martins declined to accept the assumption agreement at the higher rate of interest,[8] and instead signed a supplemental agreement with the Jorgensens withdrawing the mortgage assuming condition.[9] Mrs. Jorgensen later admitted that a Peoples Mutual loan officer had informed her that the loan was not assumable without consent of the lender.[10] In accordance with Federal Reserve Regulation

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1. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220, 222 (Iowa 1982).
2. *Id.* at 221.
3. *Id.* at 226.
4. *Id.* at 221, 222. The mortgage included the following acceleration provision:
   > If all or any part of the Property . . . is sold or transferred by Borrower without Lender's prior written consent . . . Lender may, at Lender's option, declare all the sums secured by this Mortgage to be immediately due and payable. Lender shall have waived such option to accelerate if, prior to the sale or transfer, Lender and the person to whom the Property is to be sold or transferred reach agreement in writing that the credit of such person is satisfactory to Lender and that the interest payable on the sums secured by this Mortgage shall be at such rate as Lender shall request.

   Id. at 222.
5. *Id.*
6. *Id.*
7. *Id.* The court did not specify what the interest rate was in the original note. *See id.* The rate, however, appeared to be approximately nine per cent. *Id.*
8. *Id.* at 223.
9. *Id.*
10. *Id.* at 222.

Z,[11] the loan agreement also included in typing twice as large as the other sections: "This Loan is not assumable without Lender consent."[12]

The Martins received the property on October 25, 1971, subject to[13] the Jorgensens' mortgage.[14] On November 6, 1979, Peoples Mutual demanded that the Jorgensens make full payment of the mortgage balance.[15] The Martins brought an action in equity seeking a declaratory judgment to nullify the due-on-sale acceleration clause in the mortgage.[16] The trial court construed Iowa law[17] as preventing the enforcement of the due-on-sale clause.[18] The Iowa Supreme Court *held*, reversed and remanded.[19] Due-on-sale clauses do not violate public policy and are valid and enforceable subject to statutory limitations in Iowa. *Martin v. Peoples Mutual Savings and Loan Association*, 319 N.W.2d 220 (Iowa 1982).

The Iowa Supreme Court in *Martin* divided its discussion of due-on-sale clauses[20] in mortgage assumption contracts into two main issues.[21] First, the court examined Iowa statutory law to determine whether Peoples Mutual was prohibited from enforcing the due-on-sale clause to accelerate the loan balance due under its mortgage.[22] Second, the court investigated Iowa common law to resolve whether it restricted utilization by Peoples Mutual of due-on-sale clauses in mortgages.[23]

The trial court had ruled against acceleration by Peoples Mutual of the loan balance under its due-on-sale clause in the Jorgensens' mortgage.[24] The lower court found that the mortgage acceleration violated Iowa statutory provisions concerning maximum rates of interest.[25] The trial court applied

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11. Truth in Lending Act, 12 C.F.R. § 226 (1982).

12. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 222.

13. *Id.* at 223. "Mortgagors commonly transfer real estate 'subject' to an existing mortgage." G. OSBORNE, REAL ESTATE FINANCE LAW § 5.3 at 251 (1979). This type of transfer erases any personal liability of the original holder to pay the note. *Id.* § 5.3 at 251-52. The transferee bears the burden of payment of the mortgage or risks losing the land in the case of default. *Id.*

14. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223.

15. *Id.*

16. *Id.*

17. IOWA CODE § 535.2(4) (1979).

18. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223. The grounds for the trial court's decision are discussed at *infra* notes 23-26 and accompanying text.

19. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 221.

20. "The due on sale clause is a specialized type of acceleration clause that gives the mortgagee the option of declaring the entire debt due and payable in the event the mortgagor transfers or encumbers the mortgaged real estate." G. OSBORNE, *supra* note 13, § 5.21 at 295 (1979).

21. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223, 225.

22. *Id.* at 223.

23. *Id.* at 225.

24. *Id.* at 221.

25. *Id.* at 223. The trial court specifically analyzed Iowa Code section 535.2(4) (1979). Black Hawk District Court Transcript at 324, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

section 535.2(4) of the Iowa Code to the Jorgensen mortgage agreement and held that Peoples Mutual could not validly adjust the interest rate above the rate in the agreement which the Martins were assuming.[26] The trial court also determined that the Iowa legislature had intended that due-on-sale clauses would only be enforced if the lender could prove the likelihood that repayment would be impaired or the property damaged.[27]

In its analysis the Iowa Supreme Court strictly construed the language of section 535.2(4) and rejected the trial court's judgment that Peoples Mutual violated that section by attempting to increase the interest rate in the original mortgage agreement which the Martins wished to assume.[28] The Martins had contended that the mortgage acceleration clause was a provision for the adjustment of interest rates as the term "adjustment" is used in subsection 535.2(4).[29] The statute states:

> Notwithstanding the provisions of subsection three, with respect to any agreement which was executed prior to August 3, 1978, and which contained a provision for the adjustment of the rate of interest specified in the agreement, the maximum lawful rate of interest which may be imposed under that agreement shall be nine cents on the hundred by the year, and any excess charge shall be in violation of section 535.4.[30]

The supreme court concluded that just any adjustment does not trigger the applicable Code subsection: only those made before August 3, 1978, which contain a clause allowing an adjustment of the interest rate as that agreement specifies.[31] The Iowa Supreme Court pointed out that the Martins entered a separate, second agreement with Peoples Mutual, and thus could not "invoke the subsection 535.2(4) interest ceiling because an interest rate in a subsequent agreement is not imposed 'under that agreement' that 'contained a provision for the adjustment of the rate of interest.' "[32] It appears that this reasoning, however, is questionable. A new security instrument was not created; the Martins were merely assuming the Jorgensen mortgage.[33]

The court also noted that the Martins' agreement with Peoples Mutual consisted of two components: the mortgage agreement and the promissory note, which together constituted the total contract.[34] The court pointed out

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26. Black Hawk District Court Transcript at 324, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

27. Black Hawk District Court Transcript at 325, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220, 224 (Iowa 1982). *See also* IOWA CODE § 535.8(2)(c) (providing that "it [is] unlawful to invoke due on sale clauses on mortgages executed after July 1, 1979 unless the party assuming the loan will jeopardize repayment of the loan or impair the security.").

28. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223.

29. *Id.* at 223-24.

30. IOWA CODE § 535.2(4) (1979).

31. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223.

32. *Id.* at 224.

33. *Id.* at 222.

34. *Id.* at 223. *See* Frenzel v. Frenzel, 152 N.W.2d 157, 160 (Iowa 1967).

that since the note exclusively mentioned interest rates, subsection 535.2(4) was pertinent to its provisions only.[35]

This concept was originally established in *Frenzel v. Frenzel*,[36] where the note provided that the holder could accelerate payment upon default, but the mortgage declared that failure to pay would cause the whole sum to become due.[37] The *Frenzel* court held that the note provision was controlling, and the mortgage was only incidental to the principle obligations contained in the note.[38]

In adherence to the precedent set in *Frenzel*, the *Martin* court held that the note set the interest rate and, therefore, the mortgage acceleration clause had no control over the interest agreement.[39] Yet, it was mortgage paragraph seventeen, which contained the due-on-sale clause, that specifically allowed the lender to adjust the interest rate upon assumption of the mortgage.[40] The court stated that an assumption contract between Peoples Mutual and a third party would be the only agreement which would enable Peoples Mutual to change the interest rate.[41] The Iowa court thus held a second agreement, such as that between the Martins and Peoples Mutual, would not invoke subsection 535.2(4) of the Code.[42] While the court's logic appears flawless, in reality the Martins were not entering a separate agreement with Peoples Mutual; they desired merely to assume the Jorgensens' mortgage.[43]

The Martins also argued that the supreme court could prohibit the enforcement of due-on-sale clauses in accordance with legislative intent.[44] The court examined legislative intent and rejected the Martins' rationale.[45] The court found that subsection 535.2(4) was enacted in 1978[46] and that the Iowa legislature did not impose any limitation on due-on-sale clauses until 1979.[47] The 1978 interest rate limitation in section 535.2(4), however, was passed at a time when interest rates were below nine per cent.[48] The court's interpretation was much narrower than the legislature intended; the due-on-sale limitation was passed in response to the more frequent invocation of the

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35. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223.
36. 152 N.W.2d 157 (Iowa 1967).
37. *Id.* at 158.
38. *Id.* at 160.
39. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223.
40. *See supra* note 4 and accompanying text.
41. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 224.
42. *Id.*
43. *Id.* at 222.
44. *Id.* at 224.
45. *Id.* The court determined legislative intent by examining the language of the statutes and any changes made by the legislature as recorded in the Iowa Acts. *Id.*
46. 1978 IOWA ACTS ch. 1190, § 11.
47. 1979 IOWA ACTS ch. 132, § 16.
48. Black Hawk District Court Trial Transcript at 200, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

clauses as a result of increasing interest rates.[49]

The Martins noted that subsection 535.8(2)(c) "makes it unlawful for Iowa lenders to invoke due-on-sale clauses on mortgages executed after July 1, 1979, unless the party that is assuming the loan or mortgage will jeopardize repayment of the loan or impair the security."[50] The Martins argued that since the legislature passed subsection 535.8(2)(c) the court should have construed 535.2(4) in the home buyer's favor to provide Iowa with a more homogeneous policy.[51] The court, however, found an amendment that was not passed into law which would have made the provision of subsection 535.8(2)(c) retroactive.[52] The court interpreted this action as legislative intent that the due-on-sale limitation was not to be applied retroactively.[53]

In *IPALCO Employees Credit Union v. Culver*,[54] the Iowa Supreme Court analyzed section 4.5 of the Code which states: "A statute is presumed to be prospective in its operation unless expressly made retroactive,"[55] as applicable to an action for the balance due on an unpaid note.[56] The court held that a retroactive application deprived the note holder of rights held under the Code at the time the note was executed.[57]

The *Martin* court rejected the trial court's ruling that the mortgage acceleration clause had a provision for the adjustment of interest.[58] The supreme court's analysis of the Martin agreement with Peoples Mutual as being completely separate from the Jorgensen agreement to avoid application of the interest limitation of section 535.2(4) stretches the concept of mortgage assumption.[59] Iowa law allows enforcement of due-on-sale acceleration clauses within interest ceiling limitations on notes executed prior to 1979, such as the Martins' note with Peoples Mutual.[60]

After dispensing with its examination of the applicability of section 535.2(4) of the Code to due-on-sale provisions, the *Martin* court addressed the issue of whether such acceleration clauses are prohibited under Iowa

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49. *Id.*, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982). The Martins argued that implementation of due-on-sale clauses made real estate transactions more difficult and were, therefore, not in the public benefit. *Id.*, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

50. *Id.* at 199, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982) (citing IOWA CODE § 535.8(2)(c) (Iowa 1981).

51. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 224-25.

52. 1980 IOWA ACTS ch. 1156, § 8.

53. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 225.

54. 309 N.W.2d 484 (Iowa 1981).

55. IOWA CODE § 4.5 (1981).

56. IPALCO Employees Credit Union v. Culver, 309 N.W.2d at 484.

57. *Id.* at 487.

58. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 223-25.

59. When a purchaser assumes a mortgage he becomes personally liable for the debt, and agrees to pay the mortgage according to its terms. G. OSBORNE, *supra* note 13, §§ 5.4 - .5 at 253-54.

60. IOWA CODE § 535.8(2)(c) (1981).

common law.[61] The Martins focused their allegations against due-on-sale clauses as restraints on the alienation of property.[62] It was the Martins' contention that homeowners would not be able to sell their homes because the due-on-sale clauses in their mortgages would force them to pay the mortgage in full when the property was transferred, and few people have the ability to do that.[63]

The court adhered to the precedent established in *Swearingen v. Lahner*,[64] and *Federal Land Bank v. Wilmarth*,[65] observing that Iowa law accepted the usage of acceleration clauses.[66] In *Swearingen* an action was brought to foreclose a mortgage on a note which contained an acceleration clause that was enforceable upon nonpayment of the interest.[67] The *Swearingen* court held that this agreement should be considered under contract law;[68] the provisions induced an earlier maturity of the note and could not be construed as a penalty of forfeiture.[69] The *Martin* court, however, failed to observe a major distinction between that case and *Swearingen*. The acceleration clause in *Swearingen* allowed the lender to accelerate the debt and interest due when the borrower defaulted on the interest payments.[70] The acceleration clause in *Martin* gave Peoples Mutual the option to raise interest rates when the property was transferred despite evidence that the Martins were a no bigger credit risk than the Jorgensens.[71]

The *Martin* court also noted that under Iowa commercial law acceleration clauses are common practice.[72] In *Farmers Co-Operative Elevator Inc. v. State Bank*,[73] the supreme court placed the burden on the borrower to prove that the lender did not accelerate payment under a good faith belief that prospective payment was impaired.[74] The *Martin* court, however, failed to note that the Martins' situation involved homeowners, not professional property brokers, as in most commercial law cases.[75]

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61. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 225.

62. *Id.* "[T]he major judicial attack on these clauses centers on the restraint on alienation doctrine. . . ." G. OSBORNE, *supra* note 13, § 5.21 at 297.

63. Appellees' Brief at 20, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

64. 93 Iowa 147, 61 N.W. 431 (1894).

65. 218 Iowa, 339, 252 N.W. 507 (1934).

66. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 225.

67. Swearingen v. Lahner, 93 Iowa at 148-49, 61 N.W. at 432.

68. *Id.* at 150, 61 N.W. at 433.

69. *Id.*

70. *Id.* at 148-49, 61 N.W. at 432.

71. Black Hawk County District Court Trial Transcript at 77-81, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

72. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 225 (citing Farmers Trust and Sav. Bank v. Manning, 311 N.W.2d 255 (Iowa 1981)).

73. 236 N.W.2d 674 (Iowa 1975).

74. *Id.* at 677.

75. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 225.

The Iowa Supreme Court had established the basis for upholding due-on-assignment clauses in real estate contracts in *Risser v. Union Securities Co.*[76] The court in *Risser* stressed that each party had knowledge of the acceleration provision and expressly agreed to it by signing the contract.[77] Due-on-assignment clauses in leases which provided for termination in the event that the lessee assigned or sublet the premises were also held valid in Iowa in *Snyder v. Bernstein Bros.*[78] The *Snyder* court analysis paralleled *Risser* with regard to acceleration provisions as a validly acknowledged section of a contract signed by both parties.[79]

The Martins also attacked the use of due-on-sale clauses in loan contracts as repugnant to public policy.[80] The court answered this attack by adhering to the right of the general public to contract, as discussed in *Tschirgi v. Merchants National Bank.*[81] In Iowa the ability of a court to void contracts on the basis of public policy is a delicate task which may be exercised only in clear-cut cases.[82] The *Martin* court emphasized that the Martins were not a party to the contract which they sought to invalidate for public policy reasons.[83] The argument of the court appears to be one of form over substance; it was obvious that the Martins had little option but to accept the contract terms as presented by Peoples Mutual.

The Nebraska Supreme Court had similarily dealt with the issue of whether due-on-sale clauses are repugnant to public policy.[84] In *Occidental Savings and Loan Association v. Venco Partnership,*[85] the Nebraska court considered the validity of due-on-sale clauses.[86] The *Venco* court advocated liberty of contract over public policy considerations, unless public welfare demanded nullification of the contract.[87] Although the Nebraska court decision in *Venco* was not binding on the Iowa court, Iowa clearly found the language persuasive.[88] This analysis coupled with previously established precedents in Iowa convinced the *Martin* court that due-on-sale clauses were allowable in Iowa.[89] In addressing the Martins' public policy argument,

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76. 200 Iowa 987, 205 N.W. 648 (1925).
77. *Id.* at 990, 205 N.W. at 649.
78. 201 Iowa 931, 208 N.W. 503 (1926).
79. *Id.* at 934-35, 208 N.W. at 504.
80. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 226.
81. 253 Iowa 682, 113 N.W.2d 226 (1962) (citing Richmond v. Dubuque & Sioux City R.R. Co., 26 Iowa 791, 202 (1868)).
82. Tschirgi v. Merchants Nat'l Bank, 253 Iowa at 691, 113 N.W.2d at 226-28.
83. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 226.
84. Occidental Sav. and Loan Ass'n v. Venco Partnership, 206 Neb. 469, ____, 293 N.W.2d 843, 848 (1980). *See infra* notes 98-105 and accompanying text.
85. 206 Neb. 469, 293 N.W.2d 843 (1980).
86. *Id.* at ____, 293 N.W.2d at 844.
87. *Id.* at ____, 293 N.W.2d at 849 (citing E.K. Buck Retail Stores v. Harket, 157 Neb. 867, ____, 62 N.W.2d 288, 301 (1954)).
88. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 227-28.
89. *Id.*

the court also directed its attention to the economic consequences that nullification of due-on-sale clauses would induce.[90] Peoples Mutual is a state chartered savings and loan association.[91] In examining the association's lending policies the court found that, prior to the 1970's, loan repayment was within seven years of execution.[92] This presented the savings and loan with a greater opportunity to adjust interest rates on loans to current levels.[93] The Iowa court pointed out that the rapid increase in interest rates during the 1970's caused the savings and loan to adjust interest rates on loans by invoking the due-on-sale provisions.[94] This practice became necessary to eliminate a potential economic hardship on the savings and loans because people invested their money in savings certificates that paid higher rates than Peoples Mutual received on notes.[95] There was evidence at trial that an assumption by the Martins of the Jorgensen mortgage would not hurt Peoples Mutual; there were twenty-eight and one half years left on the Jorgensen mortgage when the Martins tried to assume it.[96] This was money already borrowed by Peoples Mutual at the lower interest rate.[97]

The *Martin* court reasoned that if due-on-sale clauses were invalidated in Iowa, then mortgages with interest rates lower than the current market rate would not be prepaid because there was no other instrument to ensure savings and loans a recovery of money upon the sale of a house.[98] The Iowa Supreme Court believed such a policy would cause savings and loans to charge new borrowers higher interest rates than necessary due to the difference between the interest a savings and loan is required to pay on deposits and that received on older loans.[99] This conclusion is seriously weakened by the fact that the assets of Peoples Mutual increased by an additional nine million dollars in 1979.[100]

The Nebraska Supreme Court in *Venco* also examined the economic

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90. *Id.*

91. The association was chartered in compliance with IOWA CODE ch. 534. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 226.

92. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 226.

93. *Id.*

94. *Id.* at 227. Due-on-sale clauses give lenders the power to increase interest rates on long term loans in periods of rising rates when money is scarce. Volkmer, *Restraints on Alienation*, 58 IOWA L. REV. 769, 770 (1973).

95. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 227.

96. Black Hawk County District Court Trial Transcript at 8, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 220 (Iowa 1982).

97. *Id.*

98. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 227.

99. *Id.* "Because a large portion of their portfolios consist of older, lower yielding mortgages, they [savings and loans] have difficulty in paying the higher short term rates demanded by depositors." G. OSBORNE, *supra* note 13, § 5.23 at 307.

100. Black Hawk County District Court Trial Transcript at 319, Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d 220 (Iowa 1982).

consequences linked to the enforceability of due-on-sale clauses.[101] The *Venco* court observed that the assets of savings and loans are tied up in long-term mortgages, while funds to make these loans came from shorter term savings deposits; as interest rates the savings and loans pay on deposits rise, the difference between what is received on mortgage loans and paid to depositors is exacerbated.[102] The Nebraska Supreme Court concluded that due-on-sale clauses are valuable devices in aiding savings and loans to balance their portfolio return with the cost of lending money.[103] The court thus determined that it would probably be more repugnant to public policy to hold acceleration provisions unlawful.[104]

The Supreme Court of Iowa further emphasized that federal savings and loans "use and enforce due-on-sale mortgage provisions"[105] and that if Iowa invalidated use of acceleration clauses, then state chartered institutions would be "at a competitive disadvantage with the federal associations."[106] This argument has acquired more significance in light of the recent United States Supreme Court decision which stated that state law can not preempt the use of due-on-sale clauses by federally chartered savings and loans.[107] As a result federal institutions would be better able to maintain loans at current interest levels while receiving interest on notes at lower rates.[108]

In deciding *Fidelity Federal Savings and Loan v. de la Cuesta*,[109] the United States Supreme Court examined both the language and legislative history of the Home Owner's Loan Act of 1933,[110] to determine the authority of the Federal Home Loan Bank Board.[111] A majority of the Court found that Congress intended to vest the Federal Home Loan Bank Board (FHLBB) with broad authority to regulate savings and loans.[112] The Court

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101. Occidental Sav. and Loan Ass'n v. Venco Partnership, 206 Neb. at ____, 293 N.W.2d at 249.

102. *Id.*

103. *Id.*

104. *Id.*

105. Martin v. Peoples Mut. Sav. and Loans Ass'n, 319 N.W.2d at 228. The Federal Home Loan Bank Board (FHLBB) regulates federal savings and loans. *See infra* notes 110-113 and accompanying text.

106. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 228. *See* Mills v. Nashua Fed. Sav. and Loan, 121 N.H. 722, ____, 433 A.2d 1313, 1313-14 (1981) (court acknowledged that the FHLBB advocates the use of due-on-sale clauses by federally chartered savings and loans).

107. Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. 3014, 3022-23 (1982).

108. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 227-28.

109. 102 S. Ct. 3014 (1982).

110. Ch. 64, §§ 2-9, 48 Stat. 128 (codified as amended at 12 U.S.C. § 1464(a) (1976 & Supp. V 1981).

111. Fidelity Federal Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3025-29.

112. 77 CONG. REC. 4974 (1933) (statement of Sen. Bullkey): "This act provided for the creation of a system of federal savings and loan associations which would be regulated by the Board so as to ensure their vitality as permanent associations to promote the thrift of the

also found that Congress had delegated plenary authority to the FHLBB[113] in section 5 of the Act, which specifically states: "[T]he Board is authorized . . . to provide for the organization, incorporation, examination, operation, and regulation of associations to be known as 'Federal Savings and Loan Associations'. . . ."[114]

The FHLBB has advocated the use of due-on-sale clauses as valuable protection for the financial soundness of federal associations and for their continued ability to fund new home loans.[115] These clauses are endorsed by the FHLBB because such provisions enable savings and loans to alleviate the problem of investing funds in long-term loans thereby losing dollars in a period of rising interest rates.[116]

The Martins also asserted that due-on-sale clauses are a direct restraint on the sale of real estate.[117] A restraint on the alienation of property has been defined as follows:

> (1) A restraint on alienation . . . is an attempt by an otherwise effective conveyance or contract to cause a later conveyance
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> (a) to be void; or
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> (b) to impose contractual liability on the one who makes the later conveyance when such liability results from an agreement not to convey; or
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> (c) to terminate or subject to termination all or part of the property interest conveyed.[118]

The *Martin* court stated that "[i]t is obvious that a due-on-sale mortgage

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people in a co-operative manner to finance their homes and the homes of their neighbors." *See* 12 U.S.C. § 1416(a) (Supp. V 1981).

113. Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3026. The dissent advocated a narrower interpretation of 12 C.F.R. § 545.8-3(f) (1982) (which allows federal savings and loans to include due-on-sale provisions in loan agreements). Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3032 (Rehnquist, J., dissenting). The dissent argued that in promulgating section 545.8-3(f), the FHLBB "has gone beyond regulating how, when and in what manner a federal savings and loan association may lend mortgage money." *Id.* Thus, the dissent would have found the federal regulation to be beyond the scope of the congressional grant of power to the FHLBB. *Id.* Regulation of due-on-sale clauses, the dissent stated, should be left to the states. *Id.*

114. 12 U.S.C. § 1464(a) (Supp. V 1981). Pursuant to this statute the FHLBB promulgated the following regulation:

> An association continues to have the power to include, as a matter of contract between it and the borrower, a provision 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). *But see id.* § 545.8-3(g) (1982) (limitations on the use of due-on-sale clauses).

115. 12 C.F.R. § 545.8-3(f) (1982).

116. Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3030.

117. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 228.

118. RESTATEMENT OF PROPERTY § 404 (1944).

provision does not cause any of the above results and therefore cannot be categorized as a direct restraint on alienation."[119] The Iowa court stated that "a due on sale mortgage clause is no more an impediment to the alienation of real estate than zoning restrictions or building restrictions."[120] The court further observed that a due-on-sale clause acts to subject the sale of a home to current market rates and, therefore, it is the economy which acts to inhibit any conveyance of property.[121]

The *Martin* court analysis of due-on-sale clauses as restraints on the alienation of real estate closely paralleled the discussion of the Nebraska Supreme Court in *Venco*.[122] The *Venco* court pointed out that most courts automatically consider due-on-sale clauses as restraints and then proceed to determine whether use of them is unreasonable by examining the particular facts of each case.[123] The Nebraska court rejected that approach and held that due-on-sale clauses do not meet the definition of restraints on alienation as set out in the RESTATEMENT OF PROPERTY.[124]

The *Venco* court reasoned that the acceleration provision in the note was not an impairment to the owner's ability to convey his property; the conveyance only acted to accelerate the debt.[125] This analysis defies the reality of the situation; a mortgagee generally does not have the assets to pay the debt when the property is transferred. Venco Partnership argued that the due-on-sale clause was at least an indirect restraint[126] on alienation.[127] The court rejected that argument, finding that acceleration clauses do not impair the transferability of title.[128] The Nebraska court stated that acceleration clauses are similar to building and zoning restrictions, which are not restraints on alienation.[129]

In addressing the restraint on alienation issue, the Supreme Court of Iowa also examined the recent decision of the Minnesota Supreme Court in *Holiday Acres No. 3 v. Midwest Savings and Loan*.[130] The savings and loan in *Holiday Acres* appealed the county district court decision which declared the due-on-sale clause null and void as an unlawful restraint on the aliena-

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119. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 228.
120. *Id.* at 229.
121. *Id.*
122. Occidental Sav. and Loan Ass'n v. Venco Partnership, 206 Neb. at ____, 293 N.W.2d at 843 (discussing RESTATEMENT OF PROPERTY § 404 (1944)).
123. Occidental Sav. and Loan Ass'n v. Venco Partnership, 206 Neb. at ____, 293 N.W.2d at 845.
124. *Id.*
125. *Id.*
126. *Id.* An indirect restraint does not primarily restrain the alienation of property, but may discourage sale of the mortgaged premises. G. OSBORNE, *supra* note 13, § 5.22 at 299.
127. Occidental Sav. and Loan Ass'n v. Venco Partnership, 206 Neb. at ____, 293 N.W.2d at 846.
128. *Id.*
129. *Id.*
130. 308 N.W.2d 471 (Minn. 1981).

tion of property.[131] The Minnesota Supreme Court reversed the district court's holding.[132] The appellate court held that "the enforcement of due-on-sale clauses . . . is not *per se* unreasonable."[133] The Minnesota court, however, limited its opinion in *Holiday Acres* to contracts involving experienced business people negotiating loans for residential property.[134] The court held that, in a commercial setting, business and economic considerations outweigh any restraints on alienation caused by acceleration clauses.[135] While the Minnesota Court in *Holiday Acres* narrowed its decision to situations involving real estate developers,[136] the *Martin* case involved a loan between a financial institution and private homeowners.[137] The *Martin* court's reliance upon the Minnesota decision appears to be misplaced because the cases are factually distinguishable.

In *Martin*, the Iowa Supreme Court followed the majority rule which permits enforcement of acceleration clauses subject to equitable defenses.[138] The minority view, as advanced by the Martins, generally holds due-on-sale clauses invalid as unreasonable restraints on the transferability of prop-

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131. *Id.* at 473.

132. *Id.* at 484. The savings and loan involved in *Holiday Acres* was federally chartered, but the Minnesota court declared that it could determine the validity of the clause used by a federal association because home loan mortgages have traditionally been matters of state concern. *Id.*

133. *Id.* at 473, 475.

134. *Id.* at 484.

135. *Id.*

136. Holiday Acres No. 3 v. Midwest Sav. and Loan, 308 N.W.2d at 484.

137. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 222.

138. Tierce v. APS Co., 382 So. 2d 485, 487-88 (Ala. 1979); Malouff v. Midland Fed. Sav. and Loan Ass'n, 181 Colo. 294, ____, 509 P.2d 1240, 1244 (1973); Society for Sav. v. Bragg, 38 Conn. Supp. 8, ____, 444 A.2d 919, 924-25 (Conn. Super. Ct. 1981); Baker v. Loves Park Sav. & Loan Ass'n, 61 Ill.2d 119, ____, 333 N.E.2d 1, 4-5 (1975); Taliancich v. Union Sav. & Loan Ass'n, 142 So. 2d 626, 629 (La. Ct. App. 1962); Chapman v. Ford, 246 Md. 42, ____, 227 A.2d 26, 31 (1967); Dunham v. Ware Sav. Bank, ____ Mass. ____, 423 N.E.2d 998, 1001 (1981); Holiday Acres No. 3 v. Midwest Fed. Sav. & Loan Ass'n, 308 N.W.2d 471, 484 (Minn. 1981); Occidental Sav. & Loan Ass'n v. Venco Partnership, 206 Neb. 469, ____, 293 N.W.2d 843, 848 (1980); First Commercial Title, Inc. v. Holmes, 92 Nev. 636, ____, 550 P.2d 1271, 1272 (1976); Mills v. Nashua Fed. Sav. & Loan Ass'n, 121 N.H. 722, ____, 433 A.2d 1312, 1314 (1981); Century Fed. Sav. & Loan Ass'n v. Van Glahn, 144 N.J. Super. 48, ____, 364 A.2d 558, 560 (1976); First Fed. Sav. and Loan Ass'n v. Jenkins, 109 Misc.2d 715, ____, 441 N.Y.S.2d 373, 379-81 (S. Ct. 1981); Crockett v. First Fed. Sav. & Loan Ass'n, 289 N.C. 620, ____, 224 S.E.2d 580, 587 (1976); Northwestern Fed. Sav. & Loan Ass'n v. Ternes, 315 N.W.2d 296, 304 (N.D. 1982); People's Sav. Ass'n v. Standard Indus., Inc., 22 Ohio App.2d 35, ____, 257 N.E.2d 406, 408 (1970); First Fed. Sav. & Loan Ass'n v. Kelly, 312 N.W.2d 476, 478-81 (S.D. 1981); Gunther v. White, 489 S.W.2d 529, 532 (Tenn. 1973); Crestview, Ltd. v. Foremost Ins. Co., 621 S.W.2d 816, 826 (Tex. Civ. App. 1981); Walker Bank & Trust Co. v. Neilson, 26 Utah 2d 383, ____, 490 P.2d 328, 329 (1970); Lipps v. First Am. Serv. Corp., 286 S.E.2d 215, 219 (Va. 1982); Miller v. Pac. First Fed. Sav. & Loan Ass'n, 86 Wash.2d 363, ____, 545 P.2d 546, 549 (1976); Weickhardt v. Wauwatosa Sav. & Loan Ass'n, 103 Wis.2d 608, ____, 309 N.W.2d 865, 867-68 (Ct. App. 1981).

erty.[139] The stance of the minority of jurisdictions is best represented by the California Supreme Court decision of *Wellenkamp v. Bank of America.*[140] In *Wellenkamp* the court held that due-on-sale clauses could not be enforced unless the lender demonstrated that enforcement was essential to protect against impairment of its security or a risk of default.[141]

The *Wellenkamp* court rejected the argument that acceleration clauses are justifiable restraints which enable savings and loans to maintain their loan portfolios at current interest rates.[142] The California court decision was based on the theory that increasing interest rates are a normal economic risk inherent in an inflationary economy, and lenders are in a better position to make future projections when making long-term loan agreements.[143]

In *Wellenkamp*, the court ultimately placed the burden of proof on the lender to prove that enforcement of the due-on-sale clause was reasonably necessary to protect any impairment of its security.[144] The Iowa Court in *Martin* refused to adopt this position.[145] The United States Supreme Court also discussed the applicability of the *Wellenkamp* holding in its *de la Cuesta* decision.[146] The Supreme Court explicitly held, "that the Board's due-on-sale regulation bars application of the *Wellenkamp* rule to federal savings and loan associations."[147] The Federal Home Loan Bank Board thus believed that the restrictions found in *Wellenkamp*[148] would erode the financial stability of federal associations because such restrictions reduce the marketability of loans in the secondary market by lengthening the expected maturity date of lender's mortgage.[149]

Finally, the Martins contended that the mortgage agreement was vulnerable to the doctrine of unconscionability as an adhesion contract.[150] This

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139. Patton v. First Fed. Sav. and Loan Ass'n, 118 Ariz. 473, ____, 578 P.2d 152, 158 (1978); Tucker v. Pulaski Fed. Sav. & Loan Ass'n, 252 Ark. 849, ____, 481 S.W.2d 725, 728 (1972); Wellenkamp v. Bank of Am., 21 Cal.3d 943, 953-55, 582 P.2d 970, 976-77, 148 Cal. Rptr. 379, 385-86 (1978); First Fed. Sav. & Loan Ass'n v. Lockwood, 385 So. 2d 156, 160 (Fla. Dist. Ct. App. 1980); Nichols v. Ann Arbor Fed. Sav. & Loan Ass'n, 73 Mich. App. 163, ____, 250 N.W.2d 804, 809 (1977); Sanders v. Hicks, 317 So. 2d 61, 64 (Miss. 1975); State *ex rel* Bingaman v. Valley Sav. & Loan Ass'n, 97 N.M. 8, __, 636 P.2d 279, 283 (1981).

140. 21 Cal.3d 943, 582 P.2d 970, 148 Cal. Rptr. 379 (1978).

141. *Id.* at 953, 583 P.2d at 976-77, 148 Cal. Rptr. at 385-6.

142. *Id.* at 21 Cal. 2d at 952, 582 P.2d at 976, 148 Cal. Rptr. at 385.

143. *Id.*

144. Note, *Wellenkamp v. Bank of America; Exercise of Due on Sale Clauses as an Unreasonable Restraint Upon Alienation*, 33 U. MIAMI L. REV. 722, 733 (1979).

145. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 230.

146. Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3020.

147. *Id.* at 3031.

148. The *Wellenkamp* decision prohibits automatic enforcement of due-on-sale clauses. Wellenkamp v. Bank of Am., 21 Cal. 3d at 953, 538 P.2d at 976-77, 148 Cal. Rptr. at 385-86. The court placed the burden on the lender to prove that enforcement was reasonably necessary to protect the security. *Id.*

149. Fidelity Fed. Sav. and Loan Ass'n v. de la Cuesta, 102 S. Ct. at 3030.

150. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 229. *See* C & J Fertilizer

argument was rejected by the Iowa court because the Martins were not a party to the contract that contained the acceleration clause.[151] The court also reasoned that there was abundant evidence that the Jorgensons were fully aware of the acceleration provision when they signed the contract.[152] The court finally stated that the issue of unconsionability "was raised for the first time by the Attorney General's district court amicus brief."[153] "Reviewable issues must be in the parties' briefs, not amicus briefs."[154]

Due-on-sale clauses have been alleged to be unconscionability in other jurisdictions.[155] In *Mills v. Nashua Federal Savings and Loan Association*,[156] for example, the home buyers contended that the loan instrument formed an adhesion contract.[157] The New Hampshire court refused to interfere where the parties had freely agreed to the terms of the contract.[158] Missing from the court's analysis, however, was the fact of the unequal bargaining power between the buyers, who had little option if they wish to obtain money for the purchase of a home, but to accept the terms of the agreement as specified, and the savings and loan, the drafter of the mortgage agreement.[159]

The majority view in the country places too much emphasis on the deleterious effect of current economic conditions of savings and loans with little concern or compassion for the average citizen wishing to purchase residential property. The courts too easily set aside any consideration of due-on-sale clauses as adhesion contracts or indirect restraints on the transferability of property. Due to high interest rates, potential home buyers are more apt to forego moving and remain where they can afford the interest payment of their mortgage loan. The courts should not advocate enforcement of the due-on-sale clause by lending institutions, but rather allow acceleration of the debt payment only if the savings and loan reasonably fears an impairment to its security. This seems to be the most equitable solution.

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v. Allied Mut. Ins. Co., 227 N.W.2d 169, 176-77 (Iowa 1975) (reasonable expectations doctrine discussed).

151. Martin v. Peoples Mut. Sav. and Loan Ass'n, 319 N.W.2d at 230. The Martins also failed to allege that they might be third party beneficiaries of the contract between the Jorgensons and Peoples Mutual. *Id.*

152. *Id.*

153. *Id.*

154. *Id.*

155. *See, e.g.*, Mills v. Nashua Fed. Sav. and Loan Ass'n, 121 N.H. 722, ____, 433 A.2d 1313, 1314-15 (1981).

156. *Id.* at ____, 433 A.2d at 1313.

157. *Id.* at 1314-15.

158. *Id.*

159. *Id.*