Spring 1982

Case Summaries

Follow this and additional works at: https://scholarship.law.missouri.edu/mlr

Recommended Citation
Case Summaries, 47 Mo. L. Rev. (1982)
Available at: https://scholarship.law.missouri.edu/mlr/vol47/iss2/13

This Note is brought to you for free and open access by the Law Journals at University of Missouri School of Law Scholarship Repository. It has been accepted for inclusion in Missouri Law Review by an authorized editor of University of Missouri School of Law Scholarship Repository. For more information, please contact bassettcw@missouri.edu.
CASE SUMMARIES


Crestview Company, a partnership, purchased an office building, executing a promissory note and deed of trust in favor of Foremost, the seller. The note contained a due-on-sale clause. Several months later, Crestview entered negotiations to sell the property to Crestview, Ltd., a limited partnership. The two entities, however, were not affiliated. In exchange for its approval of the sale, Foremost requested a reduction in principal or an increased interest rate from Crestview, Ltd. Following refusal of its request, Foremost elected to accelerate the debt as provided in the due-on-sale clause. Foremost directed the trustee to sell the property after full payment was not forthcoming.

Crestview, Ltd. brought a declaratory judgment action requesting that the acceleration of the debt be declared an invalid basis for the trustee’s sale. It further sought temporary and permanent injunctive relief to prevent the sale of the property. The Texas Court of Civil Appeals affirmed the trial court’s denial of relief.

Although the court took notice of the long line of cases involving a due-on-sale clause from other jurisdictions, it relied on the social policies and precedents of Texas in determining that the due-on-sale clause was a reasonable restraint on alienation. The court further reasoned that while the dominant purpose of any mortgage instrument is to secure the underlying indebtedness, there is no legal barrier to attaching additional purposes to the agreement. The parties in this instance had added an additional purpose of allocating the risk of market interest rate fluctuations by including the due-on-sale clause for the benefit of the mortgagee and the prepayment without penalty provision for the benefit of the mortgagor. The court further concluded that the parties’ intentions to allocate the market risks did not undermine the policies prohibiting restraints against alienation as set forth in section 404 of the Restatement of Property.

The Texas decision falls in line with the majority’s approach, which permits the due-on-sale clause to be used to exact a higher interest rate. Although Missouri courts have yet to decide the validity of the due-on-sale clause, Missouri does have case law very similar to the case law relied on by the Texas Court of Civil Appeals. By drawing analogies from the Missouri decisions that discuss the reasonableness of restraints on alienation and using the reasoning of the Texas court, it seems probable that Missouri also will permit the use of the due-on-sale clause to exact a higher interest rate.

E. SID DOUGLAS III

Joseph and Sandra Karp obtained a loan from Pan American Federal Savings and Loan Association. This loan was secured by a deed of trust on a commercial building owned by the Karps. The deed of trust contained a standard due-on-sale clause providing for accelerated payments if the Karps sold the property. Notwithstanding this clause, the Karps sold the property to the plaintiffs subject to the deed of trust. When the plaintiffs’ first payment was due, it was tendered to Pan American. Rather than accept payment from the plaintiffs, Pan American invoked the due-on-sale clause and demanded the entire loan balance. Full payment was not made. After notice of default was recorded, plaintiffs sued to enjoin foreclosure. Under California law, a due-on-sale clause is not enforceable unless the lender can show impairment of its security or increased risk of default due to the sale. Pan American conceded that it could show neither in this case, but asserted that federal statutes and regulations permitting routine enforcement of due-on-sale clauses by federally chartered savings and loan associations pre-empted California law. The trial court agreed with Pan American and entered summary judgment. In *Panko v. Pan American Federal Savings and Loan Association*, however, the California Court of Appeal reversed, holding that California law was not pre-empted by federal law in this area.

The court applied several of the traditional tests for federal pre-emption. First, it found no direct conflict between state and federal law in this area because it was possible to comply with both state and federal law. Second, it also concluded Congress had demonstrated no express intent to pre-empt the field. Third, existing state law in this area in no way infringed on or was otherwise incompatible with the regulation or operation of the internal affairs of federal savings and loan associations. Fourth, there was no dominant federal interest in the application of federal law in this area because the use of due-on-sale clauses only was authorized, and not required, by federal regulations governing federal savings and loan associations.

In states such as California that limit the lender’s ability to enforce due-on-sale clauses, a holding of federal pre-emption means that state and federal savings and loan associations have different standards of enforceability for due-on-sale clauses. The effect of *Panko*, therefore, may be to promote uniformity in treatment of due-on-sale clauses. Because federal courts have unanimously held that this area is federally pre-empted, however, state court decisions such as *Panko* may have the undesirable effect of encouraging a race to the courthouse in these borrower-oriented states.

The issue of federal pre-emption in the area of due-on-sale clause enforceability is not yet settled. An appeal from the *Panko* decision has been docketed in the United States Supreme Court. More importantly, the Supreme Court has noted probable jurisdiction on the appeal of *Fidelity Federal
Savings and Loan Association v. de la Cuesta, 121 Cal. App. 3d 328, 175 Cal. Rptr. 467 (1981). de la Cuesta involves the identical issue of federal pre-emption raised in the Panko decision. Moreover, de la Cuesta specifically approves of the holding and reasoning of Panko and adopts substantial portions of the language of the Panko opinion. Because de la Cuesta is scheduled for decision in 1983, a definitive word on this controversial issue will soon be forthcoming.

DON M. DOWNING