

TRANSFERRING Mortgaged Property into a Trust

Be careful when transferring mortgaged property to a living (aka inter vivos) trust or LLC because a due-on-sale clause in the mortgage may be triggered. Due-on-sale clauses require a mortgage loan to be repaid in full upon the sale of or conveyance of an interest in the property that secures the mortgage.

Read on for more info:

The Garn-St. Germain Depository Institutions Act of 1982 (Garn-St. Germain Act) exempts certain transfers, including transfers to an inter vivos trust, from triggering a due-on-sale clause provided certain other requirements are satisfied, but the act does not protect transfers of mortgaged real property into an LLC or other ownership device.

On its face, the statutory text of the Garn-St. Germain Act limits protection to “residential” dwellings of five units or less and does not require occupancy, provided the rights of occupancy are not affected. **But the implementing regulations, in contrast, make no mention of the size of the dwelling but apply only to a “home.” This appears to require occupancy.**

For many trust-based estate plans, compliance with the requirements of both the statutory text and the implementing regulations will not be difficult because many clients own only a mortgage free single-family home that they intend to continue to occupy after the transfer to an inter vivos trust established for their own benefit. But **owners of mortgaged rental property, apartment complexes, and vacation homes may run into problems.**

One solution is to obtain lender approval in writing before executing a transfer that is not explicitly covered by the exemptions in the Garn-St. Germain Act. Some planners may go so far as to recommend lender approval even for exempted property transfers (such as mortgaged homes) to avoid any potential legal entanglements after the fact.

The safest rule is to use caution if you ever transfer mortgaged property.

Even if the lender wrongly exercises the due-on-sale clause, and you are right to claim that the transfer is exempted, mortgage disputes can be stressful and costly for homeowners.

JAN NEAL LAW FIRM, LLC

207 North 4th Street | Opelika, Alabama 36801
1-800-270-7635

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