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Comment

MORATORIA AND STAY LAWS:

MORTGAGE MORATORIA LEGISLATION IN CALIFORNIA

With the extension in 1941 of the California Mortgage Moratorium Act¹ for an additional two years, it becomes important to examine the history and interpretation of this Act and other related laws. The background and validity of this legislation have been adequately discussed in earlier articles,² and need not be further dwelt with here. Our chief problem is not to consider the validity of state moratory or stay laws under the Federal Constitution; it is rather to examine

¹ Cal. Stats. 1935, p. 1208; Cal. Stats. 1937, pp. 57, 460; Cal. Stats. 1939, p. 1045; Cal. Stats. 1941, p. 1263.

² Note (1937) 25 CALIF. L. REV. 347, 576; Legis. (1934) 22 CALIF. L. REV. 170; Legis. (1936) 9 So. CALIF. L. REV. 335, 354; (1934) 22 CALIF. L. REV. 350.

the interpretation and application of the California legislation during the past seven years.³

It is essential at the outset to distinguish the Moratorium Act from the numerous amendments to the codes. While both the Act and the code sections were results of the depression following 1929 and had the object of alleviating the debtor's position, the means adopted were different. The moratorium law operates to *postpone* the creditor's remedies, while the code amendments seek to effect a *change* (reduction) in the remedies themselves. It is apparent that a continued postponement of the creditor's remedies, even on conditions, will itself amount to a very substantial change by making foreclosure in effect discretionary with the court. However, because the moratorium law has been regarded as a temporary measure, and operates by different means, it will be considered first.

THE CHATTEL MORTGAGE, MORTGAGE AND TRUST DEED MORATORIUM ACT

This Act was passed in 1935 as emergency legislation. In its first section there appeared the recital that as a result of depressed conditions great numbers of debtors were unable to meet their obligations, and it was necessary to enact legislation to avoid the economic loss and social disruption that would result from numbers of forced sales and forfeitures. The legislature proposed to relieve these conditions by permitting the debtor, subject to certain requirements, to obtain postponements of such sales and forfeitures. These extraordinary remedies were made available for a period of two years only.⁴ However the law was reenacted in 1937, 1939 and again in 1941.

The recital of emergency conditions has been repeated in each reenactment. The original purpose of that recital was probably to aid in establishing the constitutionality of the Act. Today this recital serves no purpose because plainly untrue. Neither the earning power of the debtor nor the value of his land is abnormally low today.⁵ However this legislation has a definite place in our scheme of mortgage law, quite apart from any question of fictitious emergency conditions. As will be pointed out below, the benefits available to the debtor under sections 580a and 580b of the Code of Civil Procedure as those sections are presently construed are not available with re-

³ For an excellent article on the history of moratory legislation, see Feller, *Moratory Legislation: A Comparative Study* (1933) 46 HARV. L. REV. 1061.

⁴ Cal. Stats. 1935, p. 1208, §§ 4, 5, 7, 10, 15, 20, 25.

⁵ It is interesting to note that two state courts have held such emergency legislation no longer valid on the ground that the emergency has terminated. *First Trusts Joint S. L. Bank v. Arp* (1939) 225 Iowa 1331, 283 N. W. 441, 120 A. L. R. 937; *First Trust Co. v. Smith* (1938) 134 Neb. 84, 277 N. W. 762.

spect to mortgages executed before 1933. On the other hand, the Moratorium Act applies only to mortgages contracted prior to February 1, 1935.⁶ Though these periods overlap, it would seem that the most important function performed by the Moratorium Act is the protection of debtors who have been denied the benefits of the above code sections.

Under the Act, the court has the power upon petition seasonably filed,⁷ and upon hearing,⁸ to order postponement of a private or judicial sale; or if there has been a foreclosure and sale⁹ and there still exists a right of redemption, to order the extension of that right.¹⁰ Moreover, the court is empowered to postpone termination of the interest of the vendee under a contract of sale of real property,¹¹ and to extend or alter postponements ordered by the court under the Act.¹² There is also a provision for the tolling of the statute of limitations,¹³ which will be further discussed below.

Grounds for, and conditions to orders of postponement. The Act permits the court to postpone sales, or extend the right of redemption upon equitable grounds, if the security is not unreasonably jeopardized.¹⁴ It is not surprising, therefore, to discover that the trial court has the widest possible discretion in giving or refusing such relief.¹⁵ The authors of this Comment have not discovered any case in which the decision of the trial court in this respect has been overruled. It has been said that the mere fact of inability to pay an obligation is not a sufficient ground for relief. Relief granted must be

⁶ Cal. Stats. 1941, p. 1263, § 21. It should be noted also that the Act does not apply to mortgages or deeds of trust issued as security for bonds issued under authorization of the commissioner of corporations, or by public utilities subject to the public utilities act, nor to any loan by an agency of the United States Government, or insured by the United States, nor any mortgage or deed of trust securing an obligation already in default when the land encumbered was purchased, if the purchase was subsequent to the effective date of the act.

⁷ *Ibid.* §§ 2, 5. The mortgagor may file petition for postponement of sale at any time within 90 days after the recordation of notice of default. At any time prior to the expiration of the period of redemption, a petition for extension of that right may be filed.

⁸ *Ibid.* § 4.

⁹ *Ibid.* § 5. Also note that under section 4 no sale may be had while this proceeding is pending. It has been held that if a trial court improperly permits a sale, it will be set aside upon appeal. *Boggs v. North American Bond etc. Co.* (1936) 6 Cal. (2d) 523, 58 P. (2d) 918.

¹⁰ Cal. Stats. 1941, p. 1263, § 10. Note that under section 9 the period of redemption shall be extended until 10 days after the court makes its order in the matter. It is thus possible for the debtor to gain a slight extension although the court gives him no relief.

¹¹ *Ibid.* § 15.

¹² *Ibid.* § 16.

¹³ *Ibid.* § 20.

¹⁴ *Ibid.* §§ 5, 10.

¹⁵ *Boggs v. North American Bond etc. Co.*, *supra* note 9.

fair to both parties.¹⁶ Apparently, when the plaintiff is a purchaser of the property subject to the mortgage it is necessary for him to allege affirmatively that when he acquired the property the mortgage was not in default.¹⁷

It should be noted generally in this connection that the trial court must hear evidence before it can give relief, and although the creditor does not appear, the allegations of the petition are not taken as admitted.¹⁸ Further, there must be a hearing upon a supplemental petition before an extension of a previous order may be given.¹⁹

There has been somewhat more litigation over the propriety of conditions attached by the trial court to orders given. The statute requires that the court consider the value of the property with regard to its income and other factors, and that the court include in its order a requirement for such payments as it deems just and equitable.²⁰ These payments may not be less than the amount of present taxes, and installments on delinquent taxes, and any insurance premiums which by contract were to be paid by the debtor.²¹ The trial court is also required to make provision for the maintenance and repair of the property.

The actions of trial courts in imposing such conditions as well as in granting or in refusing postponements have been consistently upheld. It has been held that there was no abuse of discretion in giving an order putting the mortgagee in possession, and in ordering payments beyond the earning capacity of the property;²² in ordering that two wells be put into operation;²³ in refusing to order reimbursement by the mortgagor for taxes already paid by the mortgagee;²⁴ or in ordering the repair of damage caused by flood.²⁵ If the payments ordered or acts required by the trial court are not performed, the order of postponement will be discharged.²⁶

Effect on statute of limitations. Section 20 of the Act now provides that whenever the time within which an action may be commenced on a contract of sale, or obligation secured by a mortgage or deed of trust, would expire during the period of application of this Act

¹⁶ *Bennett v. California Trust Co.* (1936) 6 Cal. (2d) 381, 57 P. (2d) 914.

¹⁷ *Watts v. Currie* (1940) 38 Cal. App. (2d) 615, 101 P. (2d) 764.

¹⁸ *Boggs v. North American B. & M. Co.* (1937) 20 Cal. App. (2d) 316, 66 P. (2d) 1253.

¹⁹ *Hartman v. Bank of America* (1938) 28 Cal. App. (2d) 98, 82 P. (2d) 39.

²⁰ Cal. Stats. 1941, p. 1263, §§ 5, 10.

²¹ *Ibid.* §§ 6, 11.

²² *Williams v. Linville* (1937) 9 Cal. (2d) 256, 70 P. (2d) 485.

²³ *Ward v. Alling* (1937) 19 Cal. App. (2d) 553, 65 P. (2d) 902.

²⁴ *Hartman v. Bank of America*, *supra* note 19.

²⁵ *Leonard v. Title Ins. & Trust Co.* (1937) 18 Cal. App. (2d) 496, 64 P. (2d) 159.

²⁶ *Ibid.*; *Ward v. Alling*, *supra* note 23.

by virtue of section 337 of the Code of Civil Procedure, or any other provision of law, such time is extended until 1943. This does not apply, of course, to instruments executed subsequent to February 1, 1935.

The district courts of appeal have held that the statute of limitations is tolled under this section of the Act whether or not there has been any petition by the debtor for the benefits of the Act.²⁷ In *Rust v. Hill*²⁸ the supreme court has ruled that if the sale took place before the enactment of the Moratorium Act; so that the benefits of the Act were not available to the debtor, the statute of limitations is not tolled. However, the supreme court expressly refused to pass on the correctness of the decisions holding that where the debtor did not take advantage of the Moratorium Act the statute of limitations was tolled. This point may therefore be regarded as unsettled.²⁹

CODE OF CIVIL PROCEDURE SECTION 580A

Section 580a of the Code of Civil Procedure provides,³⁰ first, that any action for a deficiency judgment upon an obligation secured by a mortgage or deed of trust on real property must be brought within three months of the sale of the security, and, second, that the security shall be appraised, and no judgment shall be given for more than the amount of the debt less the fair market value of the property at the time of the sale.

²⁷ *Bakersfield etc. Co. v. McAlpine etc. Co.* (1938) 26 Cal. App. (2d) 444, 79 P. (2d) 410; *Evarts v. Newhouse Inc.* (1938) 28 Cal. App. (2d) 407, 82 P. (2d) 703.

²⁸ (1941) 17 Cal. (2d) 517, 110 P. (2d) 657.

²⁹ *Rust v. Hill*, *ibid.*, can probably be cited as both in accord with, and contra to the district court of appeal cases discussed above. The court expressly refused to pass on their correctness, which certainly leads one to doubt that they will be followed in the future. But on the other hand, the court cites *Harris v. Fitting* (1937) 9 Cal. (2d) 117, 69 P. (2d) 833, which is a case in accord with them.

The present moratorium Act, enacted in 1935, was preceded for a few months during 1935 by another, quite similar act. Cal. Stats. 1935, p. 56. This statute, in contrast to the present Act, expressly provided that the statute of limitations would be tolled only if an order of postponement was obtained. It might be argued that the omission of this requirement from the present Act was intentional, so that creditors who forbore without the compulsion of a court order would be protected.

³⁰ The section requires the plaintiff to state the amount of indebtedness due, the amount the property was sold for and the date of the sale, and its fair value at that time. It provides for the appointment by the court, on motion of one of the parties, or on its own motion, of one of the inheritance tax appraisers to appraise the property or the interest mortgaged. The appraisal shall be admissible in evidence, and the appraisers may be called and examined by any party or the court itself. The court must find the fair market value of the property at the time of sale. The deficiency judgment may not exceed the difference between the fair value of the property and the amount of the debt, including interest from the date of the sale. Nor may it exceed the difference between the amount of the debt and the amount brought by the sale. Any such action must be brought within three months from the date of the sale. No judgment may be rendered in any such action unless the property has first been sold pursuant to the terms of the instrument in question, unless the property has become valueless.

The California courts have held that the impairment of contracts clause of the Federal Constitution prohibits the application of the second part of this section to mortgages executed before its effective date.³¹ In the recent case of *Gelfert v. National City Bank*³² the Supreme Court of the United States sustained such a retroactive application of a very similar New York statute. It appears, therefore, that the California courts might well reconsider their construction of our code section.

The court has used as a makeweight argument the doctrine that the legislature should be presumed to intend that laws shall not operate retrospectively. But the court found that application of this doctrine to the statute of limitations portion of section 580a suggested no more than the conclusion that this section was not meant to apply if the sale was consummated before the effective date of the section.³³ The court had no hesitation in applying the three month statute of limitations if the sale occurred after the section became effective, regardless of the date of the mortgage. There seems no discernible reason for assuming that the legislature did not intend a similar application for both parts of the section.

One or two incidental matters remain to be considered. It has been held that a guarantor may not claim the benefit of section 580a.³⁴ An action against him is not regarded as being for a "balance due upon a mortgage" but as an action upon an independent contractual liability.

In *Hillen v. Soule*³⁵ a purchaser of realty gave two notes for the price to two promisees. Two deeds of trust were executed on the land, one securing each note. One of the mortgagees foreclosed and exhausted the security. The second sued on his note, and recovered. It was held that the recovery by the first mortgagee had no effect on the rights of the second, except as permitting him to sue the purchaser directly on the debt, without foreclosing. This raises the question whether it would be possible for a creditor to avoid the application of section 580a by taking several small notes for the amount of the debt, each secured by a separate mortgage. It would

³¹ *Central Bank of Oakland v. Proctor* (1936) 5 Cal. (2d) 237, 54 P. (2d) 718. *Accord*: *Bennett v. Superior Court* (1935) 5 Cal. App. (2d) 13, 42 P. (2d) 80; *Birkhofer v. Krumm* (1938) 27 Cal. App. (2d) 513, 81 P. (2d) 609.

³² (1941) 313 U. S. 221, (1941) 30 CALIF. L. REV. 71.

³³ *Reynolds v. Jensen* (1936) 14 Cal. App. (2d) 558, 58 P. (2d) 687. *Accord*: *Palo Alto Mut. B. & L. Ass'n v. Cook* (1936) 17 Cal. App. (2d) 193, 61 P. (2d) 499. *Cf.* *Bank of America Ass'n v. Dennison* (1935) 8 Cal. App. (2d) 173, 47 P. (2d) 296; *Security First National Bank v. Sapkin* (1937) 19 Cal. App. (2d) 224, 66 P. (2d) 656.

³⁴ *Bank of America etc. Ass'n v. Hunter* (1937) 8 Cal. (2d) 592, 67 P. (2d) 99.

³⁵ (1935) 7 Cal. App. (2d) 45, 45 P. (2d) 349. Section 580b of the Code of Civil Procedure was also held inapplicable. This section forbids deficiency judgments in purchase money mortgages.

seem possible that if he bid in the property for the amount of the first note, the creditor could sue the debtor personally on the other notes.

If a creditor has a claim for a deficiency judgment against an estate, the fact that the administrator has allowed the claim does not affect the application of section 580a. It has been held that suit for the deficiency must still be brought within three months from the sale.³⁶

CODE OF CIVIL PROCEDURE SECTION 580b

Enacted in 1933, section 580b forbids deficiency judgments on purchase money mortgages. A later amendment extended this prohibition to land purchase contracts. The courts have uniformly held that this section could not be given effect in cases of mortgages executed prior to 1933 without violating the impairment of contracts clause of the Federal Constitution.³⁷ In view of the arguments used by the United States Supreme Court in *Gelfert v. National City Bank*,³⁸ discussed above in connection with section 580a, it would seem possible for the California courts to apply this section retroactively. In *Whitney v. Redfern*³⁹ the trial court did apply the section in the case of a renewal note and mortgage given in 1934 to the daughter of the original creditor. The appellate court took the view that on an appeal on the judgment roll alone it could not go behind the findings of the trial court. Since the trial court had found the 1934 mortgage to be one for the purchase money, the appellate court would not inquire into earlier transactions, evidence of which was not before the court.

What is a purchase money mortgage? This question has also required adjudication. In *Banta v. Rosasco*⁴⁰ the original mortgage was not given as part of the mortgagor's purchase. An assuming grantee was held liable for the deficiency because the mortgage, given to secure other debts, was not at the outset a "purchase money mortgage". This is a rather dubious decision.⁴¹ Regardless of the character of the mortgage as between the mortgagor and the mortgagee, the assuming grantee regards his assumption as a part of the

³⁶ Estate of Naegely (1939) 31 Cal. App. (2d) 470, 88 P. (2d) 715.

³⁷ Central Bank of Oakland v. Proctor (Cal. App. 1935) 51 P. (2d) 157; Hales v. Snowden (1937) 19 Cal. App. (2d) 366, 65 P. (2d) 847; Birkhofer v. Krumm, *supra* note 31.

³⁸ *Supra* note 32.

³⁹ (1940) 41 Cal. App. (2d) 409, 106 P. (2d) 919.

⁴⁰ (1936) 12 Cal. App. (2d) 420, 55 P. (2d) 601.

⁴¹ Langmaid, *Contracts for the Benefit of Third Persons in California* (1939) 27 CALIF. L. REV. 497, 505, n. 26, 533.

price of the property, exactly as he would if he executed a mortgage to the grantor. Since there had been serious question in *Banta v. Rosasco* as to whether the grantee had, in fact, assumed the mortgage, the legislature shortly thereafter amended the statute of frauds⁴² to require that assumption of a mortgage must be either in a writing signed by the grantee, or in the deed. While this provision should reduce litigation over the issue of assumption, it will not change the consequences.

In *Coast Federal Savings & Loan Ass'n of Los Angeles v. Crawford*,⁴³ the circuit court of appeals considered a case in which the real purchaser had title taken in the name of a dummy who gave a note and mortgage guaranteed by the real purchaser for the balance of the purchase price. The court held this to be a "purchase money mortgage", to which section 580b was applicable, and said that the benefits of the section are available to a guarantor, or other party who was the real purchaser. Whether the section could be invoked by a guarantor or indorser who was *not* the purchaser was not involved in that case, and the court expressed no opinion thereon.⁴⁴

In *Stockton Savings & Loan Bank v. Massanet*⁴⁵ the first purchasers of a tract, who were unable to complete payment of their debt to the plaintiff, surrendered their interest to him. The plaintiff released these purchasers and conveyed the property to the defendants. These defendants gave the plaintiff a trust deed back, and gave the first purchasers a note secured by a second trust deed—apparently for their equity. The plaintiff contended that he did not in fact sell the property to defendants because he retained the same interest throughout, that is, merely a security title, and that the only sale was that of the original purchasers' equity. The court held that the defendants' obligation was on a purchase money trust deed and that section 580b applied to relieve them from liability for any deficiency. The court then went further, and stated that the rule for determining whether a mortgage or trust deed is to be regarded as a purchase money mortgage is the same as in the case of priorities. In other words, it need not be given *to* the vendor, but may be to a third person who advances the consideration for the vendee. The court took the view that the purchase money mortgagee is generally in a very favorable position so far as priority of his lien is concerned, so that the legislature might well deny him any recovery beyond the property. This seems to be a sound and workable interpretation of the term "purchase money mortgage" and one which will effectu-

⁴² CAL. CIV. CODE § 1624; CAL. CODE CIV. PROC. § 1973.

⁴³ (C. C. A. 9th, 1941) 117 F. (2d) 913.

⁴⁴ Cf. *Bank of America etc. Ass'n v. Hunter*, *supra* note 34.

⁴⁵ (1941) 18 A. C. 175, 4 Cal. Dec. 553, 114 P. (2d) 592.

ate the remedial purposes of the statute.

Duration. The question of duration arose in connection with section 580b, as it had with section 580a and the other code amendments. When these were enacted in 1933, they were combined in the final draft with Civil Code section 2924½ which in effect gave a further nine month stay of foreclosure to delinquent mortgagors. This latter section was intended to be temporary, expiring in 1936. However, because of inexpert drafting this limitation appeared possibly to be applicable to all the code amendments. To remove any ambiguity, the legislature in 1935 reenacted the other code sections as permanent statutes, declaring such to have been its original intention. In *Kirkpatrick v. Stelling*⁴⁶ the district court of appeal, in construing section 580a, gave effect to this language and held it to be permanent legislation. However, in the *Stockton Savings & Loan Bank* case the district court of appeal held that the section as enacted in 1933 was limited to three years, and that the language being plain, the legislature in 1935 could not extend its application beyond 1936 as to mortgages contracted in 1933 or 1934.⁴⁷ In other words, a mortgagee who so contracted during those years was regarded as having a right, which could not be subsequently divested, to "wait out" the three year period, and then secure a deficiency judgment if the property did not bring enough on foreclosure. This case is, of course, no longer law, since the supreme court granted a hearing and reached the opposite result.⁴⁸ In view of the liberal attitude displayed by the supreme court in *Rust v. Hill*,⁴⁹ it is unlikely that this point will be raised again.

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⁴⁶ (1940) 36 Cal. App. (2d) 658, 98 P. (2d) 566.

⁴⁷ (Cal. App. 1940) 104 P. (2d) 712.

⁴⁸ *Supra* note 45.

⁴⁹ *Supra* note 28.