

# Application of California's Antideficiency Statutes in Conflict of Laws Contexts

In a series of cases<sup>1</sup> culminating in *Reich v. Purcell*,<sup>2</sup> in 1967, and *Hurtado v. Superior Court*,<sup>3</sup> in 1974, the California Supreme Court abandoned the traditional vested rights methodology<sup>4</sup> for resolving conflict of laws issues and adopted governmental interest analysis.<sup>5</sup> Since *Reich* and *Hurtado*, the application of governmental interest analysis has produced principled results in diverse fields of law.<sup>6</sup> The modern conflict of laws

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1. *Bernkrant v. Fowler*, 55 Cal. 2d 588, 360 P.2d 906, 12 Cal. Rptr. 266 (1961) (holding that California's statute of frauds does not protect the estate of a California decedent against an otherwise valid Nevada oral contract to forgive a debt in a will); *People v. One 1953 Ford Victoria*, 48 Cal. 2d 595, 311 P.2d 480 (1957) (holding that a California statutory requirement that automobile dealers reasonably investigate purchaser's moral character does not apply to Texas automobile dealer holding a security interest in an automobile seized in California for transporting marijuana). Professor Currie remarked in 1961 that *Bernkrant* "is probably the only judicial opinion concerning the Statute of Frauds in the conflict of laws that does not so much as mention the substance-procedure dichotomy. The analysis is explicitly in terms of governmental policies and interests." Currie, *Justice Traynor and the Conflict of Laws*, 13 STAN. L. REV. 719, 778 n.236 (1961). Concerning the role played by *Ford Victoria* in the evolution of Traynor's conflict of laws opinions, see Kay, *Chief Justice Traynor and Choice of Law Theory*, 35 HASTINGS L.J. 747, 756-58 (1984).

2. 67 Cal. 2d 551, 432 P.2d 727, 63 Cal. Rptr. 31 (1967). In *Reich*, the court held that California had no interest in applying the California rule allowing unlimited wrongful-death recoveries in an action against a California resident when the accidental death occurred in Missouri and the decedent was an Ohio resident at the time of the accident. *Id.* at 555-56, 432 P.2d at 730, 63 Cal. Rptr. at 34.

3. 11 Cal. 3d 574, 522 P.2d 666, 114 Cal. Rptr. 106 (1974) (in action against California resident defendant for wrongful death of domiciliary of Mexico in a California accident, California had governmental interest in applying its law regarding allowable damages while Mexico had no interest in applying its limitations on damages).

4. For description of the traditional vested rights theory, see *infra* text accompanying notes 27-40.

5. In *Reich*, Chief Justice Traynor employed a form of governmental interest analysis. Justice Sullivan, in *Hurtado v. Superior Court*, 11 Cal. 3d 574, 522 P.2d 666, 114 Cal. Rptr. 106 (1974), remarked on the effect of *Reich*: "The case of *Reich v. Purcell* . . . , apart from its service in aligning California squarely with the states rejecting the vested rights theory, . . . should prove invaluable as a methodological exercise in the resolution of . . . choice-of-law problem[s] by reference to the purposes of the laws involved." *Id.* at 580 n.3, 522 P.2d at 670 n.3, 114 Cal. Rptr. at 110 n.3 (quoting Cavers, *Comments on Reich v. Purcell*, 15 U.C.L.A. L. REV. 647 (1968)). For a description of California's formulation of governmental interest analysis, see *infra* text accompanying notes 41-52.

6. See, e.g., *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978) (where employee of California corporation was injured in Louisiana due to negligence of multinational corporation, Louisiana law applied disallowing cause of action by employer for loss of key employee's services); *Bernhard v. Harrah's Club*, 16 Cal. 3d 313, 546 P.2d 719, 128 Cal. Rptr. 215, cert. denied, 429 U.S. 859 (1976), overruled on other grounds, *Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984) (in action by California resident

revolution, however, has not yet reached California's secured real-property transactions. Recent California cases<sup>7</sup> have failed to apply governmental interest analysis to resolve conflicts issues involving the extraterritorial reach of California's antideficiency statutes.<sup>8</sup>

California's unique antideficiency scheme comprises four interrelated sections of the Code of Civil Procedure which circumscribe a creditor's<sup>9</sup> rights to a deficiency judgment. Section 726,<sup>10</sup> known as the "one-action rule," compels a creditor to foreclose the real-property security interest before being allowed an action on the note. Sections 580a,<sup>11</sup> 726(b),<sup>12</sup> and 580b<sup>13</sup> were enacted during the Depression to further limit

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injured in California by an intoxicated California resident who had been served by a Nevada tavern, California had governmental interest in applying its law imposing civil liability on tavern owners who furnish liquor to intoxicated persons); *Wong v. Tenneco, Inc.*, 151 Cal. App. 3d 376, 198 Cal. Rptr. 526 (1984) (where marketing contract for crops grown in Mexico was illegal and unenforceable under Mexican law, California nevertheless has governmental interest in enforcing contract in accordance with California law); *Ashland Chemical Co. v. Provence*, 129 Cal. App. 3d 790, 181 Cal. Rptr. 340 (1982) (in action to recover on promissory note which was executed in Kentucky by a California corporation in favor of a Kentucky corporation, California has governmental interest in applying California's statute of limitations rather than Kentucky's statute); *Pacific Diamond Co. v. Superior Court*, 85 Cal. App. 3d 871, 149 Cal. Rptr. 813 (1978) (where hotel guest's valuables were stolen in Colorado hotel, California has no governmental interest in limiting the liability of a hotel outside its jurisdiction).

7. *Hersch & Co. v. C & W Manhattan Assocs.*, 700 F.2d 476 (9th Cir. 1982); *Kerivan v. Title Ins. & Trust Co.*, 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

8. Commentators have explored thoroughly the domestic operation of the California antideficiency statutes. See generally Hetland, *Deficiency Judgment Limitations in California—A New Judicial Approach*, 51 CALIF. L. REV. 1 (1963) [hereinafter cited as Hetland, *Deficiency Judgment*]; Hetland, *Real Property and Real Property Security: The Well-Being of the Law*, 53 CALIF. L. REV. 151, 159-65 (1965); Leipziger, *Deficiency Judgments in California: The Supreme Court Tries Again*, 22 U.C.L.A. L. REV. 753 (1975); Riesenfeld, *California Legislation Curbing Deficiency Judgments*, 48 CALIF. L. REV. 705 (1960); Rintala, *California's Anti-Deficiency Legislation and Suretyship Law: The Transversion of Protective Statutory Schemes*, 17 U.C.L.A. L. REV. 245 (1969).

9. For the sake of clarity, this Comment will use the term "creditor" generically to denote both mortgagees under conventional instruments and trust-deed beneficiaries. Similarly, the term "debtor" will be used generically to denote both conventional mortgagors and trustors under deeds of trust.

10. CAL. CIV. PROC. CODE § 726 (West Supp. 1985). In 1983, the two important separate functions of § 726 were recodified as §§ 726(a) and 726(b). Section 726(a) contains the security-first rule, requiring that the real property security be sold before obtaining a judgment on the note. Section 726(b) requires appraisal of the property after a *judicial* foreclosure of a mortgage if the creditor seeks a deficiency judgment. In the *nonjudicial* foreclosure of a mortgage or deed of trust, § 580a parallels § 726 in containing both a security-first rule and an appraisal rule. In this Comment, § 726 generally, or § 726(a) specifically, will be used to refer to the security-first purposes of the statute. Section 726(b) will be used when referring to the fair-value appraisal requirements of the statute.

11. CAL. CIV. PROC. CODE § 580a (West Supp. 1985).

12. CAL. CIV. PROC. CODE § 726(b) (West Supp. 1985).

13. CAL. CIV. PROC. CODE § 580b (West 1976). Section 580b provides, in part:

No deficiency judgment shall lie in any event after any sale of real property for failure of the purchaser to complete his contract of sale, or under a deed of trust, or mortgage, given to the vendor to secure payment of the balance of the purchase price of real property, or under a deed of trust, or mortgage, on a dwelling for not more than four families given to a lender to secure repayment of a loan which was in fact used to pay all or part of the purchase

creditors' rights in deficiency actions. Sections 580a and 726(b) require a fair-value hearing after both nonjudicial and judicial foreclosure sales. Both sections limit the permissible deficiency to the difference between the fair value of the property and the remaining indebtedness, thus providing protection against a creditor's inadequate bid. Section 580b disallows any creditor's action for a deficiency after the foreclosure of a purchase-money security interest. Section 580d,<sup>14</sup> enacted in 1939, prohibits a creditor from maintaining an action for a deficiency after a nonjudicial foreclosure.

Governmental interest analysis is incompatible with the case law<sup>15</sup> decided under the now discredited vested rights methodology.<sup>16</sup> Interest analysis and the vested rights approach are based upon fundamentally different premises. Governmental interest analysis relies exclusively on evaluation of the policies underlying conflicting laws. The vested rights theory attempted to connect "substantive law" issues to a particular jurisdiction by black letter rules for different fields of law. Moreover, the vested rights theory dictated that issues of "procedural law" were governed by the law of the forum. Under the territorially based rules of the vested rights theory, California's antideficiency statutes typically have been characterized as a procedural remedy. Therefore, their application has depended simply on forum location—California or foreign. Yet two recent cases, *Hersch & Co. v. C & W Manhattan Associates*<sup>17</sup> and *Kerivan*

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*price of such dwelling occupied, entirely or in part, by the purchaser.*

The italicized language reflects the 1963 amendment to § 580b.

14. CAL. CIV. PROC. CODE § 580d (West 1976). Section 580d provides, in part:

No judgment shall be rendered for any deficiency upon a note secured by a deed of trust or mortgage upon real property hereafter executed in any case in which the real property has been sold by the mortgagee or trustee under power of sale in such mortgage or deed of trust.

Because § 580d provides a complete deficiency bar following a nonjudicial foreclosure, it restricts the scope of the appraisal function of § 580a.

15. In several cases, courts have used language which explicitly tracks the vested rights doctrine including the substance-versus-procedure characterization process. *See, e.g., Commercial Nat'l Bank v. Catron*, 50 F.2d 1023, 1024 (10th Cir. 1931) (§ 726 "relates only to a remedy in the courts of California and does not affect a substantive right of contract, sought to be enforced in other courts"); *Maxwell v. Ricks*, 294 F. 255, 257 (9th Cir. 1923) ("[E]nforcement of the payment of the debt . . . is but a remedy, limited . . . [to] an action brought in the courts of California . . ."); *Martin v. Midgett*, 100 Ariz. 284, 288, 413 P.2d 754, 757 (1966) ("§§ 580b and 729 [sic] are procedural only and do not bar plaintiff from recovery in this action filed in . . . Arizona.").

Other decisions do not employ expressly the substance-versus-procedure characterization process common to traditional vested rights decisions. *See, e.g., Ould v. Stoddard*, 54 Cal. 613 (1880) (without questioning whether California or foreign substantive law governed a note secured by California property, court held that § 726 bars foreclosure of the mortgage in California after an action on the note in Ohio had been reduced to final judgment); *Yunker v. Reseda Manor*, 255 Cal. App. 2d 431, 438, 63 Cal. Rptr. 197, 202 (1967) (in a California deficiency action against a California corporation on a purchase-money loan contracted for and made payable in Nevada and secured by Nevada property, § 580b barred the deficiency judgment).

16. The vested rights theory has been severely criticized by commentators. *See infra* note 39 and accompanying text.

17. 700 F.2d 476 (9th Cir. 1982).

*v. Title Insurance & Trust Co.*<sup>18</sup> relied exclusively on existing vested rights precedents to determine the extraterritorial effect of sections 726, 580b, and 580d in conflict of laws contexts.<sup>19</sup> In effect, the *Hersch* and *Kerivan* holdings resurrect the territorial-based vested rights theory. They therefore must be considered suspect.

The California Supreme Court's adoption of governmental interest analysis has gutted existing case law of any supporting rationale.<sup>20</sup> It is necessary to reevaluate the existing conflict of laws holdings to distinguish cases with precedential value from those without continued vitality.<sup>21</sup> This Comment will consider the antideficiency statutes in prototypical conflict of laws contexts. It will apply governmental interest analysis in order to suggest policy-based resolutions of conflicts issues.

This Comment will employ two paradigms, one derived from *Hersch & Co. v. C & W Manhattan Associates*,<sup>22</sup> the other from *Kerivan v. Title Insurance & Trust Co.*<sup>23</sup> In both cases the parties made express contract provisions concerning which state's law governed the debt. The paradigms will be useful first because many future conflicts issues might be expected to fall squarely into either the *Hersch* or *Kerivan* fact pattern.

18. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983). See *infra* text accompanying notes 105-12.

19. In *Hersch*, the litigants conceded that *Yunker v. Reseda Manor*, 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967), a case seemingly decided under the traditional theory, controlled the potential conflict of laws issue relating to § 580b. *Hersch*, 700 F.2d at 478 n.2.

The *Kerivan* court relied entirely on two vested rights precedents: *Martin v. Midgett*, 100 Ariz. 284, 413 P.2d 754 (1966), see *infra* notes 97-99 and accompanying text, and *Bayside-Flushing Gardens v. Beuermann*, 36 F. Supp. 706 (D.D.C. 1941). Both *Martin* and *Bayside-Flushing* relied entirely on the vested rights methodology. In *United Bank v. K & W Trucking Co.*, 147 Cal. App. 3d 217, 195 Cal. Rptr. 49 (1983), a companion case to *Kerivan*, the court relied on the same vested rights cases that it relied on in *Kerivan*.

The *Kerivan* and *United Bank* cases were brought in California after a Colorado appellate court affirmed a trial court's deficiency judgment following a California nonjudicial foreclosure. See *United Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), cert. denied, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*).

20. For a description of the incompatibility of governmental interest analysis and the vested rights approach, see *infra* text accompanying notes 27-52.

21. The following cases address the extension of California antideficiency statutes to the foreign real-property security context: *Hersch & Co. v. C & W Manhattan Assocs.*, 700 F.2d 476 (9th Cir. 1982); *First-Trust Joint Stock Land Bank v. Meredith*, 5 Cal. 2d 214, 53 P.2d 958 (1936); *Denver Stockyards Bank v. Martin*, 177 Cal. 223, 170 P. 428 (1918); *McGue v. Rommel*, 148 Cal. 539, 83 P. 1000 (1906); *Felton v. West*, 102 Cal. 266, 36 P. 676 (1894); *Maryland Casualty Co. v. Nottingham*, 18 Cal. App. 2d 135, 63 P.2d 864 (1936).

The following cases address the potential nonapplicability of the antideficiency statutes in contexts involving California real-property security interests: *Commercial Nat'l Bank v. Catron*, 50 F.2d 1023 (10th Cir. 1931); *Maxwell v. Ricks*, 294 F. 255 (9th Cir. 1923); *Martin v. Midgett*, 100 Ariz. 284, 413 P.2d 754 (1966); *Ould v. Stoddard*, 54 Cal. 613 (1880); *Kerivan v. Title Ins. & Trust Co.*, 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983); *Mantle v. Dabney*, 47 Wash. 394, 92 P. 134 (1907).

22. 700 F.2d 476 (9th Cir. 1982).

23. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

Second, in cases with dissimilar facts, analysis of the *Hersch* and *Kerivan* fact patterns will suggest the correct resolution of the conflict of laws issues. For purposes of illustration, this Comment will evaluate the general policies of only a single foreign state within the framework of interest analysis. However, the conclusions should apply to a conflicts issue raised between California and any other state.

Part I of this Comment will outline the discrete steps of governmental interest analysis. In order to understand California's and other states' policies towards the antideficiency statutes, it also will be necessary to outline briefly the principal competing conflicts methodologies: the traditional vested rights theory and the "most significant relationship" theory underlying the *Restatement (Second) of Conflict of Laws*.<sup>24</sup> Part II will identify the leading conflict of laws precedents for the antideficiency statutes. Part III will employ governmental interest analysis to consider the extension of the antideficiency statutes to situations involving foreign security—the setting of *Hersch & Co. v. C & W Manhattan Associates*.<sup>25</sup> It will then apply interest analysis to situations involving California real property in which a creditor seeks to avoid the operation of the antideficiency statutes—the setting of *Kerivan v. Title Insurance & Trust Co.*<sup>26</sup>

## I

### RELEVANT CONFLICTS METHODOLOGIES

#### A. *The Traditional Vested Rights Doctrine*

The traditional vested rights theory<sup>27</sup> for resolving conflict of laws issues was developed in part by Justice Story<sup>28</sup> in the 1840's and later sponsored by Justice Holmes.<sup>29</sup> At the turn of the century, Professor Beale reduced the vested rights theory to a series of terse formulations titled "Summary of Conflict of Laws."<sup>30</sup> In 1923, Beale was named Reporter for the *Restatement of Conflict of Laws*.<sup>31</sup> The *Restatement*, published in 1934, enshrined his vested rights dictates.

The premise of the traditional vested rights theory was that a particular state's power to make rules of law to govern events, transactions, or

24. RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971).

25. 700 F.2d 476 (9th Cir. 1982).

26. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

27. For a brief description of the vested rights theory, see generally E. SCOLES & P. HAY, CONFLICT OF LAWS 13-14 (1982).

28. J. STORY, COMMENTARIES ON THE CONFLICT OF LAWS (2d ed. 1841).

29. See, e.g., *Mutual Life Ins. Co. v. Liebing*, 259 U.S. 209 (1922) (law of the state in which life insurance contract was executed controls).

30. See J. BEALE, A SELECTION OF CASES ON THE CONFLICT OF LAWS (1902). "Summary of the Conflict of Laws" appeared at the end of Beale's three-volume set of cases.

31. RESTATEMENT OF CONFLICT OF LAWS (1934).

relationships connected with its territory gave rise to "rights" vesting in a particular territorial jurisdiction.<sup>32</sup> Accordingly, when any forum entertained a controversy where rights were vested in a foreign state, the vested rights theory directed the forum to apply the foreign state's laws to all substantive issues in the case.<sup>33</sup> However, each forum remained free to apply its domestic law to procedural issues. The now familiar dichotomy between "substance" and "procedure" which pervades much of conflict of laws jurisprudence developed from the vested rights approach.<sup>34</sup>

Within the "procedure" characterization were included the forum state's remedies for enforcing substantive rights, whether such rights vested domestically or in a foreign jurisdiction.<sup>35</sup> In the vested rights era, California's antideficiency statutes were typically characterized as "procedure," controlling only the remedy in a California forum.<sup>36</sup> Consequently, California's antideficiency statutes were considered without effect when the controversy was adjudicated in a foreign forum, even when California property was hypothecated and California substantive law governed all elements of the secured transaction.<sup>37</sup> Conversely, California antideficiency statutes appear to have been given effect in California fora, even when foreign property was hypothecated in a secured transaction governed by foreign law.<sup>38</sup>

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32. While the vested rights precepts were included in the original *Restatement*, several leading conflict of laws cases concerning California's antideficiency statutes antedated its 1934 publication. See cases cited *supra* note 15. The following rules in Beale's 1902 treatise are reflected in the early decisions.

§ 2. In the legal sense, all rights must be created by some law . . . .

§ 6. For the creation of rights . . . there must exist some law with power to create them: or in the ordinary phrase, with jurisdiction.

§ 7. Wherever, therefore, there is a political society, there must be some complete body of law, which shall cover every event there happening . . . .

This single law is the "law of the land," a law which belongs to a certain political division of territory. The law prevails throughout this territory; and conversely, it cannot prevail as law outside it . . . .

J. BEALE, *supra* note 30, at 501-02.

33. § 48. Though a foreign right must be recognized as existing, it does not follow that it will be given any legal force . . . . [S]ince nothing can have the force of law in a State except the law of that State . . . , it follows that no foreign right can be enforced unless the law of the State so provides.

*Id.* at 517-18.

34. "§ 52. The remedy afforded for the enforcement of a foreign right is such only as the State may choose to allow. . . . § 54. Where [a] suit is brought in a foreign court, all matters relating merely to the remedy are determined by the law of the forum." *Id.* at 519-20.

35. See *id.*

36. See *supra* note 15.

37. See, e.g., *Commercial Nat'l Bank v. Catron*, 50 F.2d 1023 (10th Cir. 1931) (§ 726 not applicable in federal court sitting in New Mexico); *Maxwell v. Ricks*, 294 F. 255 (9th Cir. 1923) (§ 726 not applicable in federal court sitting in Washington); *Martin v. Midgett*, 100 Ariz. 284, 413 P.2d 754 (1966) (§§ 580b and 726 not applicable in Arizona state court).

38. See, e.g., *Yunker v. Reseda Manor*, 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967)

By the mid-twentieth century, the traditional vested rights doctrine had been repudiated thoroughly by academic commentators.<sup>39</sup> With the demise of the vested rights theory underlying the original *Restatement*, commentators began the development of modern conflict of laws methodologies. Two divergent trends developed in modern conflicts methodologies which are relevant to California conflicts jurisprudence: governmental interest analysis, to which California became committed, and the alternative "most significant relationship" theory which formed the foundation of the *Restatement (Second) of Conflict of Laws*.<sup>40</sup>

### *B. California's Commitment to Governmental Interest Analysis*

In the 1950's and 1960's, Justice Traynor led the California Supreme Court away from the traditional vested rights methodology toward an approach based upon the analysis of the policies underlying conflicting states' laws.<sup>41</sup> With Traynor's final conflict of laws opinion in *Reich v. Purcell*<sup>42</sup> and Justice Sullivan's opinion in *Hurtado v. Superior Court*,<sup>43</sup> the supreme court consolidated its commitment to a conflicts methodology based on policy analysis.

In conjunction with Traynor's approach, Professor Brainerd Currie first formally laid out the conflict of laws methodology now known as

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(§ 580b given effect in California court when purchase-money transaction seemed to be governed by Nevada law, but some contacts existed with California).

39. Professor Cook led the academic attack on the original *Restatement*. See W. COOK, *THE LOGICAL AND LEGAL BASES OF THE CONFLICT OF LAWS* (1942); see also B. CURRIE, *SELECTED ESSAYS ON THE CONFLICT OF LAWS* (1963); E. LORENZEN, *SELECTED ARTICLES ON THE CONFLICT OF LAWS* (1947); Cavers, *A Critique of the Choice-of-Law Problem*, 47 HARV. L. REV. 173 (1933).

40. RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971).

41. See cases cited *supra* note 1.

42. 67 Cal. 2d 551, 432 P.2d 727, 63 Cal. Rptr. 31 (1967). In *Reich*, Traynor avoided any mention of vested rights mechanics, relying entirely on analysis of the policies underlying California statutes. He determined that California had no interest in extending its own law giving unlimited wrongful-death recoveries to litigation between a California defendant and a plaintiff originally residing in Ohio over a fatal automobile collision in Missouri. 67 Cal. 2d at 556, 432 P.2d at 730, 63 Cal. Rptr. at 34.

43. 11 Cal. 3d 574, 522 P.2d 666, 114 Cal. Rptr. 106 (1974). In *Hurtado*, Justice Sullivan confirmed California's adoption of governmental interest analysis as its conflict of laws methodology. The court in *Hurtado* applied California law rather than Mexican law on wrongful-death recovery limitations where an accident occurred in California and involved a California defendant, but plaintiff and decedent were Mexican domiciliaries. The court reasoned that Mexico had no interest in applying its law to put a ceiling on its own domiciliary's wrongful-death recovery. 11 Cal. 3d at 581, 522 P.2d at 670, 114 Cal. Rptr. at 110.

Justice Sullivan, in *Hurtado*, focused on the following language in *Reich* as evidence of Traynor's adoption of interest analysis: "The forum must search to find the proper law to apply based upon the interests of the litigants and the involved states." 11 Cal. 3d at 580 n.2, 522 P.2d at 669 n.2, 114 Cal. Rptr. at 109 n.2. (quoting *Reich v. Purcell*, 67 Cal. 2d 551, 553, 432 P.2d 727, 729, 63 Cal. Rptr. 31, 33 (1967)).

governmental interest analysis.<sup>44</sup> In part, Currie developed his theories with reference to, and in defense of, Traynor's opinions.<sup>45</sup> Both Traynor's<sup>46</sup> and Currie's<sup>47</sup> approaches first identify the policies underlying

44. For Currie's earliest methodological statements, see Currie, *The Constitution and the Choice of Law: Governmental Interests and the Judicial Function*, 26 U. CHI. L. REV. 9, 9-10 (1958); Currie, *Notes on Methods and Objectives in the Conflict of Laws*, 1959 DUKE L.J. 171, 178.

Currie's major articles have been collected in B. CURRIE, *supra* note 39. Two later articles are Currie, *The Disinterested Third State*, 28 LAW & CONTEMP. PROBS. 754 (1963); Currie, *Full Faith and Credit, Chiefly to Judgments: A Role for Congress*, 1964 SUP. CT. REV. 89. Valuable reviews of Currie's approach can be found in Sedler, *The Governmental Interest Approach to Choice of Law: An Analysis and A Reformulation*, 25 U.C.L.A. L. REV. 181, 181-91 (1977) and Kay, *Theory into Practice: Choice of Law in the Courts*, 34 MERCER L. REV. 521, 538-52 (1983).

45. See Currie, *supra* note 1; see also Currie, *Survival of Actions: Adjudication versus Automation in the Conflict of Laws*, 10 STAN. L. REV. 205 (1958).

46. After his retirement from the California Supreme Court, Justice Traynor identified the methodological steps which he had developed for conflicts cases:

*First:* The court should apply forum law and not interject a choice-of-law issue into a case when the parties have not done so.

*Second:* When the parties have presented a choice-of-law issue, the court should determine at the outset whether the issue is controlled by a forum statute and, if not, whether it is controlled by a forum judicial precedent.

*Third:* If the court concludes that a forum statute or judicial precedent does not control the choice-of-law issue, the court should determine whether the forum's policy for domestic cases should be limited to such cases or extended to cases with multi-State elements.

*Fourth:* If the court finds that the forum policy extends to multi-State cases, it should then determine whether the forum's contacts with the case are substantial enough to give the forum an interest in applying that policy.

*Fifth:* If the court finds that the forum has an interest in applying its policy, it should ordinarily apply that policy even though it is in head-on conflict with the policy of another interested State.

Traynor, *War and Peace in the Conflict of Laws*, 25 INT'L & COMP. L.Q. 121 (1976) [hereinafter cited as Traynor, *War and Peace*]. Justice Sullivan's introduction of the comparative impairment principle in *Bernhard v. Harrah's Club*, 16 Cal. 3d 313, 546 P.2d 719, 128 Cal. Rptr. 215, *cert. denied*, 429 U.S. 859 (1976), *overruled on other grounds*, *Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984), fundamentally alters only step 5 in Traynor's formulation. See *infra* text accompanying notes 51-52. Like Currie, Traynor would have applied forum law in a true conflict.

For a complete description of Justice Traynor's role in the development of governmental interest methodology, see Kay, *supra* note 1. Traynor, a member of the American Law Institute, was also named Advisor to the Reporter of the *Restatement (Second) of Conflict of Laws*. *Id.* at 776 & n.193.

For Traynor's written contributions to the conflict of laws field, see Traynor, *War and Peace*, *supra*; Traynor, *Is This Conflict Really Necessary?*, 37 TEX. L. REV. 657 (1959).

47. Currie's methodology is set out here for comparison with the conjunction of the methodologies of Currie and Justice Sullivan employed in this Comment, see *infra* text accompanying notes 51-52.

1. When a court is asked to apply the law of a foreign state different from the law of the forum, it should inquire into the policies expressed in the respective laws, and into the circumstances in which it is reasonable for the respective states to assert an interest in the application of those policies. In making these determinations the court should employ the ordinary processes of construction and interpretation.

2. If the court finds that one state has an interest in the application of its policy in the circumstances of the case and the other has none, it should apply the law of the only interested state.

3. If the court finds an apparent conflict between the interests of the two states, it should reconsider. A more moderate and restrained interpretation of the policy or interest of one state or the other may avoid conflict.

ing the conflicting laws and proceed to analyze the states' interests in applying their respective laws in the multistate context. A second element common to both approaches is the resolution of false conflicts—situations in which only a single state is found to have an interest in applying its law. In a false conflict, both Traynor's and Currie's approach would apply the law of the only state found to have an interest.<sup>48</sup>

California's method of resolving true conflicts—when both states have a governmental interest in applying their rule of law—was not resolved until 1976, in *Bernhard v. Harrah's Club*.<sup>49</sup> In *Bernhard*, Justice Sullivan determined that true conflicts should be resolved in accordance with the principle of comparative impairment. Under this doctrine, the court applies the law of the state whose policies would be most impaired should the competing state's law be applied.<sup>50</sup> With *Bernhard*, California's version of governmental interest analysis reached its fullest development. *Bernhard* outlines the steps that a court should take in a conflicts case:

1. When a court is asked to apply the law of a foreign state different from the law of the forum, it should inquire into the policies expressed in the respective laws, and into the circumstances in which it is reasonable for the respective states to assert an interest in the application of those policies. In making these determinations the court should employ the ordinary processes of construction and interpretation.
2. If the court finds that one state has an interest in the application of its policy in the circumstances of the case and the other has none . . . [a false conflict exists. The court] should apply the law of the only inter-

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4. If, upon reconsideration, the court finds that a [true] conflict between the legitimate interests of the two states is unavoidable, it should apply the law of the forum.

5. If the forum is disinterested, but an unavoidable conflict exists between the interests of two other states, and the court cannot with justice decline to adjudicate the case, it should apply the law of the forum, at least if that law corresponds with the law of one of the other states . . . .

W. REESE & M. ROSENBERG, CASES AND MATERIALS ON CONFLICT OF LAWS 470 (7th ed. 1978).

The California Supreme Court's formulation of governmental interest analysis alters fundamentally only step number 4 in Currie's methodology. While Currie would apply forum law in a true conflict situation, the California Supreme Court would quantify the extent of impairedness of the competing states' policies, and apply the law of the state whose policies would be more greatly impaired. See *infra* text accompanying notes 51-52.

48. See *supra* notes 46 & 47.

49. 16 Cal. 3d 313, 546 P.2d 719, 128 Cal. Rptr. 215, cert. denied, 429 U.S. 859 (1976), overruled on other grounds, *Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984).

50. Professor Baxter developed comparative impairment analysis as a tool for resolving true conflicts. See Baxter, *Choice of Law and the Federal System*, 16 STAN. L. REV. 1 (1963).

Some commentators argue that the introduction of comparative impairment into California's interest methodology is an undesirable deviation from Currie's formulation of interest analysis. See Kay, *The Use of Comparative Impairment to Resolve True Conflicts: An Evaluation of the California Experience*, 68 CALIF. L. REV. 577 (1980); see also Kanowitz, *Comparative Impairment and Better Law: Grand Illusions in the Conflict of Laws*, 30 HASTINGS L.J. 255 (1978).

ested state.<sup>51</sup>

3. [If the] preliminary analysis . . . identifie[s] a true conflict of the governmental interests involved as applied to the parties under the particular circumstances of the case, the "comparative impairment" approach to the resolution of such conflict seeks to determine which state's interest would be more impaired if its policy were subordinated to the policy of the other state. This analysis proceeds on the principle that true conflicts should be resolved by applying the law of the state whose interest would be the more impaired if its law were not applied.<sup>52</sup>

### C. *The Most Significant Relationship Theory of the Restatement (Second) of Conflicts of Law*

Academic repudiation of the vested rights theory hastened California's adoption of interest analysis. It also spurred the American Law Institute to begin work on the *Restatement (Second) of Conflicts of Law* in 1953. Professor Reese, the Reporter for the *Restatement (Second)*, intended to formulate jurisdiction-selecting rules to substitute for those of the first *Restatement*. Reese rejected the modern theorists' arguments for a case-by-case analysis of the policies underlying competing laws.<sup>53</sup> He maintained that black letter jurisdiction-selecting rules were appropriate for conflict of laws issues in many fields of law. In fields where the first *Restatement* rules had been rejected most frequently, Reese proposed that the black-letter rules be made more flexible by utilization of the most significant relationship theory.<sup>54</sup> The vested rights theory typically had employed a single factor, such as domicile, place of contracting, or place of wrong, to connect an issue with a particular jurisdiction. The most significant relationship theory, by contrast, was intended to allow a flexible evaluation of various factors which might connect an issue to a particular jurisdiction.<sup>55</sup>

In response to academic criticism that the most significant relationship theory did not reflect underlying state policies,<sup>56</sup> the *Restatement*

51. W. REESE & M. ROSENBERG, *supra* note 47, at 470. For the complete text of Currie's methodology, see *supra* note 47. The text of Currie's false conflict test is used here for clarity. The court in *Bernhard* did not adopt explicitly this formulation.

52. Justice Sullivan's formulation of the comparative impairment principle is extracted from the text of *Bernhard*, 16 Cal. 3d at 320, 546 P.2d at 723, 128 Cal. Rptr. at 219.

53. See Reese, *Conflict of Laws and the Restatement Second*, 28 LAW & CONTEMP. PROBS. 679 (1963).

54. See Kay, *supra* note 44, at 552-56.

55. See *id.*

56. See, e.g., Currie, *Comments on Babcock v. Jackson, A Recent Development in Conflict of Laws*, 63 COLUM. L. REV. 1233, 1242 (1963) ("If I were asked to restate the law of conflict of laws I would decline the honor. A descriptive restatement with any sort of internal consistency is impossible."); Ehrenzweig, *The "Most Significant Relationship" in the Conflicts Law of Torts—Law and Reason Versus the Restatement Second*, 28 LAW & CONTEMP. PROBS. 700 (1963); Ehrenzweig, *The Second Conflicts Restatement: A Last Appeal for Its Withdrawal*, 113 U. PA. L. REV. 1230 (1965);

(*Second*) drafters compromised, in 1967, by including section 6, entitled "Choice of Law Principles." Section 6 offers seven general choice-of-law principles to guide a court in determining which jurisdiction's law should be applied.<sup>57</sup> Two of those are probably most important to the proponents of governmental interest analysis. They are section 6(2)(b), providing that the relevant policies of the forum should be considered, and section 6(2)(c), providing that the relevant policies of other interested states should be considered.<sup>58</sup> In substance, these section 6 provisions duplicate elements of interest analysis.<sup>59</sup>

As a result of the section 6 compromise, the *Restatement (Second)* reflects an uneasy marriage between the case-by-case approach requiring policy analysis and the jurisdiction-selecting black letter rules. The only attempt in *Restatement (Second)* to reconcile the black letter rules and the interest analysis approach occurs in a comment to section 6 indicating that the black letter rules already accommodate the policy factors encompassed within the section.<sup>60</sup>

The black letter rules of the *Restatement (Second)* rely entirely on the most significant relationship theory which is fundamentally incompatible with governmental interest analysis. Recognizing this, the California Supreme Court's most recent conflict of laws decisions convey

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Ehrenzweig, *American Conflicts Law in Its Historical Perspective: Should the Restatement Be "Continued"?*, 103 U. PA. L. REV. 133 (1954).

57. Section 6 reads:

Choice-of-Law Principles

(1) A court, subject to constitutional restrictions, will follow a statutory directive of its own state on choice of law.

(2) When there is no such directive, the factors relevant to the choice of the applicable rule of law include

(a) the needs of the interstate and international systems,

(b) the relevant policies of the forum,

(c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,

(d) the protection of justified expectations,

(e) the basic policies underlying the particular field of law,

(f) certainty, predictability and uniformity of result, and

(g) ease in determination and application of the law to be applied.

RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 (1971).

58. *Id.* § 6(2)(b), (c).

59. See Kay, *supra* note 44, at 552-56. The early tentative drafts of *Restatement (Second)* made no efforts to integrate Reese's most significant relationship theory with the flexible policy analyses favored by Currie and other scholars. The initial introduction of § 6 occurred in 1965. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 (Tent. Draft No. 12, 1965). The current version of § 6 appeared at the A.L.I.'s annual meeting in May, 1967. See Kay, *supra* note 1, at 777. Reese stated that "the Advisers, and particularly Chief Justice Traynor, felt that this matter was of some importance, and that it should be put in black letter form." A.L.I., 44TH ANNUAL MEETING: PROC. 394-95 (1967).

60. "Those chapters in the Restatement of this Subject which are concerned with choice of law state the rules which the courts have evolved in accommodation of the factors listed in [§ 6(2)]." RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 comment c (1971).

an express rejection of the black letter rules of *Restatement (Second)*.<sup>61</sup>

However, though the black letter rules of *Restatement (Second)* may play no part in determining California's policies, they may well define the policies of those states which have elected to follow them. Section 2 of the *Restatement (Second)* declares that its "Conflict of Laws rules, when adopted, become as definitely a part of the law as any other branch of the state's law."<sup>62</sup> The *Restatement (Second)* offers detailed jurisdiction-selecting rules for antideficiency conflicts issues.<sup>63</sup> It was the incorporation of these rules into Colorado's substantive law<sup>64</sup> that gave rise to the antideficiency conflicts issue in *Kerivan v. Title Insurance & Trust Co.*<sup>65</sup>

61. *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978) (where key employee of a California corporation was injured in Louisiana due to the negligence of a multinational corporation, Louisiana law applied, disallowing a cause of action by the employer for loss of services). The supreme court stated plainly that the trial court erred in relying on the most significant relationship theory rather than governmental interest analysis. *Id.* at 161, 583 P.2d at 723, 148 Cal. Rptr. at 869.

The supreme court's most recent action involving conflict of laws issues was to depublish an appellate court opinion which relied in part on the black letter rules in the *Restatement (Second)*. *Duarte v. McKenzie Constr. Co.*, 152 Cal. Rptr. 373 (1st Dist. 1979) (not officially reported) (where an employee of a California subcontractor was injured on a Nevada construction site, Nevada law applied regarding worker's compensation was applied, disallowing a claim against third parties). In *Duarte*, the court applied governmental interest analysis, but identified California's policies and interests with extensive reference to the black letter rules of the *Restatement (Second)*, characterizing such rules in tort cases as "recognized principles of conflict of laws." *Id.* at 379.

62. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 5 comment a (1971).

There remains the question whether a foreign state's conflict of laws methodology is constrained by due process limitations or possible full faith and credit recognition of the intended substantive effect of California's statutes. In *Allstate Ins. Co. v. Hague*, 449 U.S. 302 (1981), the United States Supreme Court reviewed a decision by the Minnesota Supreme Court to apply Minnesota insurance law, in accordance with its conflicts methodology. The insurance policy involved was issued in Wisconsin to a Wisconsin resident who was killed in Wisconsin. The plurality opinion focused on an aggregation of the contacts between Minnesota and the insured, which were sufficient to support the Minnesota court's application of forum law.

Justice Brennan, author of the plurality opinion in *Allstate*, stated only that "for a State's substantive law to be selected in a constitutionally permissible manner, that State must have a significant contact or significant aggregation of contacts, creating state interests, such that choice of its law is neither arbitrary nor fundamentally unfair." *Allstate*, 449 U.S. at 312-13. For a thorough review of the post-*Allstate* environment concerning constitutional limits on conflict of laws methodologies, see *Symposium, Choice-of-Law Theory After Allstate Insurance Co. v. Hague*, 10 HOFSTRA L. REV. 1 (1981).

In order to avoid conflict of laws decisions in foreign forums which refuse to give effect to §§ 726, 580b, and 580d as intended by California's underlying policies, the most practical solution would be to obtain declaratory relief in California, which would be owed recognition in the foreign court under the full faith and credit clause.

63. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 comments a-e (1971).

64. The Colorado appellate court relied on *Restatement (Second)* § 229 comment e, to conclude that a Colorado resident lender was not required to comply with § 580d following a California nonjudicial foreclosure, since the promissory note was governed by Colorado law. See *United Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), cert. denied, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*).

65. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

## II

CONFLICT OF LAWS PRECEDENTS REGARDING  
ANTIDEFICIENCY ISSUES

Conflict of laws problems under California's antideficiency statutes can arise in a California forum in two paradigmatic fact patterns. First, a litigant may attempt to extend the operation of any of the antideficiency statutes to a lending transaction involving a foreign real-property security interest. Such extraterritorial extension has been attempted with most of the antideficiency statutes.<sup>66</sup> Section *A* below reviews these precedents. Second, conflict of laws issues may develop when the impact of the antideficiency statutes on security transactions involving California real-property security interests is called into question by a foreign action or a foreign contract. The precedents<sup>67</sup> regarding such avoidance issues are reviewed in Section *B*.

*A. Extension of Antideficiency Statutes to Security Transactions  
Involving Foreign Real Property*

*1. Foreign Property: Extension of Section 726*

In *Felton v. West*,<sup>68</sup> decided in 1894, the California Supreme Court first analyzed the operation of section 726 in a fact setting involving foreign property. In *Felton*, a domestic California lending transaction between California domiciliaries was secured by Oregon property. The court indicated that a California forum would give effect to section 726 by allowing an affirmative defense<sup>69</sup> to an attempted action on the note regardless of the situs of the real-property security.<sup>70</sup> Later California

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66. See cases cited *supra* note 21.

67. See cases cited *supra* note 21.

68. 102 Cal. 266, 36 P. 676 (1894). In *Felton*, both the creditor and debtor were California residents and the note was made payable in California. The debtor hypothecated Oregon real property as security for the note. *Id.* at 267, 36 P. at 676.

69. In *Felton*, the creditor had completed a foreclosure action in Oregon and subsequently brought an action in California for the deficiency. Service of process was made by publication since the debtor was not physically present in Oregon. Since the creditor foreclosed first, he fully complied with the primary-fund policy underlying § 726. No attempt was made to encumber or execute on the debtor's general assets before foreclosure of the security interest. Consequently, the court in *Felton* only questioned whether the creditor had violated the single-action policy underlying § 726, which requires the creditor to obtain all relief, foreclosure and deficiency, in a single action. See *infra* text accompanying notes 124-37. The court determined that the one-action sanction could not be justified because the Oregon court had no jurisdiction over the debtor and therefore could not render a personal money judgment for the deficiency. "[O]ne action . . . in Oregon . . . could not be made sufficient to secure all of respondent's rights." *Felton*, 102 Cal. at 270, 36 P. at 677. The court in *Felton* also stated that the creditor "could not bring a personal action at law upon the note only, for our courts would not allow him to waive his security." *Id.* at 269, 36 P. at 677. Thus, the court in *Felton* would have given effect to the affirmative defense requiring foreclosure first, had that issue been before the court.

70. Much apparent confusion surrounds the following passage in *Felton*: "The circumstances

Supreme Court cases backed away from the *Felton* court's willingness to give effect to section 726 in such foreign-security transactions.<sup>71</sup> Not

of this case take it completely without the purview of [§ 726] . . . . This section only refers to actions for the recovery of a debt secured by a mortgage upon property situated in the *state of California*." *Felton*, 102 Cal. at 270, 36 P. at 677 (emphasis in original). The "circumstances" referred to in the *Felton* passage concerned the Oregon foreclosure, where absent the debtor's consent to jurisdiction, both foreclosure and a deficiency relief could not be obtained in a single action. It should be clear that the cited passage refers only to the potential imposition of the one-action sanction in relation to the single-action policy, since in the preceeding paragraph the court stated that the affirmative defense would be enforced to require foreclosure before a California action on the note. The court in *Felton* concluded its opinion by again restating that the affirmative defense would defeat an attempted action on the note in California. "[The creditor] had no standing whatever in the courts of California. He was compelled to go to Oregon to bring his action." *Id.* at 271, 36 P. at 678. *Felton* stands for the straightforward proposition that the primary-fund policy is enforceable by the affirmative defense in foreign-security transactions, while the single-action policy is not enforceable if the creditor cannot obtain both foreclosure and deficiency relief in a single action. In California-security transactions, since both foreclosure and deficiency relief are always available in the single action, California courts usually have found it unnecessary to focus on the discrete policies underlying § 726. See *infra* text accompanying notes 124-37.

71. See, e.g., *McGue v. Rommel*, 148 Cal. 539, 83 P. 1000 (1906). In *McGue*, the creditor brought an action on a note which was secured by, among other interests, "concessions granted by the republic of Mexico . . . to sell a large body of the public lands of that republic." *Id.* at 542, 83 P. at 1001. The "concession" had lapsed and was therefore worthless; the other security similarly was worthless. The case could have been categorized as a worthless-security exception to the § 726 affirmative defense, thus allowing the action on the note. See R. BERNHARDT, CALIFORNIA MORTGAGE AND DEED OF TRUST PRACTICE, § 4.6, at 144-46 (1979). Instead, the court in *McGue* allowed the action on the note, stating that § 726 "refers solely to debts secured by mortgages of property situated in the state of California . . .," *McGue*, 148 Cal. at 545, 83 P. at 1002 (emphasis added), citing *Felton* in support. The italicized language of the *McGue* passage, in fact, is a near verbatim repetition of the language employed in *Felton*, *supra*, note 70. However, the section of *Felton* apparently referred to by the court in *McGue* dealt only with the one-action sanction aspect of § 726—not the affirmative defense which was implicated in *McGue*. Hence, the *Felton* holding was not on point. In fact, *Felton* supported the enforcement of the affirmative defense in foreign-security transactions, at least when the parties were California domiciliaries and the note was executed and made payable in California.

See also *First-Trust Joint Stock Land Bank v. Meredith*, 5 Cal. 2d 214, 53 P.2d 958 (1936); *Denver Stockyards Bank v. Martin* 177 Cal. 223, 170 P. 428 (1918).

In *Meredith*, the note was executed in Iowa by Iowa residents and was secured by Iowa property. An evident post-transaction change of residency by the debtor resulted in an action on the note in California. Had § 726 been characterized as a procedural remedy, strict application of the vested rights doctrine would have required foreclosure first. However, the court cited *Felton* for the proposition that the affirmative defense was not allowable, *Meredith*, 5 Cal. 2d 214, 217, 53 P.2d 958, 959, although *Felton* supported the operation of the affirmative defense in foreign-security contexts.

*Denver Stockyards* also involved a foreign note and foreign security. Colorado residents had entered into a lending transaction secured by Colorado property. The action was brought in California by an executor of the Colorado decedent's estate. The court cited *Felton* for the proposition that the affirmative defense was not available in foreign-security transactions. In fact, *Felton* supported the operation of the affirmative defense.

*Denver Stockyards* and *Meredith* can be reconciled with *Felton*. The affirmative defense should be allowed in fact patterns like the one in *Felton* where there exists an entirely domestic lending transaction. The affirmative defense should *not* be allowed in *Meredith* and *Denver Stockyards* fact patterns where there exists an entirely foreign lending transaction. See *infra* text accompanying notes 160-63.

For a previous attempt to reconcile *Felton* with other early decisions concerning the extraterritorial effect of § 726, see generally Note, *Mortgages: Cal. Code Civ. Proc. § 726 as Creating a Condi-*

only did these later cases fail to distinguish *Felton*, they most frequently cited it to support the *nonapplicability* of the section 726 affirmative defense in such foreign-security contexts.<sup>72</sup>

The court in *Felton* did not expressly characterize section 726 as substantive or procedural law, and the opinion supports readings consistent with either characterization.<sup>73</sup> Yet, later opinions characterizing section 726 as procedural law cited *Felton* as support.<sup>74</sup> However, in *First-Trust Joint Stock Land Bank v. Meredith*,<sup>75</sup> the most recent California Supreme Court conflicts case dealing with section 726, the court declined to enforce section 726 by means of the affirmative defense. The court implicitly characterized the statute as a substantive rule of law.<sup>76</sup> In *Meredith*, the promissory note was executed in Iowa and was secured by Iowa property. Only a post-transaction change of residence by the debtor brought the action on the note before a California court. The court stated that the security-first policy was to be determined by Iowa law—implying that Iowa was the state in which substantive rights had vested.<sup>77</sup>

In *Hersch & Co. v. C & W Manhattan Associates*,<sup>78</sup> where the loan agreement was governed by California law but was secured by Iowa and New Mexico real property, the Ninth Circuit did not give effect to section 726 via the affirmative defense. The court cited *Felton*, although not

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*tional Cause of Action: Enforcement of a Mortgage Debt in a Foreign Jurisdiction: Laws Applicable in an Action for a Deficiency Judgment Outside the State of Situs*, 25 CALIF. L. REV. 576 (1937).

72. The inconsistencies between *Felton*, on the one hand, and *McGue*, *Denver Stockyards*, and *Meredith*, on the other hand, arise from the inadequate definitions of the two policies underlying § 726, single-action and primary-fund. See *infra* text accompanying notes 124-29.

73. In *Felton*, the court did not impose the one-action sanction. The opinion could be interpreted either as creating an equitable exception to a procedural vested rights characterization or as limiting the reach of § 726 in accordance with a substantive characterization. Cf. *Toby v. Oregon Pac. R.R.*, 98 Cal. 490, 33 P. 550 (1893). In *Toby*, decided the year before *Felton*, the court seemed to characterize § 726 as procedural law rather than substantive law, although the conflicts issue was not made explicit. *Toby* involved the foreclosure of a mortgage on a ship entered into in New York by a Florida company with a Oregon corporate debtor. The court held that the fact that the ship was within the jurisdiction of a California court was sufficient to invoke the operation of § 726. (Section 726 was amended in 1963, with the enactment of the CALIFORNIA COMMERCIAL CODE, and no longer applies to security interests in personal property).

74. See, e.g., *Maxwell v. Ricks*, 294 F. 255, 256-57 (9th Cir. 1923).

75. 5 Cal. 2d 214, 53 P.2d 958 (1936).

76. Within the vested rights methodology, the nonapplicability of § 726 would imply it was characterized as substantive law since the note was executed in Iowa. The *Meredith* court stated: "It is beyond dispute that these provisions [of § 726] deal with procedure only and cannot operate extraterritorially." *First-Trust Joint Stock Land Bank v. Meredith*, 5 Cal. 2d 214, 217, 53 P.2d 958, 959 (1936).

77. The court in *Meredith* did not consider § 726 relevant, since substantive rights between the parties originated at the inception of the transaction in Iowa. "The question whether the [creditor] . . . has waived its security is one properly for the courts of the state of Iowa in the event the plaintiff institutes a foreclosure proceeding in that state after having brought its action on the note alone in this state." *Id.* at 218, 53 P.2d at 959.

78. 700 F.2d 476 (9th Cir. 1982).

on point, as authority for the holding.<sup>79</sup>

The section 726 precedents fail to examine the policies underlying the one-action rule. As a consequence, it remains unclear under what circumstances, if any, a California forum should allow a California domiciliary debtor to force a creditor to foreclose on the foreign property before allowing an action on the note. Governmental interest analysis offers the methodological tools to fashion principled applications or nonapplications of section 726.

## 2. *Foreign Property: Extension of Section 580b*

Section 580b bars a deficiency judgment on a purchase-money mortgage. The leading conflict of laws case involving section 580b is *Yunker v. Reseda Manor*,<sup>80</sup> decided in 1967. In *Yunker*, a California corporation operating in Nevada bought land in Nevada financed in part by the Nevada domiciliary seller. The indebtedness was secured by a purchase-money mortgage, apparently governed by Nevada law.<sup>81</sup> After foreclosure, the seller brought an action for the deficiency in California against the California corporation which had defaulted.<sup>82</sup> The California debtor claimed the action was barred by section 580b,<sup>83</sup> but the Nevada creditor argued that the court should apply Nevada law—which provided no purchase-money deficiency bar—since Reseda Manor was doing business in Nevada and all transactional contacts had occurred there.<sup>84</sup> The *Yunker* court barred the deficiency judgment but obscured the doctrinal basis for its holding.<sup>85</sup> The opinion offered no evaluation of whether the

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79. *Id.* at 478 n.3.

80. 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967).

81. In *Yunker*, there was a senior third-party purchase-money lender who conducted the senior sale. The § 580b defense extends to sold-out junior purchase-money creditors who bring an action on the note for what has been labeled a “Brown v. Jensen deficiency.” The reference is to *Brown v. Jensen*, 41 Cal. 2d 193, 259 P.2d 425 (1953). See Hetland, *Deficiency Judgment*, *supra* note 8, at 7-12.

82. Although the *Yunker* opinion does not explain why the creditor brought the deficiency action in California rather than Nevada, it was likely an attempt by the creditor to maintain a single action against both Reseda Manor, the California corporate purchaser, and Len, the owner of Reseda Manor who had guaranteed the corporation’s obligation. The court noted that respondents alleged this purpose in their brief. *Yunker*, 255 Cal. App. 2d at 436, 63 Cal. Rptr. at 201. The creditor might not have been able to assume jurisdiction over the guarantor in Nevada. The guarantee issue was returned to the trial court for factual determinations. *Id.* at 438-39, 63 Cal. Rptr. at 202-03.

83. *Id.* at 432, 63 Cal. Rptr. at 199.

84. *Id.* at 436, 63 Cal. Rptr. at 201.

85. The court in *Yunker* stated that “purchase money security transactions . . . are valid . . . [b]ut the creditor may not invoke California law in event of deficiency because deficiency judgments are forbidden ‘in any event’ to vendors [in a California forum].” *Id.* at 438, 63 Cal. Rptr. at 202. The court took the “in any event” language from the text of the statute. See *supra* note 13. The cited passage could be interpreted to characterize § 580b as a domestic procedural remedy in accordance with the traditional vested rights theory. However, the court also cited various “contacts” with California as support for its decision to apply § 580b. “[T]here is a particular reason for finding

policies underlying section 580b supported the application of the deficiency bar.

By contrast, the court in *Kish v. Bay Counties Title Guaranty Co.*<sup>86</sup> declared that in purchase-money financing of a Nevada property sale, the section 580b antideficiency rights were integrated into the contract, which was to be performed in California and was governed by California law.<sup>87</sup> Neither the *Kish* nor the *Yunker* holding is supported by an analysis of the policies underlying section 580b. Because they apply section 580b inconsistently, and more importantly, because they lack policy analysis, *Yunker* and *Kish* offer little guidance for evaluating section 580b in accordance with interest analysis.

In *Hersch & Co. v. C & W Manhattan Associates*,<sup>88</sup> where the loan agreement was governed by California law, the Ninth Circuit, sitting in California, relied exclusively on *Yunker* to uphold the application of section 580b.<sup>89</sup> The *Hersch* case merits reanalysis to determine the proper extraterritorial effect of section 580b, since the opinion did not rely on governmental interest analysis.

### 3. *Foreign Property: Extension of Section 580d*

No reported case has yet determined the proper extraterritorial reach of section 580d. However, unquestioned adherence to the vested rights theory, including the characterization of section 580d as a California procedural remedy, could direct a California court to apply the section 580d deficiency bar following a foreign nonjudicial foreclo-

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California contacts here. According to [the debtor's] declaration, [the creditor] told him . . . that the law of Nevada was the same as that of California in respect of deficiency judgments. . . . [W]here respondents contend . . . superior contacts of the state of situs exist, we deem it relevant to consider the statement alleged . . . ." *Id.* at 437, 63 Cal. Rptr. at 202. Such listing of "contacts" might also reflect the most significant relationship theory of the *Restatement (Second) of Conflict of Laws*, then in tentative draft form.

86. 254 Cal. App. 2d 725, 62 Cal. Rptr. 494 (1967). In *Kish*, a California resident purchased Nevada property and sold California property in a single transaction. A California resident real estate agent loaned purchase money to the purchaser which was to be secured by the Nevada property. The purchaser later successfully sued in Nevada to rescind the purchase contract relating to the Nevada property. Further, the defendant title company had prepared a defective junior purchase-money lender's security instrument so that the junior lender was unsecured. The purchaser, in a cross-action, contended that misconduct by the title company had denied him the protection of § 580b, which he theorized would have prevented the creditor's action on the note.

87. The court in *Kish* stated:

Section 580b . . . destroys rights that would otherwise exist, by directing that any satisfaction of the debt must come from the land. The protection the statute provides is a part of the contract between borrower and secured lender. The fact that the land lies in another state makes no difference, when the contract was made in California and was to be performed here.

*Id.* at 733, 62 Cal. Rptr. at 500.

88. 700 F.2d 476 (9th Cir. 1982).

89. *Id.* at 478 n.2.

sure if the deficiency action were maintained in a California forum.<sup>90</sup> The reasoning of a California appellate court in the counterpart section 580d avoidance case, *Kerivan v. Title Insurance & Trust Co.*,<sup>91</sup> would support such a holding. In *Kerivan*, the court reasoned that section 580d constituted a California procedural remedy that could be ignored by a foreign forum.<sup>92</sup> The *Kerivan* court's reasoning was supported exclusively by vested rights precedents.<sup>93</sup> It will be the task of future California courts applying interest analysis to examine the policies underlying section 580d in deciding whether the deficiency proscription should apply following foreign foreclosures.

#### 4. *Foreign Property: Extension of the Fair-Value Statutes*

No precedents dictate whether California's fair-value statutes apply following a foreclosure of a security interest in foreign property when the deficiency action either takes place in California or transactional contacts might invoke California law. Thus, courts are free to use governmental interest analysis to develop a policy-based rationale for the application or nonapplication of the fair-value provisions in foreign-security contexts.

#### B. *Avoidance of the Antideficiency Statutes in Security Transactions Involving California Real Property*

Issues related to the avoidance of California's antideficiency statutes typically arise when the promissory note is governed by foreign law, but the security is California property and the security contract is expressly or impliedly governed by California law. These issues also may arise in an entirely domestic California transaction in which the creditor attempts to maintain a deficiency action in a foreign state.

##### 1. *California Property: Section 726 Avoidance*

The typical section 726 avoidance issue is presented when, in the context of a California-property secured transaction, a creditor obtains a judgment on the note in a foreign forum and later attempts to foreclose the California security interest. *Ould v. Stoddard*,<sup>94</sup> decided in 1880, is the leading precedent. In *Ould*, the California Supreme Court gave effect

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90. Under the vested rights theory, § 580d could be labeled a procedural remedy as were §§ 726 and 580b. In a case involving a foreign nonjudicial foreclosure followed by a California deficiency action, a California court strictly following the vested rights dictates might ignore the foreign substantive foreclosure law and apply § 580d as domestic procedure simply because the deficiency controversy arose in a California forum.

91. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

92. See *infra* notes 105-12 and accompanying text.

93. See *infra* note 112.

94. 54 Cal. 613 (1880). For an earlier discussion of the holding in *Ould*, see Note, *supra* note 71, at 591-92.

to section 726, holding that a creditor had waived the security interest in the California property by obtaining a final judgment in an initial action on the note in Ohio. The *Ould* decision did not expressly characterize section 726 as a procedural remedy in accordance with the traditional vested rights theory. However, the holding can probably best be explained by the court's reasoning that section 726 related to domestic procedure. Had the court considered section 726 to confer substantive contract rights, it would have been compelled to review the circumstances surrounding the actual contract, such as whether the parties were Ohio domiciliaries entering into the contract in Ohio, or California domiciliaries contracting in California. The *Ould* court made no findings on the issue. The continued vitality of *Ould* is thus questionable.

The court in *First-Trust Joint Stock Land Bank v. Meredith*<sup>95</sup> held that the place of contracting governs the application of the security-first policy. Under this view, a court should focus on the law which impliedly governed the promissory note.<sup>96</sup> In order to determine the proper effect of section 726 in California-security transactions, it is necessary to focus squarely on the California policies underlying section 726 through interest analysis.

## 2. California Property: Section 580b Avoidance

In *Martin v. Midgett*,<sup>97</sup> the Arizona Supreme Court declared section 580b without effect in an Arizona court, even when the initial purchase-money transaction was between California residents, governed by California law, and dealt with California property.<sup>98</sup> The court reasoned in strict accordance with vested rights precedents.<sup>99</sup> The more recent California case of *Yunker v. Reseda Manor* may well support this approach.<sup>100</sup> In *Yunker*, the court seemed to treat section 580b as a California domestic remedy which could be applied to a Nevada purchase-money transaction, ignoring the involvement of Nevada law in the initial transaction.<sup>101</sup> Moreover, *Martin's* characterization of section

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95. 5 Cal. 2d 214, 53 P.2d 958 (1936).

96. See *supra* notes 72-77 and accompanying text.

97. 100 Ariz. 284, 413 P.2d 754 (1966).

98. The court in *Martin*, citing *Commercial Nat'l Bank v. Catron*, 50 F.2d 1023 (10th Cir. 1931) and *Maxwell v. Ricks*, 294 F. 255 (9th Cir. 1923), stated that "§§ 580b and 729 [sic] are procedural only and do not bar plaintiff from recovery in this action filed in the . . . State of Arizona." *Martin*, 100 Ariz. at 288, 413 P.2d at 757. Alternatively, the court reasoned that § 580b should not bar an action since the original purchase-money note had been subordinated after the initial transaction. *Id.* at 287, 413 P.2d at 756-57.

99. "The contract which formed the basis for the action was executed in California, and at the time the action was filed both parties were residents of California." *Martin*, 100 Ariz. at 285, 413 P.2d at 755.

100. 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967).

101. See *supra* notes 80-85 and accompanying text.

580b as procedural has found a place in California case law. In *Kerivan v. Title Insurance & Trust Co.*,<sup>102</sup> the appellate court cited *Martin* with approval in treating sections 580b and 580d analogously—either could be ignored in a foreign forum.<sup>103</sup> Whether section 580b legitimately can be avoided by resort to a foreign forum can be answered by application of governmental interest analysis.<sup>104</sup>

### 3. California Property: Section 580d and Fair-Value Avoidance

Conflict of laws issues concerning the avoidance of section 580d were implicated in *Kerivan v. Title Insurance & Trust Co.*,<sup>105</sup> a California case arising out of a controversy originally litigated in Colorado.<sup>106</sup> In *Kerivan*,<sup>107</sup> the promissory note was governed by Colorado law,<sup>108</sup> but the note was secured by California real property and the security instrument was governed by California law.<sup>109</sup> The creditor foreclosed nonjudicially in California, and later obtained a deficiency judgment in Colorado.

The court in *Kerivan* indicated that section 580d could not bar the Colorado deficiency action, since Colorado law governed the promissory note.<sup>110</sup> The court reached its conclusion by relying on vested rights precedents,<sup>111</sup> endorsing the vested-rights concept that “[t]he remedial

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102. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

103. *Id.* at 231, 195 Cal. Rptr. at 57. *Martin* is also cited with approval in *United Bank v. K & W Trucking Co.*, 147 Cal. App. 3d 217, 224, 195 Cal. Rptr. 49, 53 (1983), the companion case to *Kerivan*.

104. Since a foreign court might disregard the effect of § 580b because of its own conflict of laws methodology, the extraterritorial effect of § 580b identified in governmental interest analysis could play no role. In such a case, an action for declaratory relief in California would constitute the only circumstance in which government interest analysis could focus squarely on the avoidance issue. *See supra* note 62.

105. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

106. *See United Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), *cert. denied*, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*). In the Colorado case, the creditor obtained a deficiency judgment following a nonjudicial foreclosure in California. The court disregarded the effect of § 580d by relying on the RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 comment e (1971). *See infra* text accompanying notes 295-306.

107. In *Kerivan*, the debtor brought an action against the California title company for negligence in releasing the uncanceled note to the creditor subsequent to the nonjudicial foreclosure in California. *See infra* note 286.

108. *Kerivan*, 147 Cal. App. 3d at 228 n.1, 195 Cal. Rptr. at 55 n.1.

109. *Id.*

110. The court in *Kerivan* stated:

[W]e conclude that the trustee under a deed of trust has a duty to cancel the note following a non-judicial foreclosure in this state, whenever the laws of this state are applicable to the transaction, but need not cancel the note when the beneficiary may seek a deficiency judgment in a jurisdiction other than ours.

*Kerivan*, 147 Cal. App. 3d at 231, 195 Cal. Rptr. at 57.

111. The *Kerivan* court cited *Martin v. Midgett*, 100 Ariz. 284, 413 P.2d 754 (1966), *see infra*

measure in one state [i.e., section 580d in California] would not prevent a recovery of the deficiency in another state."<sup>112</sup> Such avoidance of section 580d by a foreign choice-of-law provision in the promissory note should be reconsidered in light of interest analysis to develop a policy-based rule governing the effect of section 580d in multistate contexts.

#### 4. *California Property: Fair-Value Avoidance*

No court yet has addressed directly the avoidance of the fair-value statutes by either resort to a foreign forum or by contracting for foreign law. However, the debtor-protection policies underlying the fair-value provisions are necessarily implicated in cases involving section 580d avoidance.<sup>113</sup> Consequently, issues relating to fair-value avoidance can be included in the analysis of section 580d avoidance.

### III

#### GOVERNMENTAL INTEREST ANALYSIS APPLIED

The two cases on which this Comment focuses special attention, *Hersch & Co. v. C & W Manhattan Associates*<sup>114</sup> and *Kerivan v. Title Insurance & Trust Co.*,<sup>115</sup> present the two principal contexts in which modern conflicts issues arise. *Hersch* represents the foreign-security paradigm in which the promissory note is governed by California law but secured by foreign property.<sup>116</sup> The foreclosure remedies are governed

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notes 97-99 and accompanying text, and *Bayside-Flushing Gardens, Inc. v. Beuermann*, 36 F. Supp. 706 (D.D.C. 1941).

112. *Kerivan*, 147 Cal. App. 3d at 231, 195 Cal. Rptr. at 57.

113. Section 580a played a role in the enactment of § 580d. See *infra* text accompanying notes 245-58.

114. 700 F.2d 476 (9th Cir. 1982).

115. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

116. In *Hersch*, foreign property was purchased in accordance with "agreements" requiring the application of California law. *Hersch*, 700 F.2d at 478. The promissory notes, evidently separate from the "agreements," were secured by mortgages and deeds of trust. *Id.* at 477. For purposes of this Comment, the *Hersch* paradigm assumes that the promissory note, or any other instrument evidencing the debt, is expressly or impliedly governed by California law. In the actual *Hersch* case, the debtor initially sued to rescind the property-purchase transaction and the creditor counter-claimed for unpaid principal and interest. *Id.* at 478. This Comment focuses on actions on the note for the amount of the debt. Actions for principal and interest due, like any action other than foreclosure, can be disallowed by the debtor who claims the § 726 affirmative defense in domestic California contexts.

The *Hersch* court relied on *Felton v. West*, 102 Cal. 266, 36 P. 676 (1894), to disallow the affirmative defense, stating: "Hersch also argues that California Code of Civil Procedure § 726, which requires one form of action to recover any debt or enforcement of any right secured by a mortgage or trust deed, bars C & W's counterclaims. Section 726, however, is limited in its effect to property located in California." *Hersch*, 700 F.2d at 478 n.3. In fact, *Felton* was not on point, since it rejected only the applicability of the one-action sanction, not the affirmative defense. In contrast, *Hersch* involved only the issue of the affirmative defense, not the one-action sanction. The court in *Felton*, in dictum, supported the applicability of the affirmative defense in the foreign-security context. See *supra* notes 69-70. The court in *Hersch* did not apply governmental interest analysis.

by the security-situs state.<sup>117</sup> *Kerivan*, conversely, represents the California-security paradigm in which California law governs foreclosure remedies while foreign law governs the promissory note.<sup>118</sup>

In the *Hersch* paradigm, where California law governs the promissory note, it is necessary to resolve the conflicts issue by examining California's governmental interest in applying the antideficiency statutes to any California promissory note, regardless of the security-situs law governing the foreclosure remedy. In the *Kerivan* paradigm, where foreign law governs the note,<sup>119</sup> the analysis evaluates whether California has a governmental interest in applying any of the antideficiency statutes, regardless of the *foreign* law governing the note. Section *A* below will examine seriatim the application of the antideficiency statutes in the context of the *Hersch* paradigm. Section *B* will examine the application of the antideficiency statutes in the *Kerivan* paradigm.

*A. The Hersch Paradigm: Extension of the Antideficiency Statutes to Foreign-Security Transactions*

*1. Section 726*

This discussion employs the following hypothetical based on *Hersch*. The debtor is a California domiciliary or other person with California connections<sup>120</sup> who borrows money in a California transaction and offers as security real property located in New Mexico.<sup>121</sup> The creditor, also a

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117. Under traditional conflicts methodologies, the local law of the property situs in secured transactions governs all aspects of the mechanical foreclosure procedures, e.g., notice period, reinstatement rights, and issues affecting title, (redeemable or nonredeemable), whether or not a security agreement expressly calls for the application of local law. See, e.g., RESTATEMENT OF CONFLICT OF LAWS §§ 227-28 (1934); RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 (1971).

118. See *infra* note 286.

119. In *Kerivan*, the promissory note was expressly governed by California law. 147 Cal. App. 3d at 228 n.1, 195 Cal. Rptr. at 55 n.1.

120. This Comment proposes solutions for prototypical transactions governed by California law: the parties are California domiciliaries, the parties contract in California for performance in California, or the parties expressly contract for California law. In such circumstances, California's governmental interest in applying §§ 726 and 580b legitimately would extend to the parties. In cases in which the parties have fewer connections with California, interest analysis will focus on questions of fairness to the parties and respect for the justified contract expectations of the parties. See *infra* note 155.

Two further issues will arise which are beyond the scope of this inquiry. First, in a foreign-security transaction involving a California domiciliary debtor and a promissory note governed by California law, should California's public policy against prospective waiver of the protection of §§ 726 and 580b be measured by a different standard than in California-security transactions? Second, should an entirely foreign lending transaction involving foreign security, but in which a California choice-of-law provision was made, support only a mitigated California governmental interest in giving effect to §§ 726 or 580b?

121. In *Hersch*, the creditor took security interests in both New Mexico and Iowa real property. For purposes of illustration, the hypothetical in this section will focus only on the New Mexico security interest. New Mexico has no security-first or election of remedies statute. Iowa has a type

California domiciliary, expressly agrees that the promissory note be governed by California law. Further, the debtor and creditor expressly agree that the law of the security situs, New Mexico, governs the security instrument, and hence the foreclosure remedy. Additionally, the note is not purchase-money. After default, the creditor brings an action on the note in a California forum. The debtor claims that section 726 is integrated into the promissory note and that the affirmative defense should be allowed in order to compel foreclosure of the security first. In response, the creditor claims that the law of the security situs should control, and argues that New Mexico law does not require foreclosure first.<sup>122</sup> The relevant inquiry under interest analysis is whether California has a governmental interest in giving effect to section 726 by allowing the affirmative defense.<sup>123</sup>

As a first step, the policies underlying section 726 must be identified through construction and interpretation of the statute. It then must be determined if the identified policies would be advanced by the statute's application to the particular circumstances of the case. A comparable inquiry is required with respect to New Mexico's policies and interests.

#### *a. California: Policy Identification and Policy Advancement*

*i. Policy identification through construction/interpretation.* Section 726 typically is considered to promote a security-first policy requiring a creditor to foreclose the real-property security before being allowed a deficiency judgment.<sup>124</sup> A careful review of the case law addressing section 726, however, reveals two policies at work in the notion of "security-first:" the single-action policy and the primary-fund policy. The objective of the single-action policy is to eliminate the burden on the debtor when multiple actions are pursued under the common law.<sup>125</sup> Prior to

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of security-first statute which would imply a false conflict between California and Iowa policies. See *infra* note 122.

122. At least eleven states other than California have a form of single-action statute. If the issues within the *Hersch* foreign-security paradigm involved one of these states, it is probable that no policy conflict would exist. The statutes are GA. CODE ANN. § 67-1503 (1980); IDAHO CODE § 45-1512 (1977); IOWA CODE § 615.3 (1950); KAN. STAT. ANN. § 60-2403 (Supp. 1984); MASS. GEN. LAWS ANN. ch. 244, § 17A (West 1959); NEV. REV. STAT. § 40.455 (1983); N.J. REV. STAT. § 2A:50-2 (Supp. 1985); N.Y. REAL PROP. ACTS. LAW § 1371 (McKinney 1979); N.C. GEN. STAT. § 1-54(6) (1983); N.D. CENT. CODE § 32-19-06 (1976); OHIO REV. CODE ANN. § 2329.08 (Page Supp. 1984).

123. See *supra* text accompanying notes 51-52.

124. See generally, R. BERNHARDT, *supra* note 71, § 4.4, at 141-43; J. HETLAND, SECURED REAL ESTATE TRANSACTIONS §§ 9.4-.5 (1974).

125. See, e.g., *Toby v. Oregon Pac. R.R.*, 98 Cal. 490, 494-95, 33 P. 550, 551 (1893); *Ould v. Stoddard*, 54 Cal. 613, 615 (1880).

The creditor may nevertheless maintain multiple piecemeal *nonjudicial* foreclosure actions on primary-fund security interests without violating the single-action policy. See *Hatch v. Security-First Nat'l Bank*, 19 Cal. 2d 254, 120 P.2d 869 (1942). But *nonjudicial* actions on *nonprimary-fund*

the enactment of section 726, a creditor could first bring an action at law on the note, then bring an action in equity to foreclose the security interest. The result was a double burden on the debtor. Section 726 both permitted and required that a creditor obtain all relief—foreclosure relief and a deficiency judgment—in a single *judicial* action. The original single-action policy underlying section 726, dating from 1860,<sup>126</sup> gained additional importance after the enactment in 1939 of section 580d.<sup>127</sup> Since section 580d was intended to prevent a creditor from obtaining nonredeemable title and a deficiency judgment,<sup>128</sup> it is essential that section 726 operate, through the single-action policy, to confine the creditor to a single *judicial* action. Without section 726, the creditor theoretically could obtain a first judgment on the note, and then foreclose *nonjudicially*, resulting in a de facto deficiency judgment and nonredeemable title. Section 580d policies reject such an outcome.

The related primary-fund policy<sup>129</sup> requires that on default the creditor resort first to the secured real property—the primary fund—before obtaining a money judgment which could be used to reach the debtor's general assets.<sup>130</sup> The policy objective here is to prevent the creditor from obtaining recourse to the debtor's general or nonprimary-fund assets, while still retaining the mortgage lien. A debtor could be severely burdened by such successive actions. Under the traditional common law practice, for example, the creditor could reduce an action at law on the note to final judgment, and thereafter lien and execute on the debtor's nonprimary-fund assets to partially satisfy the debt. Meanwhile, the original mortgage would remain valid, with the consequence that the all the debtor's assets would be frozen by the creditor's liens. The debtor

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assets have been held to violate § 726, and the one-action sanction has been imposed. *Bank of Am. v. Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984). See *infra* note 134.

126. See California Civil Practice Act § 246 (1880).

127. See *infra* text accompanying notes 235-58.

128. See J. HETLAND, *supra* note 124, § 9.16, at 198-99.

129. See *Merced Sec. Sav. Bank v. Casaccia*, 103 Cal. 641, 644, 37 P. 648, 649 (1894). "The obvious purpose of the statute [§ 726] is to compel one who has taken a special lien to secure his debt to exhaust his security before having recourse to the general assets of the debtor." *Id.* at 644, 37 P. at 649. The requirement that a debtor exhaust his security before having recourse to the debtor's general (nonprimary-fund) assets has been routinely noted as the primary-fund purpose of § 726. See, e.g., *Toby v. Oregon Pac. R.R.*, 98 Cal. 490, 495, 33 P. 550, 551 (1893) ("to make the mortgaged property the primary fund"); *Porter v. Muller*, 65 Cal. 512, 513, 4 P. 531, 531 (1884) ("the mortgaged premises constituted the primary fund . . ."). But cf. Comment, *Mortgages and Trust Deeds: Enforcement of a Secured Debt in California*, 31 CALIF. L. REV. 429, 430-31 (1943). The Comment argues that "[m]uch of the confusion [concerning § 726] may be ascribed to the failure . . . to distinguish between the purpose of the statutory 'one action' rule and its effect . . . . The sole intention of the legislature was to . . . prevent [a] . . . multiplicity of actions . . . . The effect . . . was to make the mortgage a primary fund . . . ." *Id.* (emphasis in original) (footnote omitted).

130. Case law does not make clear what event would trigger the one-action sanction for a violation of the primary-fund policy. It could be either encumbering the nonprimary-fund assets by judgment lien or executing on the nonprimary-fund assets. See *infra* note 134.

would be deprived of any ability to realize the credit potential in his non-primary-fund assets, thus hampering his ability to correct or defend the default. The primary-fund policy, therefore, forbids access to nonprimary-fund assets in advance of a single *judicial* action in which all relief might be legitimately obtained.<sup>131</sup>

The legislative objectives of the single-action and primary-fund policies are implemented by either of two judicially created enforcement mechanisms, the affirmative defense and the one-action sanction. If the creditor brings an action on the note, the first step in attempting to realize on nonprimary-fund assets, the debtor may plead the existence of real-property security. This forces the creditor to exhaust the primary fund first through foreclosure.<sup>132</sup> Second, the debtor may stand by and allow the creditor to obtain a final money judgment on the note, without foreclosing the security interest. In this case the court may impose the one-action sanction, which voids the security interest in the real property.<sup>133</sup> Both mechanisms implement the goals of the primary-fund policy and simultaneously give effect to the single-action policy.<sup>134</sup> The

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131. See J. HETLAND, *supra* note 124, § 9.16, at 198-99.

132. See, e.g., *Barbieri v. Ramelli*, 84 Cal. 154, 23 P. 1086 (1890).

133. See, e.g., *Salter v. Ulrich*, 22 Cal. 2d 263, 138 P.2d 7 (1943).

134. In domestic-security cases, courts typically have found it unnecessary to distinguish between the proscribed effects within the single-action and primary-fund policy framework when imposing the one-action sanction. Indeed, most sanction cases refer only to the single-action policy aspect of § 726. However, this Comment argues that the primary-fund policy objective—avoidance of a debtor's lien or execution on nonprimary-fund assets—remains vital. See *supra* text accompanying notes 129-31.

The reason that the single-action policy violation overshadows the primary-fund policy violation in domestic contexts can be seen in *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974). In *Walker*, the creditor did not foreclose all interests in multiple securities (real and personal property) in a first judicial action. The court imposed the one-action sanction, voiding the remaining security interests at the completion of the first action, focusing only on the single-action policy. The primary-fund policy, however, could still have been implicated. In the *Walker* fact pattern, the violation of the primary-fund policy—recourse to the nonprimary-fund assets—may be involved if the creditor uses his final judgment to encumber or execute on previously nonprimary-fund assets instead of first ordering a sale of the primary-fund property. Two arguments apply in this situation. First, the very purpose of the judicial action is to obtain legitimately a final judgment, thereby gaining recourse to the debtor's nonprimary-fund assets. It is therefore logical to argue that the primary-fund policy objectives are fully attained when the creditor is prevented from encumbering or executing on the debtor's nonprimary-fund assets *before the completion of the judicial action for all relief*. This line of reasoning would support the apparent original legislative design of altering the harsh effects of the common law concerning concurrent or successive actions.

Second, however, it could be argued that although the creditor did not violate the single-action policy, he would still violate the primary-fund policy in the postjudgment period if he encumbered or executed on nonprimary-fund assets before selling the primary-fund assets. To implement such a rule, the affirmative defense again might be allowed to prevent encumbering or execution on the nonprimary-fund assets. The one-action sanction could be imposed if the creditor actually encumbered or executed on the nonprimary-fund assets. The policies which might support this argument cannot be derived from the apparent legislative intent of correcting inequities in the common law, since that intent would be confined to the prejudgment period.

Nevertheless, in *In re Kristal*, 37 Bankr. 659 (Bankr. 9th Cir. 1984), the Bankruptcy Appellate

affirmative defense requires that the creditor seek all relief in a single judicial action. The one-action sanction, imposed *following* a judicial action in which all relief was not sought, confines the creditor to whatever relief was obtained in the original action.

These two enforcement mechanisms have been applied consistently by the courts, and their continued use reflects the current vitality of the single-action and primary-fund policies underlying section 726.<sup>135</sup> The

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Panel of the Ninth Circuit, per Bankruptcy Judge Ashland, extended the one-action sanction to postjudgment execution on nonprimary-fund assets in the fact pattern just outlined. In *Kristal*, the creditor foreclosed all interests in multiple security in a single judicial action. The creditor used the judgment to execute on the debtor's general assets, apparently before ordering a sale of the primary-fund assets. The original primary-fund property also was sold pursuant to a writ of execution. Bankruptcy Judge Ashland agreed with the bankruptcy court that the creditor had violated § 726 by his "acts to reach the propert[ies] of the debtor that were not security for the debt. . . . [T]he money judgment and execution on property that was not collateral for the loan had the . . . effect of subjecting the debtor to personal liability before exhausting all security, thus, violating C.C.P. § 726." *Id.* at 662-63. Bankruptcy Judge Ashland, in part, supported the holding of a primary-fund policy violation by focusing on the fair-value requirements of § 726(b). "[The creditor] should have applied to the court any time within three months of the date of the foreclosure sale . . . for a fair value hearing. . . . [The creditor's] nonfeasance caused it to violate C.C.P. § 726." *Id.* at 663. Since the objective of the fair-value hearing is to reduce the amount of remaining indebtedness by the appraised value of the property rather than the bid price, that policy objective might have been attained simply by requiring an appraisal of the primary-fund property, when and if it were sold.

Bankruptcy Judge Ashland's reasoning in *Kristal* was reflected in his later decision, *In re Rivers*, 39 Bankr. 608 (Bankr. C.D. Cal. 1984), *rev'd*, No. CV84-4544-RMT (C.D. Cal. Sept. 27, 1984) (order reversing and remanding on file with the *California Law Review*). In *Rivers*, Judge Ashland imposed the one-action sanction after the first of a planned series of piecemeal *nonjudicial* sales of multiple security interests. The judge reasoned, as in *Kristal*, that the one-action sanction was justified since the creditor had failed to "apply for a fair value hearing within three months of the date of the [first] foreclosure sale. . . ." *Id.* at 609. *Rivers* contradicted the California Supreme Court's holding in *Hatch v. Security-First Nat'l Bank*, 19 Cal. 2d 254, 120 P.2d 869 (1942), where piecemeal *nonjudicial* foreclosures of multiple security interests were allowed without a requirement of intermediate fair-value hearings under §§ 726 or 580a. Judge Ashland's holding in *Rivers* was reversed and remanded by order, although *Hatch* was not cited. Since Judge Ashland's decisions to impose the one-action sanction in *Kristal* and in *Rivers* were based principally on noncompliance with the fair-value mechanics, the reversal of *Rivers* should weaken the holding in *Kristal*, where the one-action sanction was extended to postjudgment executions on nonprimary-fund assets in advance of foreclosure and appraisal of primary-fund assets. Neither case implicated the single-action policy. In *Kristal*, the creditor obtained all relief in a single judicial action. In *Rivers*, the single-action policy did not apply to the *nonjudicial* foreclosure procedure.

In domestic cases in which an initial *judicial* action has not yet taken place so there is no violation of the single-action policy, the one-action sanction may yet be imposed for a violation of the primary-fund policy, at least when actual recourse is made to the nonprimary-fund assets. See *Bank of Am. v. Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984). In *Daily*, the one-action sanction was imposed after the bank partially reduced a secured debt in default by setting off the debtor's nonprimary-fund bank account. Since no judicial action allowing foreclosure and deficiency relief had been completed, the single-action policy had not been violated.

135. The California Supreme Court, in *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978), stated that an evaluation of the current strength or vitality of a state's law is a test within the comparative impairment framework. "[T]he current status of a statute is an important factor to be considered in a determination of comparative impairment: the policy underlying a jurisdiction's law may be deemed 'attenuated and anachronistic and properly . . . be limited to domestic occurrences in the event of [a multistate] clash of interests.'"

affirmative defense mechanism appeared at least as early as 1883 in *Bartlett v. Cottle*,<sup>136</sup> and the one-action sanction was imposed as early as 1863, in *Ladd v. Ruggles*.<sup>137</sup> Both the affirmative defense and the one-action sanction have been reaffirmed as enforcement devices as recently as 1974 by the California Supreme Court.<sup>138</sup> This indicates that the policies underlying section 726 which are implemented through these two enforcement mechanisms remain intact. The next step is to determine whether these identified policies would be advanced if applied to the facts of the *Hersch* paradigm.

ii. *Policy advancement in the Hersch multistate context.* The foregoing discussion provides guidance in understanding the policies underlying section 726 in domestic contexts. The pertinent question remains whether these policies are advanced in cases involving foreign security. It is reasonably certain that the drafters of section 726 assumed that the foreclosure proceeding would occur in California. It could be argued that the existence of California security should be a condition precedent to assertion of section 726 protection. On the other hand, it could be argued that the provision is designed exclusively to affect debtor-creditor relationships within the state and that therefore situs of the property is not relevant. The answer depends on whether section 726 is conceived of as a *land-related* issue, thus limited to cases in which a California foreclosure occurs, or whether the provision is a *debtor-creditor related* issue, not limited to cases involving a California foreclosure.

The principal argument that section 726 is *land-related*, that is, an integral part of a California foreclosure remedy, is that section 726 becomes effective only *after* the debtor has defaulted. It is at this time the creditor proceeds, either in a judicial foreclosure action, or in an action on the note, which the debtor could disallow by asserting the affirmative defense.<sup>139</sup> One can argue, therefore, that section 726 is part of the comprehensive regulation of the post-default stage of a *California foreclosure remedy*, and that this presupposes that the entire range of internal remedial procedures—the rules governing notice,<sup>140</sup> reinstatement,<sup>141</sup> regulations on sale,<sup>142</sup> and the section 726 provisions—must transpire within the context of a California foreclosure. Under this the-

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*Id.* at 166, 583 P.2d at 726, 148 Cal. Rptr. at 872 (quoting Freund, *Chief Justice Stone and the Conflict of Laws*, 59 HARV. L. REV. 1210, 1224 (1946)).

136. 63 Cal. 366 (1883).

137. 23 Cal. 232 (1863).

138. *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 11 Cal. Rptr. 897 (1974).

139. The debtor has the option of waiting until after a final judgment has been rendered in the action on the note, and then pleading the one-action sanction.

140. CAL. CIV. CODE §§ 2924, 2924b (West Supp. 1985).

141. *Id.* § 2924c.

142. *Id.* §§ 2924d, 2924g, 2924h.

ory, the debtor might not be allowed to separate the section 726 protections from the *land-related* moorings and assert them in a foreign-security context.

This argument, however, considers context but ignores consequences. Section 726 was intended specifically to implement two policy objectives—the prevention of multiple actions and the prevention of an encumbrance or an execution on nonprimary-fund assets. These objectives are not *land-related*.

First, consider the primary-fund policy objective in the *Hersch* foreign-security paradigm. If a creditor in a foreign-security situation is permitted to obtain a personal money judgment on the note in California while continuing to hold the security interest in the foreign property, he will, in effect, lock up the debtor's nonprimary-fund assets while retaining the mortgage lien on the primary-fund assets. This is the exact outcome rejected by the primary-fund policy. True, the liens on both primary-fund and nonprimary-fund assets stretch across California borders. But the effects on the debtor are, nonetheless, identical to the effects if there were California security. Hence, the precise policy objectives which underlie section 726 in its domestic context are implicated in the *Hersch* foreign-security paradigm, namely, the prevention of a creditor's potentially devastating ability to encumber or execute on the debtor's nonprimary-fund assets in advance of foreclosure. The policies identified are not *land-related*, but are modifications of common law procedures, that is, *debtor-creditor related*. It follows, therefore, that California has a strong governmental interest in applying section 726 to implement the primary-fund policy objectives in the *Hersch* foreign-security paradigm.

The single-action policy objective enforced by the one-action sanction, however, is less amenable to extraterritorial application. Here the goal is to confine foreclosure and deficiency relief to a single judicial action. In the *Hersch* paradigm, the foreclosure remedy must necessarily take place in the foreign state due to the situs of the security. Therefore, the *only* single action in which the creditor could obtain both foreclosure and deficiency relief would be a foreign judicial action.

Insofar as the creditor is able to obtain personal jurisdiction over the debtor in the initial foreign action, the single-action policy should operate. That is, the creditor should be required to obtain foreclosure and deficiency relief in the first judicial action. However, the foreign court may not have personal jurisdiction over the debtor and/or the debtor may refuse jurisdictional consent. In this context, the creditor could not be sanctioned justifiably for bringing a second action in California for the deficiency. Unlike the California-security example, the *Hersch* foreign-security paradigm may not necessarily conform to the dictates of the sin-

gle-action policy. Consequently, determining whether the discrete single-action policy objective can be advanced will depend on case-by-case inquiry into jurisdictional requirements. Two actions may be required for the creditor to obtain both foreclosure and deficiency relief.<sup>143</sup> Thus, of the two policies, only the primary-fund necessarily is advanced by application of section 726 to the *Hersch* facts.

It could also be argued that extension of the affirmative defense to the foreign-security context is unnecessary to protect the debtor from the burden of encumbrances on both primary-fund and nonprimary-fund property, since the debtor would be protected by the one-action sanction. If a debtor fails to plead the affirmative defense in the initial action on the note, he still can avoid the burden of encumbrances on both primary-fund and nonprimary-fund assets by pleading the one-action sanction in any attempted foreclosure action following the award of a money judgment. The affirmative defense, under this line of reasoning, might simply assure that California courts will not have to confront the issue more than once.<sup>144</sup> However, as noted,<sup>145</sup> the affirmative defense gives the debtor the power to ensure that the creditor can not encumber nonprimary-fund assets while retaining the mortgage lien. The affirmative defense is required to afford the debtor the full discretion to prevent a violation of the primary-fund policy objective. This policy objective is advanced equally in foreign-security and California-security contexts.

The policy objectives underlying section 726 relate exclusively to a redefinition of the common law procedures, that is, a redefinition of *debtor-creditor* rights. It therefore must be considered that those policy objectives are integrated into the contract concerning the debt, which is governed by California law. The fact that the law of the situs governs the foreclosure method is not incompatible with the section 726 policy objectives. Simply stated, once section 726 dictates that a foreclosure is required instead of an action on the note, the situs state's law should govern all elements relating to land title and the method of foreclosure of the security interest. Since California's policy objectives would be advanced in the *Hersch* paradigm, California would have a legitimate, real<sup>146</sup> governmental interest in extending the operation of section 726 to

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143. Supporting this view, the court in *Felton v. West*, 102 Cal. 266, 36 P. 676 (1894), recognized that the single-action policy underlying § 726 could not be enforced justifiably in a foreign-security case. "[O]ne action, either in Oregon or California, could not be made sufficient to secure all of [the creditor's] rights." *Id.* at 270, 36 P. at 677. See *supra* notes 68-71.

144. While an *effect* of § 726 might be to conserve judicial resources, no case law has viewed the single-action policy as founded, even in part, on a legislative intent to protect judicial resources.

145. See *supra* text accompanying notes 131-38.

146. Professor Sedler defined a real governmental interest as follows:

[A] state has a real interest when "the reasons or governmental interests behind the state's policy are such that the state has a logical, rational, legitimate cause to apply its policy to the case in question . . . because the local elements of the case—the parties, the subject

foreign-property secured transactions in any case in which California law governed the promissory note.

*b. New Mexico: Policy Identification and Policy Advancement*

*i. Policy identification through construction/interpretation.* Since the foreclosure remedies are expressly (or impliedly) governed by the situs state, the creditor could plead that the conflicting law of New Mexico should be applied. New Mexico has not adopted a security-first statute.<sup>147</sup> Two reasons for allowing successive actions in New Mexico might be identified. First, it is possible that New Mexico has maintained the common law status quo simply through inertia, not through any significant policy. On the other hand, it is possible that New Mexico has a deliberate policy of favoring a creditor's right to maintain successive actions. Assuming that New Mexico's internal legislative scheme allows successive actions—for either reason mentioned—the next question is whether New Mexico's internal policy would be advanced in the *Hersch* paradigm, so as to give rise to a New Mexico governmental interest in allowing the creditor an action on the note.

*ii. Policy advancement in the Hersch multistate context.* In the *Hersch* paradigm, the creditor is assumed to be a California domiciliary or other party transacting business in California, and further, the parties agreed that California law would govern the promissory note, allowing New Mexico law to govern only the foreclosure method. Several factors suggest that New Mexico would have no interest in extending its procreditor policy to such a multistate context. First, New Mexico's procreditor policy, strong or weak, presumably is intended to benefit domiciliary creditors, creditors transacting business in New Mexico or, at a minimum, those parties who contracted for New Mexico law to govern the promissory note. In fact, in the *Hersch* paradigm, since New Mexico's law does not govern the promissory note, New Mexico, like California, should have a policy interest in the enforcement of contracts according to the justified expectations of the parties.<sup>148</sup> The debtor might

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matter, the transaction . . . bear a rational relationship to the reasons and interests behind the policy of the state."

Sedler, *supra* note 44, at 223 (quoting Kramer, *Interests and Policy Clashes in Conflict of Laws*, 13 RUTGERS L. REV. 523, 532 (1959)). The California Supreme Court has cited Sedler's conceptualization of real interests in its application of governmental interest analysis. *See, e.g., Bernhard v. Harrah's Club*, 16 Cal. 3d 313, 320, 546 P.2d 719, 723, 128 Cal. Rptr. 215, 219 ("This process of reexamination requires identification of a 'real interest . . .'" (citing Sedler, *Symposium, Conflict of Laws Roundtable, Value of Principled Preferences*, 49 TEX. L. REV. 211, 224 (1971))), *cert. denied*, 429 U.S. 859 (1976), *overruled on other grounds, Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984).

147. *See* N.M. STAT. ANN. §§ 39-5-18, -21, 48-7-7 (1983).

148. *See, e.g.,* RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(2)(d) (1971), concerning the protection of justified expectations of the parties. Even if New Mexico's internal policy could be

reasonably have relied on California's protective policy, since California law governed the promissory note.<sup>149</sup>

New Mexico should not consider its procreeitor policy to be implicated simply because the foreclosure remedies are governed by its law. It was argued above that section 726 modified the common law rights of the creditor, and is thus only collateral to the foreclosure remedies governed by the property-situs state. The application of section 726 does not affect New Mexico's policies regarding property title and foreclosure method. Rather, it simply would empower the debtor to prevent an action on the note. Consequently, under interest analysis, New Mexico would not have a governmental interest in affording the right to successive actions to a creditor taking a security interest in the state's property when the promissory note was governed by California law. Because the foreign state could identify no governmental interest in applying its law in the *Hersch* paradigm, a false conflict would exist. Accordingly, California's legitimate governmental interest in applying section 726 should be respected.<sup>150</sup>

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described as procreeitor, it would be untenable to argue that it was intended specifically to burden debtors who owned and hypothecated New Mexico property without regard to the foreign domiciles of the parties or the parties' agreement that foreign law governed the debt. It should not be against New Mexico's public policy for a debtor to obtain by contract greater protection than that offered by the common law.

149. In *Wong v. Tenneco, Inc.*, 151 Cal. App. 3d 376, 198 Cal. Rptr. 526 (1984), a California court, applying governmental interest analysis to a contract dispute implicating both California and Mexico law, considered that California has a general policy supporting contract enforcement, citing in support, CAL. CIV. CODE § 3300 (West 1974), which deals with contract damages. "California's general polic[y] of affording relief to breach of contract . . . victims . . . give[s] it a strong interest in application of its law." 151 Cal. App. 3d at 383, 198 Cal. Rptr. at 530 (citing § 3300).

150. In antideficiency conflicts cases, a foreign state's policy toward deficiency issues might be controlled not only by internally directed policies, but also by the dictates of its conflicts methodology for dealing with separate promissory notes and security agreements. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 5 comment a (1971), states: "Conflict of Laws rules, when adopted, become as definitely a part of the law as any other branch of the state's law."

For example, in *Union Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), cert. denied, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*), the Colorado court derived its rule of law concerning a separate promissory note governed by Colorado law and a security agreement governed by Colorado law exclusively with reference to RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 comment c (1971). The comment states, in part:

Issues which do not affect any interest in the land, although they do relate to the foreclosure, are determined . . . by the law which governs the debt for which the mortgage was given. Examples of such . . . issues [include] . . . the mortgagee's right . . . to bring suit upon the underlying debt without first having proceeded against the mortgaged land.

In the *Hersch* paradigm, since the promissory note is governed by California law, a state strictly following the black letter rules of the *Restatement (Second)* would defer to California law. A state following the *Restatement (Second)* in such a manner would consider § 726 as a condition to the promissory note, circumscribing the creditor's common law remedies.

At least 14 states rely on the *Restatement (Second)* for their methodology in resolving conflicts. See Kay, *supra* note 44, at 591-92 & 556 n.223.

The conclusion reached through analysis of the *Hersch* paradigm—that California has a governmental interest in giving effect to section 726—is supported by the leading California case involving such facts: *Felton v. West*.<sup>151</sup> In *Felton*, although the security situs was foreign, the debt impliedly was governed by California law: both parties were California residents and the note was executed in California. The court stated that the creditor would not have been allowed to “bring a personal action at law upon the note only, for our courts would not allow him to waive his security.”<sup>152</sup> In *Hersch & Co. v. C & W Manhattan Associates*,<sup>153</sup> the case upon which this paradigm is based, the court’s failure to give effect to the affirmative defense cannot be reconciled with *Felton* or with the conclusion derived from interest analysis.<sup>154</sup>

*c. Application of Section 726 in non-Hersch Context*

In a non-*Hersch* situation, where a promissory note secured by foreign property is expressly or impliedly governed by the foreign state’s law, a California court should allow or disallow the affirmative defense in accordance with the law governing the note. Such a situation could arise if the debtor establishes a California domicile or other connection to California which results in the action being brought in California. Countervailing policies should preclude California from asserting a governmental interest in applying section 726. As this Comment has argued, the security-first right afforded to the debtor derives from a secured loan agreement that is governed by California law. But when a promissory note is made in a foreign state and there are few, if any, pretransaction connections with California, California’s debtor-protection policies could not be said to inhere at the inception of the contract.

In cases involving a California resident conducting business in a foreign state, where the action was brought in a California forum, courts have been willing to defer to the foreign law, concluding that California’s governmental interest was mitigated.<sup>155</sup> In *Offshore Rental Co. v.*

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151. 102 Cal. 266, 36 P. 676 (1894).

152. *Id.* at 269, 36 P. at 677.

153. 700 F.2d 476 (9th Cir. 1982).

154. See *supra* notes 68-69 and accompanying text.

155. In *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978), the California Supreme Court apparently took into account the justified expectations of a party that foreign law would govern a relationship that had little connection to California. In *Offshore*, an employee of a California corporation was injured in Louisiana due to the negligence of a multinational corporation operating in that state. Louisiana law did not allow a cause of action for loss of a key employee’s services, whereas California law might have allowed such an action. The California court, addressing the issue of which party better might have been able to insure against the particular risk, concluded that the multinational corporation operating in Louisiana “would most reasonably have anticipated a need for . . . liability insurance based on Louisiana law.” *Id.* at 169, 583 P.2d at 728, 148 Cal. Rptr. at 874. The court also stated that the party claiming that California law should be applied could “not expect to subject defendant to a financial hazard that

*Continental Oil Co.*<sup>156</sup>, the court took notice that the California resident "plaintiff 'exposed [it]self to the risks of the [foreign] territory . . .'"<sup>157</sup> and could not reasonably expect that a Louisiana corporation doing business in Louisiana would be subject to California law. The court favored the foreign state's policies toward the point in issue over California's mitigated interest in protecting a California resident operating a business out of state. Similarly, in *Reich v. Purcell*,<sup>158</sup> the court declined to apply California law where a wrongful death plaintiff had made an after-the-fact change in residency from Ohio to California.<sup>159</sup> In such cases, when the initial transaction, event, or relationship giving rise to a controversy is entirely governed by foreign state's policies, California courts have considered California policies mitigated.

Accordingly, in cases where the foreign-property secured note is governed by the law of a state which has a prodeficiency policy more favorable to the creditor than the California scheme, the foreign state will identify a governmental interest in affording the creditor the advantages of its law. On the other hand, California would likely identify only a mitigated interest in giving effect to section 726. In such a case, a California court should apply the foreign law.

This conclusion is supported by *First-Trust Joint Stock Land Bank v. Meredith*,<sup>160</sup> the supreme court's most recent review of a conflict of laws case dealing with section 726.<sup>161</sup> In *Meredith*, the note, secured by Iowa property, was impliedly governed by Iowa law, since the parties

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Louisiana law had not created." *Id.* The *Offshore* court appears to have relied on a notion similar to that of respecting the justified expectations of the parties. This treatment parallels § 6(2) of RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971) ("[T]he factors relevant to the choice of the applicable rule of law include . . . (d) the protection of justified expectations . . .").

The *Offshore* holding is also supported by a kind of fairness standard. Professor Sedler stated: As I have emphasized many times, fairness to the parties is an independent choice of law consideration. A state will not—and constitutionally cannot—apply its own law in any situation in which to do so would be fundamentally unfair to the party against whom the law is sought to be applied. If a party could not reasonably be expected to conform . . . to the standards imposed by the law of a particular state, then it would be fundamentally unfair to apply those standards to that party . . . . The application of a state's law to govern . . . a party must have been *foreseeable to a party at the time the party acted*. If interest analysis allowed unpredictable results in the sense that it allowed the application of a state's law to a party who could not have foreseen such application . . . , those results would not only be unsound, they would be unconstitutional.

Sedler, *Interest Analysis and Forum Preference in the Conflict of Laws: A Response to the 'New Critics'*, 34 MERCER L. REV. 593, 611 (1983) (emphasis in original) (footnotes omitted). For the United States Supreme Court's test concerning fairness in conflict of laws cases, see *supra* note 62.

156. 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978).

157. *Id.* at 169, 583 P.2d at 728, 148 Cal. Rptr. at 874.

158. 67 Cal. 2d 551, 432 P. 2d 727, 63 Cal. Rptr. 31 (1967).

159. In *Reich*, the widow of decedent who died in an automobile accident in Missouri brought an action for wrongful death in California against a California resident defendant. The widow and decedent resided in Ohio at the time of the accident.

160. 5 Cal. 2d 214, 53 P.2d 958 (1936).

161. See *supra* note 71 and text accompanying notes 73-77.

were domiciled in Iowa at the time of contracting. The action on the note in a California court apparently resulted from the debtor's change of residence from Iowa to California, followed by the debtor's claim that section 726 should apply. The court in *Meredith* declined to give effect to section 726, stating that "[t]he question whether the [creditor] waived its security is one properly for the courts . . . of Iowa . . . after . . . its action on the note alone in this state."<sup>162</sup> The court in *Meredith* did not elaborate a policy of deferring to foreign law on the basis of fairness<sup>163</sup> to the creditor or respect for the justified expectations of the creditor. On its face, however, the holding indicates that section 726 rights crystallize at the inception of the contract and that they are governed by the law which governs the promissory note.

## 2. Section 580b

The extension of section 580b to purchase-money transactions involving non-California property again can be explored in a hypothetical based on *Hersch*.<sup>164</sup> Assume that a California domiciliary purchases New Mexico real property and the California domiciliary seller carries back a purchase-money mortgage.<sup>165</sup> The promissory note expressly provides for the application of California law. Also, the parties expressly agree in a security instrument that the foreclosure remedies are governed by New Mexico law. After default and a foreign foreclosure, the purchase-money creditor brings an action for a deficiency in California against the debtor.<sup>166</sup> The debtor claims that section 580b bars the deficiency action. The creditor claims that the laws of New Mexico, which offer no purchase-money antideficiency protection, should control.<sup>167</sup>

Under governmental interest analysis, the court first identifies the

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162. *Meredith*, 5 Cal. 2d at 218, 53 P.2d at 959.

163. Fairness to the parties is an independent test within the framework of governmental interest analysis. See *supra* note 155.

164. In the actual case, *Hersch & Co. v. C & W Manhattan Assocs.*, 700 F.2d 476 (9th Cir. 1982), the court relied on *Yunker v. Reseda Manor*, 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967) to resolve the § 580b issue. See *supra* notes 80-85 and accompanying text. Apparently, the debtors conceded that § 580b could be applied extraterritorially. *Hersch*, 700 F.2d at 478 n.2.

165. In the actual *Hersch* case, the seller was a Texas-based limited partnership which owned New Mexico property. In this hypothetical, as in *Hersch*, it is assumed that the seller is not a domiciliary of New Mexico.

166. Since this Comment has argued that the § 726 affirmative defense applies in the *Hersch* foreign-security paradigm, the deficiency action will necessarily occur after the foreign foreclosure.

167. Five other states have purchase-money antideficiency statutes. If the foreign security in the *Hersch* paradigm were located in one of these states, presumably no policy conflict would arise if the seller pleaded the law of such a state conflicted with application of § 580b. See ARIZ. REV. STAT. ANN. § 33-729 (1974); N.C. GEN. STAT. § 45-21.38 (1984); N.D. CENT. CODE § 32-19-07 (1976) (the North Dakota statute is restricted to mortgages executed between July 1, 1937 and July 1, 1951); OR. REV. STAT. ANN. §§ 88.070, .075 (1984); S.D. CODIFIED LAWS ANN. §§ 44-8-20, -22, -25 (1983).

policies underlying section 580b through construction and interpretation of the statute. It next determines whether the underlying policies would be advanced by extending the operation of section 580b to the multistate context, giving rise to a California governmental interest in applying the deficiency bar.<sup>168</sup> After its analysis of California's policies and interests, the court would undertake a similar two-step inquiry into New Mexico's competing policies and interests.

*a. California: Policy Identification and Policy Advancement*

*i. Construction/interpretation of policies underlying section 580b.* Recognizing that early case law merely recited the antideficiency effect of section 580b without providing a policy rationale,<sup>169</sup> Justice Traynor attempted to identify the discrete policy objectives underlying section 580b in two 1963 cases, *Roseleaf Corp. v. Chierighino*<sup>170</sup> and *Bargioni v. Hill*.<sup>171</sup> In *Roseleaf*, the issue was whether section 580b barred a separately secured, sold-out purchase-money lender from an action for a deficiency. In *Bargioni*, the issue was whether section 580b barred third-party lenders of purchase-money from deficiency actions. In a frequently quoted passage in *Roseleaf*, Traynor identified the rationale for section 580b:

Section 580b places the risk of inadequate security on the purchase money mortgagee. A vendor is thus discouraged from overvaluing the security. Precarious land promotion schemes are discouraged . . . . If inadequacy of security results, not from overvaluing, but from a decline in property values during a general or local depression, section 580b prevents the aggravation of the downturn that would result if defaulting purchasers were burdened with large personal liability. Section 580b thus serves as a stabilizing factor in land sales.<sup>172</sup>

In Traynor's view, section 580b applied in two distinct foreclosure situations in which the security is overvalued in relation to the indebtedness: the price-overvaluation context and the depression context. In the first context, Traynor identified a situation in which the land is overvalued at the inception of the transaction, an overvaluation which later results in the buyer's default and an attendant deficiency.<sup>173</sup> In these circumstances, Traynor ascribed to section 580b the policy objective of "discourag[ing] land sales that are unsound because the land is over-

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168. See *supra* text accompanying notes 51-52.

169. See, e.g., *Brown v. Jensen*, 41 Cal. 2d 193, 259 P. 2d 425 (1953); *Mortgage Guarantee Co. v. Sampsell*, 51 Cal. App. 2d 180, 124 P.2d 353 (1942).

170. 59 Cal. 2d 35, 378 P.2d 97, 27 Cal. Rptr. 873 (1963).

171. 59 Cal. 2d 121, 378 P.2d 593, 28 Cal. Rptr. 321 (1963).

172. *Roseleaf*, 59 Cal. 2d at 42, 378 P.2d at 101, 27 Cal. Rptr. at 877.

173. See *supra* text accompanying note 172. The first portion of the *Roseleaf* passage addresses the situation in which price overvaluation induces the deficiency.

valued . . . .”<sup>174</sup> However, Traynor did not elaborate the mechanism by which such “unsound” and “overvalued” land sales transactions might be avoided merely by barring the deficiency. As a result, the dimensions of the policy against overvaluation (usually referred to as the overvaluation purpose), have been the subject of substantial controversy.<sup>175</sup>

In Traynor’s second deficiency context,<sup>176</sup> a depression-induced decline in property values causes the debt to be overvalued in relation to the security. Traynor theorized that section 580b justifiably would disallow a deficiency judgment. It would serve the policy objective of “prevent[ing] the aggravation of the downturn that would result if defaulting purchasers were burdened with personal liability.”<sup>177</sup> This second policy objective is most often referred to as the “stabilization” purpose underlying section 580b.<sup>178</sup> In neither *Roseleaf* nor *Bargioni* did Traynor explore the means by which allocating the entire loss to the seller rather than the purchaser would mitigate the economic downturn.<sup>179</sup> It remains necessary, therefore, to evaluate the modern dimensions of both the overvaluation and the stabilization policies.

(a) *Construction/interpretation of overvaluation-related policy.* Judges<sup>180</sup> and commentators<sup>181</sup> since *Roseleaf* and *Bargioni* typically have defined the price-overvaluation scenario to involve merely a seller who demands and receives a sum greater than the realistic fair market value at the time of purchase. In that literal context, section 580b could be considered to effectuate a regulatory<sup>182</sup> policing of the domestic real estate market. Since *Roseleaf* and *Bargioni*, however, the serial develop-

174. *Bargioni*, 59 Cal. 2d at 123, 378 P.2d at 594, 28 Cal. Rptr. at 322.

175. See, e.g., Hetland, *Deficiency Judgment*, *supra* note 8, at 3-7; Leipziger, *supra* note 8, at 758-63.

176. See *supra* text accompanying note 172. The latter half of the *Roseleaf* passage addresses the depression-induced deficiency scenario.

177. *Roseleaf*, 59 Cal. 2d at 42, 378 P.2d at 101, 27 Cal. Rptr. at 877 (1963).

178. See, e.g., Leipziger, *supra* note 8, at 763-66. Professor Hetland gives an alternative label to the policy objective—the “depression cushion” purpose. See Hetland, *Deficiency Judgment*, *supra* note 8, at 3-7.

179. For criticism of the purported stabilization policy objective, see Hetland, *Deficiency Judgment*, *supra* note 8, at 3-7; Leipziger, *supra* note 8, at 763-66.

180. See, e.g., *Prunty v. Bank of Am.*, 37 Cal. App. 3d 430, 112 Cal. Rptr. 370 (1974).

181. See Hetland, *Deficiency Judgment*, *supra* note 8, at 2-7; Leipziger, *supra* note 8, at 758-66; Rintala, *supra* note 8, at 257-62.

182. Professor Brilmayer, drawing on work of earlier academic commentators, divided government policies into two types: protective policies and regulatory policies. Brilmayer, *Interest Analysis and the Myth of Legislative Intent*, 78 Mich. L. Rev. 392 (1980). “If a state has a protective policy, then its interest in applying its law depends upon the residence of the defendant. State protective policies are designed to benefit resident defendants alone.” *Id.* at 395. Brilmayer identified regulatory policies as directed toward matters within the territory of the state, regardless of the domicile of the implicated party.

Currie found . . . “conduct-regulating” interests—the third class implicit in his analysis of legislative policies—to be triggered by territorial connecting factors rather than domiciliary

ment of case law<sup>183</sup> effectively has reshaped the price-overvaluation policy. The significance of any market-regulatory objective has been diminished.<sup>184</sup> Instead, section 580b has come to reflect the goal of allocating the deficiency loss through risk analysis. Modern case law retains the conceptual framework of the overvaluation-induced default, as Traynor visualized. Courts now hold, however, that section 580b requires that the risk of the deficiency loss be borne by the seller, with a possible reallocation of the risk of loss to the purchaser if the purchaser's activities jeopardize the reasonable value of the security.<sup>185</sup> The redefinition of the overvaluation policy—and the reasons behind it—can be identified in the development of section 580b decisional law.<sup>186</sup>

First, in *Roseleaf*, Traynor set out the overvaluation and stabilization rationales as support for section 580b, and determined that a separately secured purchase-money creditor was allowed a deficiency action.<sup>187</sup> In *Bargioni*, decided three weeks later, Traynor extended the policies defined in *Roseleaf* to hold that third-party purchase-money creditors were barred from a deficiency action by section 580b.<sup>188</sup>

The policy rationales of *Roseleaf* and *Bargioni* were met with almost

factors. The most significant territorial connection with the forum [is the] . . . presence of the complained of activity . . .

Because statutes embodying only regulatory policies are so obviously territorial, their conflict of laws implications are rarely litigated. . . . Regulatory policies are triggered by territorial connecting factors, and protective . . . policies by domiciliary factors.

*Id.* at 396-98 (footnote omitted).

183. The California Supreme Court has decided four § 580b cases since *Roseleaf* and *Bargioni*. *Cornelison v. Kornbluth*, 15 Cal. 3d 590, 542 P.2d 981, 125 Cal. Rptr. 557 (1975) (purchase-money creditor's action against debtor for "bad faith" waste of security allowable irrespective of § 580b bar); *Spangler v. Memel*, 7 Cal. 3d 603, 498 P.2d 1055, 102 Cal. Rptr. 807 (1972) (purchase-money lender who subordinated loan not barred from deficiency action by § 580b); *Kistler v. Vasi*, 71 Cal. 2d 261, 455 P.2d 106, 78 Cal. Rptr. 170 (1969) (third-party lender of purchase money not barred from deficiency action by § 580b); *American Sav. & Loan Ass'n v. Leeds*, 68 Cal. 2d 611, 440 P.2d 933, 68 Cal. Rptr. 453 (1968) (§ 580b does not prevent purchase-money creditor from recovering damages for waste of security).

184. If the § 580b overvaluation purpose were to police the domestic real estate market for "unsound" or "overvalued" transactions, such "regulatory policies [would be] . . . so obviously territorial, their conflict of laws implications [would be] . . . rarely litigated." Brilmayer, *supra* note 182, at 397; see *supra* note 182. In other words, California's regulatory interest would be confined to California territory, rather than extending to the regulation of "unsound" or "overvalued" purchase-money transactions in a foreign market. Extending a California regulatory interest to a foreign territory would imply that a California domiciliary could purchase property in any state and § 580b would protect against deficiency judgments. Professor Sedler firmly rejected such a notion. "Interest analysis, of course, does not mean that 'each individual carries around with him his home state's law.'" Sedler, *supra* note 155, at 633 (quoting Ely, *Choice of Law and the State's Interest in Protecting Its Own*, 23 WM. & MARY L. REV. 173, 211 (1981)).

185. For example, the seller's risk might be significantly altered if he subordinates to a construction loan. See *Spangler v. Memel*, 7 Cal. 3d 603, 498 P.2d 1055, 102 Cal. Rptr. 807 (1972), discussed *infra* text accompanying notes 192-98.

186. See cases cited *supra* note 183.

187. 59 Cal. 2d 35, 378 P.2d 97, 27 Cal. Rptr. 873 (1963).

188. 59 Cal. 2d 121, 378 P.2d 593, 28 Cal. Rptr. 321 (1963).

immediate criticism from both legislative and academic quarters.<sup>189</sup> Within a matter of months, the legislature partially overruled the holding in *Bargioni*,<sup>190</sup> providing deficiency rights to third-party lenders, except when the purchase-money loans were made in relation to owner-occupied residences.<sup>191</sup> It was unclear whether the legislative action had undermined altogether the policy rationales on which Traynor had relied to reach third-party purchase-money transactions.

In 1972, the supreme court again took the opportunity to review the policy rationales underlying section 580b. In *Spangler v. Memel*,<sup>192</sup> a seller of development property subordinated purchase-money financing to a third-party commercial development loan. After the construction of an office building and a subsequent default, the junior purchase-money creditor was sold-out and thereafter sued on the note.<sup>193</sup> The partial legislative reversal of *Bargioni* did not lead the supreme court to abandon the overvaluation concept altogether, but rather to change the focus of the inquiry. The court did not stress the policy objective of preventing overvalued purchase-money transactions. Strict compliance with the overvaluation policy objective stated in *Roseleaf* would have required a comparison of the sales price with actual value at the time of the sale, to determine whether the seller's "unsound" and "overvalued" sale destined the commercial project for failure. The court made no market analysis. Instead, the court assessed whether the risk could not be more equitably borne by the purchaser rather than the seller, since the purchaser's development activities undermined the seller's ability to calculate the post-development value of his security.<sup>194</sup>

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189. See Hetland, *Deficiency Judgment*, *supra* note 8, at 2-7.

190. The legislature amended § 580b in 1963. 1963 CAL. STATS. 4500. The court in *Prunty v. Bank of Am.*, 37 Cal. App. 3d 430, 112 Cal. Rptr. 370 (1974), cited the timing of the *Bargioni* decision and the amending legislation as supporting its view that the "amendment was adopted in direct response to *Bargioni*." *Id.* at 441 n.13, 112 Cal. Rptr. at 377 n.13.

191. See *supra* note 13.

192. 7 Cal. 3d 603, 498 P.2d 1055, 102 Cal. Rptr. 807 (1972).

193. In *Brown v. Jensen*, 41 Cal. 2d 193, 259 P. 2d 425 (1953), the court extended the operation of § 580b to a case involving a sold-out junior purchase-money lender. Although commentators had argued that the holding had been eroded, *Spangler* reaffirmed *Brown*. See, e.g., J. HETLAND, *supra* note 124, § 9.24, at 210-14; Hetland, *Deficiency Judgment*, *supra* note 8, at 7-12; Comment, *Application of Antideficiency Statute to Construction Subordination Arrangement*, 61 CALIF. L. REV. 536 (1973).

194. The court stated:

If in [the property development] . . . situation section 580b is applied to prevent the vendor from suing on his promissory note, after the development has failed . . . the risk of failure of the . . . development is thrust upon the vendor. In fact, . . . the success of the . . . development depends upon the competence . . . of the . . . purchaser. It would seem proper . . . that the purchaser not the vendor bear the risk of failure . . . .

*Spangler*, 7 Cal. 3d at 613, 498 P.2d at 1061, 102 Cal. Rptr. at 813.

The court in *Spangler* also invoked, less convincingly, the literal overvaluation purpose by noting that, in the development context, "the security value of the property at the time of sale . . . gives no clue to the market value, since the sale contemplates radical improved and changed use of the

In *Budget Realty v. Hunter*,<sup>195</sup> the court forcefully affirmed the shift from a focus on overvaluation to a focus on risk allocation.<sup>196</sup> The court stated that application of section 580b after a default should allocate the risk between the buyer and seller in accordance with an "equitable analysis of the effect the variant transaction has on the seller's security."<sup>197</sup> That is, it mandated an analysis which would reveal any material alteration of the seller's position of risk. The concept reflects the common maxim that "section 580b places the risk of inadequate security on the purchase money mortgagee."<sup>198</sup> Where a deficiency is induced by price overvaluation, sellers now bear all risk of deficiency loss following a purchase-money mortgage foreclosure, unless the court finds it just to reallocate the risk from the seller to the purchaser because of the purchaser's activities.

(b) *Construction/interpretation of the stabilization-related policy.* The literal language in *Roseleaf* appears to indicate that the stabilization objective underlying section 580b is to regulate the domestic California real estate economy by minimizing the effects of widespread defaults.<sup>199</sup> However, the original stabilization policy also has been substantially redefined by the supreme court. In *Cornelison v. Kornbluth*,<sup>200</sup> the court considered how section 580b should apply when a deficiency was induced not only by a depression but also by the mortgagor's waste of the secur-

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property." *Id.* at 613, 498 P.2d at 1061, 102 Cal. Rptr. at 813. Professor Rintala claimed that "the 'clue' notion buried in the 'overvaluation' paragraph [of *Roseleaf*] . . . becomes critical." See Rintala, *supra* note 8, at 261. The *Spangler* court, apparently reasoned that the unknown postdevelopment value of the property left the seller no clue as to the value of his security at the time of sale. The court continued: "Effective prevention of overvaluation in the sale of property for commercial development . . . lies in forcing the purchaser-developer to make realistic assessments of the likelihood of the project's success . . ." *Spangler*, 7 Cal. 3d at 613, 498 P.2d at 1061, 102 Cal. Rptr. at 813.

195. 157 Cal. App. 3d 511, 204 Cal. Rptr. 48 (1984).

196. The court noted that, rather than preventing literal overvaluation, section 580b promotes [literal] overvaluation in all its application, whether standard or variant. "[T]he impact of CCP § 580b is to encourage overvaluation in every context . . . . The seller will sell for as high a price as he can, even though he is to be undersecured, CCP § 580b notwithstanding . . . . The seller . . . has nothing to lose by taking a purchase-money trust deed that includes the part of the price that is the excess of the property's value . . . . A valueless encumbrance for the excess leaves the seller in no worse position than if he had not had it . . . ."

*Id.* at 515-16, 204 Cal. Rptr. at 51 (quoting J. HETLAND, *supra* note 124, § 9.24, at 212-13).

197. *Id.* at 516, 204 Cal. Rptr. at 51.

198. *Roseleaf*, 59 Cal. 2d at 42, 378 P.2d at 101, 27 Cal. Rptr. at 877.

199. In Justice Traynor's words, § 580b operated "to prevent the aggravation of a depression in land values by not burdening purchasers with loss of the property plus personal liability." *Id.*

If the stabilization concept were really focused on preventing the aggravation of a price collapse, that policy objective might appear to be a territorially connected regulatory policy. See *supra* note 182. In other words, while California might have a strong interest in regulating a localized California depression, there might be no California governmental interest in regulating a localized foreign depression in the *Hersch* foreign-security paradigm.

200. 15 Cal. 3d 590, 542 P.2d 981, 125 Cal. Rptr. 557 (1975).

ity. The court disregarded all analysis of how section 580b might limit the "aggravation of the downturn"<sup>201</sup> by allocating the loss to either party. The *Cornelison* court retained the conceptual framework of the depression-induced default, as well as the premise that the seller assumed full risk of the depression-induced deficiency loss. Within that framework, however, the court applied a risk calculus to determine whether the debtor's actions jeopardized the value of the security, questioning whether the risks should be reallocated to the purchaser.<sup>202</sup>

The *Cornelison* court's solution was straightforward. It segregated the loss due to the debtor's impairment of the security value from the depression-induced reduction in the security value. In contrast to the all-or-nothing *Spangler* solution, the *Cornelison* court elected to offset the seller's justifiable loss (the depression-induced loss in security value) by reallocating part of the loss to the purchaser. The court determined that the seller should be afforded a cause of action for damages due to "bad faith" waste—the reduction in security value caused by the purchaser's bad faith acts.<sup>203</sup>

As a result of this policy reshaping by the court in *Cornelison*, the stabilization concept emerged as a legitimate protective policy,<sup>204</sup> intended to insulate purchase-money debtors from deficiency liability. Other cases subsequent to *Roseleaf* and *Bargioni* have made no analysis of market-regulatory aspects of the stabilization concept in a depression-induced deficiency.

Common to both default contexts which Traynor envisaged is the proposition that whether the inadequacy of purchase-money security at foreclosure is caused by unsound overpricing or by a depression in land values, the seller "knows the value of his security and assumes the risk that it may become inadequate."<sup>205</sup> There is an exception when a purchaser's activities jeopardize the security value in a way that cannot be anticipated by the seller. In such a case, the risk of loss may be reallocated, in whole or in part, to the purchaser through equitable-risk analysis.

(c) *Policies underlying per se risk allocation to seller.* The courts have yet to delineate the policy underlying the rule of per se allocation of loss to the seller in the standard purchase-money foreclosure.<sup>206</sup> Identi-

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201. *Roseleaf*, 59 Cal. 2d at 42, 378 P.2d at 101, 27 Cal. Rptr. at 877.

202. In *Cornelison*, since the creditor had entered a full credit bid at the trustee's sale which established the value of the security as equal to the remaining indebtedness, no action for "bad faith" damages existed. *Cornelison*, 15 Cal. 3d at 606, 542 P.2d at 992, 125 Cal. Rptr. at 568.

203. *Id.* at 604, 542 P.2d at 991, 125 Cal. Rptr. at 567.

204. See *supra* note 182.

205. *Brown v. Jensen*, 41 Cal. 2d 193, 197, 259 P. 2d 425, 427 (1953).

206. Justice Traynor introduced the notion of standard and variant purchase-money transactions in *Roseleaf*:

fyng such a specific policy has been largely unnecessary in applying section 580b in domestic contexts, since the cases simply evaluate how a variant transaction differs from the standard purchase-money transaction. Fortunately, the policies underlying section 580b's per se risk allocation are evident. The rationale which supported section 580b prior to establishment of the overvaluation and stabilization concepts should still retain vitality, and can be discerned from sources predating *Roseleaf* and *Bargioni*.

The drafters of section 580b apparently denied the purchase-money creditor the right to a deficiency judgment simply because in the event of default, the seller could reacquire the property at foreclosure with a credit bid.<sup>207</sup> Since the seller could reacquire the property and retain the principal payments, the drafters reasoned that he was not justified in obtaining deficiency rights as well.<sup>208</sup> An amicus curiae brief in *Roseleaf* urged this traditional point of view:

For many years the law respecting the position of lenders has been certain . . . . One who sold real property and took back a note and trust deed for the balance owing has known for many years that if he were required to foreclose he would only be entitled to retain the payments thus far made [without deficiency rights] . . . . This was felt to be fair because he at least received back what he had sold plus the down payment and the payments thus far collected. . . . [T]he law was certain and the choice his.<sup>209</sup>

In *Roseleaf*, which concerned the imposition of a section 580b bar following the foreclosure of a separately secured purchase-money mortgage, Justice Traynor seemed to give effect to traditional theory, which held that the purpose of section 580b was to return the seller/creditor to his presale position without any additional advantage. In holding section 580b inapplicable to separately secured notes, Traynor acknowledged that the seller would not be returned to his presale status: "[T]o apply section 580b here would mean that the [purchaser] would acquire the

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Section 580b was apparently drafted in contemplation of the standard purchase money transaction, in which the vendor . . . retains an interest in the land sold to secure payment of the purchase price. Variations on the standard are subject to section 580b only if they come within the purpose of that section.

59 Cal. 2d at 41, 378 P.2d at 101, 27 Cal. Rptr. at 877.

207. Interview with Edward Landels (Jan. 28, 1985). Landels was counsel for the California Land Title Association and the California Bankers Association during the 1930's. He was primarily responsible for drafting Senate Bill 7 in 1932, which was amended to contain § 580b and was enacted in 1933. Senate Bill 7, as enacted, also included §§ 580a and 726 fair-value requirements. For Landels' contemporaneous commentary on the proposed legislation, see Landels, *Objections to Three Proposed Trust Deed Bills*, 9 THE COMMONWEALTH—PART TWO 27 (1932); Landels, *Report of the Executive Secretary*, 1932 CAL. LAND TITLE ASS'N PROC. 9.

208. Interview with Edward Landels (Jan. 28, 1985).

209. Amicus Curiae Brief of M. Luftig at 1-2, *Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 378 P.2d 97, 27 Cal. Rptr. 873 (1963) (on file with the *California Law Review*).

[property] at less than the agreed price."<sup>210</sup> In *Roseleaf*, only the separately secured note was in default. In *Bargioni*, the controversial and partially reversed extension of section 580b to third-party lenders,<sup>211</sup> Traynor did not refer to the original policy limits. Probably this was because they would not support the extension of section 580b to third parties. A third-party lender bargains for repayment of a debt, and only payment of a deficiency judgment could return him to his presale position, if the foreclosure proceeds do not satisfy the indebtedness.

The original policy of denying the unjustified deficiency right, while not yet expressly cited by the courts, seems best to explain the modern policy content which supports the per se risk allocation to the creditor in standard purchase-money transactions. The modern concept of equitable risk analysis and the original policy rationale coexist comfortably.<sup>212</sup> Thus, when the purchaser's activities jeopardize the security value, it is

210. *Roseleaf*, 59 Cal. 2d at 43, 378 P.2d at 101, 27 Cal. Rptr. at 877.

211. See *supra* notes 189-91 and accompanying text.

212. Within Professor Brilmayer's framework, the policy of forbidding a deficiency judgment to the purchase-money creditor could be categorized as a domiciliary-connected protective policy. See *supra* note 182.

However, the redefinition of the overvaluation and stabilization policies and the rationale that the seller can be returned to his presale position by a credit bid, does not identify the policy objective behind the 1963 amendment to § 580b. The amendment extends the deficiency proscription to third-party purchase-money lending on owner-occupied residential property. Third-party lenders cannot be returned to their pretransaction position by a credit-bid acquisition of the secured property at a foreclosure sale, since they only bargained for repayment of the loan. In the owner-occupied residential-lending context, the § 580b policy objective may be to impose the risk of loss, due either to price overvaluation or depression, on the party who can bear it best. Typically, this would be the third-party institutional lender who financed the residential property purchase.

The leading case interpreting the owner-occupied residential third-party lender aspect of § 580b supports this view. In *Prunty v. Bank of Am.*, 37 Cal. App. 3d 430, 112 Cal. Rptr. 370 (1974), the Bank of America made a residential construction loan that was not strictly a purchase-money loan since the debtor already owned the land. The residence was destroyed later in a landslide. In support of imposing the entire risk on the third-party lender through § 580b, the court stated:

[I]t seems particularly appropriate that the "risk," and the ensuing loss in consequence, be borne by defendant bank because of the opportunities it had—and utilized—to protect its security interest against the landslide loss . . . . These opportunities included the control exercised by the bank over the . . . construction of plaintiff's residence in contemplation of landslide and other physical risks . . . . We may reasonably assume that such protective measures are readily available to lenders who finance residential construction . . . and that . . . protection of residential construction borrowers, against deficiency judgments, was continued (under the 1963 amendment) in recognition of the fact that the lenders involved are able to protect themselves against . . . devaluation of their security . . . ."

*Id.* at 442, 112 Cal. Rptr. at 378.

This Comment applies governmental interest analysis only to the *Hersch* foreign-security paradigm involving *vendor* purchase-money financing. The policies underlying the third-party, residential-lending aspect of § 580b are necessarily separate from the policies underlying the vendor-financing aspect of § 580b, so they must be considered independently when such a conflicts case arises. It would be logical to find that such policies are regulatory and hence territorially connected. In other words, California might identify no legitimate interest in regulating a foreign third-party institutional lender financing a foreign residential loan, even if the deficiency controversy found its way into a California forum.

recognized that the risk should be allocated to the purchaser. This is equivalent to recognizing that the seller could not be returned to his presale position by a credit bid.

ii. *Policy advancement in the multistate context.* A court must determine whether it would advance the legitimate policies underlying 580b to apply the section in the multistate context.<sup>213</sup> In the *Hersch* paradigm, where California law governs the promissory note, the policy objective of imposing the entire deficiency loss on the seller is advanced equally in foreign-security transactions and in domestic-security transactions. In either case, the seller can retain the principal payments, reacquire the property by credit bidding in the event of default, and be returned to his presale position. Conversely, if the deficiency were permitted following the sale of the foreign security, the exact harm section 580b seeks to remedy would occur: the creditor could burden the California debtor with an unjustified deficiency judgment. With a California purchaser, the allowance of deficiency rights would result in the same intrastate effects in either the California or foreign property purchase-money transaction. Accordingly, the state policy underlying 580b suggests that in such a foreign-property default scenario, the seller should not be afforded more than the right to principal payments and the right to reacquire the property by credit bid.

Should it affect California's section 580b policy if the security contract in the *Hersch* paradigm is governed by foreign law? The security contract merely allows the security-situs state to control the foreclosure remedy. The purchaser's acquiescence to New Mexico's control of the foreclosure proceedings is unrelated to the intended effect of section 580b, which separately bars a deficiency action after the foreign foreclosure. That California law governs the promissory note, while foreign law governs the security instrument and concomitant foreclosure procedures, should not affect the antideficiency policy underlying section 580b.<sup>214</sup>

It must be noted that section 580b will offer broader protection to purchase-money debtors in foreign-security transactions than it would in California-security transactions. Professor Hetland explains that the fair-value appraisal requirement will insulate defaulting purchase-money debtors from unjustified deficiency liability in most domestic default scenarios, except when a depression significantly lowers land values, thus duplicating the effect of section 580b.<sup>215</sup> As will be argued,<sup>216</sup> however,

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213. See *supra* text accompanying notes 51-52.

214. The provisions in the security contract could not be construed as a waiver of § 580b rights. Under California law, a debtor may not prospectively waive the protection of the antideficiency statutes. CAL. CIV. CODE § 2953 (West 1974) prevents a creditor from extracting a waiver of §§ 726 and 580a. *Valinda Builders v. Bissner*, 230 Cal. App. 2d 106, 40 Cal. Rptr. 735 (1964), holds that §§ 580b and 580d cannot be waived prospectively.

215. See Hetland, *Deficiency Judgment*, *supra* note 8, at 2-7.

California should have no governmental interest in imposing its fair-value appraisal requirements on a foreign state's internal foreclosure scheme. Consequently, the application of section 580b would protect a California domiciliary purchase-money debtor from a wider range of deficiency actions in the foreign-security context than in the California-security context. In accordance with Hetland's analysis, it might be argued that California's section 580b policies are directed exclusively toward the depression-induced deficiencies not prevented by the fair-value statutes.<sup>217</sup> However, as noted, the policies underlying section 580b are advanced regardless of whether there is a depression, so long as the seller can recover his property by credit bidding.<sup>218</sup> Hence, it is appropriate to apply section 580b in a nondepression foreign-security context.

*b. New Mexico: Policy Identification and Policy Advancement*

*i. Policy identification through construction/interpretation.* In response to a debtor's section 580b defense, the seller might argue for application of the conflicting laws of New Mexico, which allow a deficiency action. In support of such a claim, the seller might urge that New Mexico's law on deficiencies is a part of the security agreement, expressly (or impliedly) governed by New Mexico's law.

New Mexico's law allows deficiency judgments following the foreclosure of purchase-money mortgages. Alternative rationales might support New Mexico's prodeficiency policy in purchase-money transactions. First, New Mexico's legislative scheme might reflect a normative policy requiring purchasers to assume the full risk of their lending contracts, including the risk that the property purchased is overpriced, or that the property might become less valuable in a depression. Alternatively, a prodeficiency scheme simply might reflect a procreditor policy, allowing the purchase-money lender a deficiency action like any other lender. Such a procreditor policy might be founded on New Mexico's desire to encourage seller financing as market-efficient. Without attempting to identify concrete reasons for New Mexico's prodeficiency policy, it is possible to evaluate New Mexico's governmental interest in extending its deficiency policy to the *Hersch* paradigm.

*ii. Policy advancement in the Hersch multistate context.* In the *Hersch* paradigm, the seller of the New Mexico property acquiesced in choice of California law to govern the purchase-money note, agreeing

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216. See *infra* text accompanying notes 269-81.

217. See Hetland, *Deficiency Judgment*, *supra* note 8, at 2-7.

218. See, e.g., *Spangler v. Memel*, 7 Cal. 3d 603, 498 P.2d 1055, 102 Cal. Rptr. 807 (1972); *Prunty v. Bank of Am.*, 37 Cal. App. 3d 430, 112 Cal. Rptr. 370 (1974), in which the applicability of § 580b was evaluated without focusing on the existence of a depression.

that New Mexico law was to govern only the security contract. The bases for prodeficiency policies suggest that New Mexico would have no governmental interest in extending these policies to the *Hersch* facts. First, the intended beneficiaries of New Mexico's prodeficiency policy are, presumably, purchase-money creditors who are New Mexico domiciliaries or creditors whose contracts are governed by New Mexico law. No matter whether the prodeficiency policy is based on the normative theory that debtors should be burdened with liability for their debts, or on the pragmatic theory that creditors deserve deficiency rights, the policy should be mitigated by the fact that the purchase-money creditor agreed to let California law govern the promissory note. It would be unreasonable to consider New Mexico's prodeficiency policy so strong as to deny its landowner the right to contract for deficiency protection.

Second, New Mexico could not claim legitimately that its prodeficiency policy was integrated into a security contract governed by its law. The security contract should do no more than hypothecate the property and provide for its foreclosure, while a separate promissory note controls the debt. It is more reasonable to consider New Mexico's prodeficiency policy or California's antideficiency policy as integral parts of a debt governed by either state's law. Personal liability on the note governed by California law should be precluded from the inception of the transaction, regardless of the foreclosure remedies later provided for by the situs state.<sup>219</sup>

Finally, since in the *Hersch* paradigm the debtor contracted for California law, it is likely that he justifiably relied on purchase-money deficiency protection accruing to him in making the contract. New Mexico, accordingly, should respect the justifiable expectations of the contracting parties, as California courts appear to do.<sup>220</sup>

The preceding analysis suggests that New Mexico could not identify a legitimate governmental interest in extending its prodeficiency scheme to the *Hersch* paradigm. Since only one state would have an interest in applying its law, a false conflict would exist, and interest analysis would direct the application of California law.<sup>221</sup>

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219. The same equitable exceptions developed in California case law would govern the *Hersch* foreign-security context. For example, *Spangler v. Memel*, 7 Cal. 3d 603, 498 P.2d 1055, 102 Cal. Rptr. 807 (1972) would apply in the subordination context. See *supra* text accompanying notes 192-98. In the "bad faith" waste context, *Cornelison v. Kornbluth*, 15 Cal. 3d 590, 542 P.2d 981, 125 Cal. Rptr. 557 (1975), would apply. See *supra* text accompanying notes 200-04.

220. See *supra* note 155.

221. Additional support for the conclusion, on the *Hersch* facts, that a false conflict exists might be derived from a foreign state's adopted choice of law methodology. For example, the black letter rules of the *Restatement (Second)* are intended to form a part of the foreign state's common law, from which policy content could be identified. Thus, a foreign state having adopted the *Restatement (Second)* could identify its policy toward § 580b in § 229 comment e, which states, in part:

Issues which do not affect any interest in the land, although they do relate to the foreclo-

c. *Application of Section 580b in non-Hersch Context*

The conclusion that California has a governmental interest in applying section 580b in foreign-security transactions, as in the case of section 726, stems from the parties' decision to let California law govern the promissory note. What if foreign property were purchased by a California domiciliary and financed by a purchase-money mortgage, but the transaction was conducted entirely in a foreign state, and foreign law expressly or impliedly governed the promissory note? Should section 580b then apply if a deficiency action were brought in a California forum? As this Comment has argued, the debtor's section 580b antideficiency rights crystallize at the inception of a purchase-money transaction governed by California law. Therefore, where a foreign-property transaction is made in a foreign state absent any connection with California, no deficiency protection exists. The creditor's deficiency rights are integrated into the initial promissory note.

As noted previously, California courts are willing to assume that a foreign state has strong policies toward events, contracts, or relationships within its territory which are governed by its law.<sup>222</sup> Accordingly, when a creditor claims the benefit of a foreign state's remedies for default on a foreign note, California's governmental interest in applying section 580b should be mitigated, even though the controversy arises in a California forum.<sup>223</sup> In *Offshore Rental Co. v. Continental Oil Co.*<sup>224</sup>, the court noted that a California party might be viewed as having "exposed [it]self to the risks of the territory . . . ."<sup>225</sup> In this case, the California party should not expect to subject the other party to California law. The "maximum attainment of underlying purpose by all governmental entities . . . ."<sup>226</sup> would support the foreign state's legitimate interest in applying its own policies to the transaction. Hence, in the foreign-security case where the foreign state has struck a balance in creditor-debtor rights more favorable to the creditor than the scheme in California, and the promissory note impliedly or expressly reflects such a foreign state's legislative scheme, California's interest in applying section 580b should be mitigated.

This foreign-security fact pattern substantially parallels that of

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sure, are determined . . . by the law which governs the debt for which the mortgage was given. Examples of such issues [include] . . . the mortgagee's right to hold the mortgagor liable for any deficiency remaining after foreclosure . . . .

Thus, the *Restatement (Second)*'s black letter rule supports the interpretation that § 580b operates independent of the situs state's foreclosure remedies, and would direct the foreign state to defer to California law.

222. See *supra* text accompanying notes 155-58 and note 155.

223. The court's analysis appears to reflect a fairness inquiry. See *supra* note 155.

224. 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978).

225. *Id.* at 169, 583 P.2d at 728, 148 Cal. Rptr. at 874 (citation omitted).

226. *Id.* at 166, 583 P.2d at 726, 148 Cal. Rptr. at 872 (citation omitted).

*Yunker v. Reseda Manor*.<sup>227</sup> In *Yunker*, a California corporation doing business in Nevada purchased land from a Nevada domiciliary secured by a purchase-money mortgage on the Nevada property. The promissory note impliedly was governed by Nevada law; nonetheless, the California court applied section 580b and barred the deficiency.<sup>228</sup> Certain allegations in *Yunker* could be interpreted to connect the initial purchase-money transaction with California.<sup>229</sup> In substance, however, the *Yunker* holding is inconsistent with the California policy objective of respecting the foreign state's legislative scheme governing its domestic transactions and the justified expectations of the contracting parties. The Nevada creditor could not have expected a deficiency bar in the event of default. The *Yunker* holding appears to deviate significantly from the notion that section 580b rights (or the lack thereof) inhere at the time of contracting. It therefore must be considered suspect as precedent.

### 3. Section 580d and the Fair-Value Statutes

This Comment has argued that the policies underlying sections 726 and 580b are advanced by applying them in the *Hersch* paradigm in which the promissory note is governed by California law, but the security is foreign and the foreclosure remedies are governed by foreign law. The question remains whether state policies underlying section 580d and the fair-value statutes, sections 580a and 726(b), would be advanced in the *Hersch* paradigm if the statutes were given effect following a foreign foreclosure.

Suppose a California domiciliary owns property in Colorado and uses it as security for a promissory note entered into in California.<sup>230</sup> The creditor, also a California domiciliary, expressly agrees that the promissory note is governed by California law.<sup>231</sup> After default, the creditor elects Colorado's nonjudicial foreclosure procedure and then intends to acquire a deficiency judgment.<sup>232</sup> The debtor brings an action in California seeking a declaratory judgment that, in effect, would extend

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227. 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967).

228. See *supra* notes 80-85 and accompanying text.

229. The debtor alleged that the purchase-money creditor had misrepresented that Nevada had a purchase-money antideficiency statute comparable to § 580b. See *supra* note 85.

230. In the actual *Hersch* case, the notes were secured by New Mexico and Iowa property. However, both New Mexico and Iowa require judicial foreclosure sales rather than allowing the creditor to elect judicial or nonjudicial foreclosure. Hence, under the actual *Hersch* facts, the debtor could not raise meaningfully a § 580d issue, since the statute applies only to nonjudicial sales. To make the foreign-security hypothetical workable, it will be assumed that Colorado property is used for security. Colorado was chosen because it allows the creditor a choice between judicial and nonjudicial sales and because Colorado laws are implicated in the *Kerivan* case, also involving § 580d, which is discussed subsequently.

231. The domicile of the debtor should play no part in determining whether Colorado has an interest in applying its internal foreclosure procedures to the Colorado foreclosure.

232. See COLO. REV. STAT. §§ 38-39-101 to -119 (1982).

section 580d and/or sections 580a and 726(b) to the multistate context.<sup>233</sup> Colorado law employs neither a section 580d-type nonjudicial sale deficiency bar, nor fair-value appraisal requirements.<sup>234</sup> Under interest analysis it is necessary in such a fact setting first to determine whether California's policies would be advanced by the operation of section 580d and/or sections 580a/726(b).

*a. California: Policy Identification and Policy Advancement*

*i. Construction/interpretation of policies underlying section 580d and the fair-value statutes.* The enactment of section 580d and the fair-value provisions reflect legislative attempts to protect a defaulting California landowner/hypothecator from unfair treatment by the foreclosing creditor.<sup>235</sup> For convenience, the three statutes will be subsumed under the heading of "debtor-protection" statutes.

The debtor-protection statutes reflect two central policies. First, there is the price-adequacy objective of providing a statutory scheme to insure that the debtor will receive an adequate price for any remaining equity in the foreclosed property.<sup>236</sup> Second, there is the deficiency-limiting objective to insure that the debtor not be burdened by an unfair deficiency.<sup>237</sup> Although both inadequate foreclosure price and unfair deficiencies result from the same event—underbidding at the foreclosure sale—the policy objectives were sometimes treated separately in legislative initiatives.

Debtor-protection objectives arise from the awareness that creditors have two opportunities to profit unfairly from a debtor's default. First, the creditor frequently can outbid other parties at the foreclosure and acquire title to the property at a depressed auction price, then acquire a resale surplus from a later resale at fair market value. Second, the creditor can hold the debtor liable for the deficiency after either a credit bid or a third-party bid disposes of the security interest. The size of the deficiency will vary in inverse proportion to the level of the purchasing bid at the foreclosure sale.

To comprehend the policies underlying section 580d and the fair-value provisions, it is helpful first to outline the policy objectives of a

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233. In order to resolve the issue by means of governmental interest analysis, it is necessary to hypothesize an action brought in a California court.

234. See COLO. REV. STAT. §§ 38-39-101 to -119 (1982).

235. See *Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 40-41, 378 P.2d 97, 99-100, 27 Cal. Rptr. 873, 875-76 (1963).

236. See Washburn, *The Judicial and Legislative Response to Price Inadequacy in Mortgage Foreclosure Sales*, 53 S. CAL. L. REV. 843, 845-51, 930-32 (1980); see also *1982 Creditors' Remedies Legislation*, 16 CAL. L. REVISION COMM'N REP. 1001, 1117-18 (1982).

237. See Washburn, *supra* note 236, at 930-32.

counterpart<sup>238</sup> "debtor-protection" statute, the postsale redemption provision.<sup>239</sup> The redemption statute was enacted in 1851 to implement both the price-adequacy and deficiency-limiting objectives explained above.<sup>240</sup> It was theorized that the redeemable title itself would coerce prospective purchasers (the creditor included) to bid at or near the fair market value of the property in order to avoid the redemption risk. This would insure an adequate price at the foreclosure sale. Further, the statutory redemption period probably would force the creditor to wait twelve months to realize the resale surplus, which entailed substantial risk and expense. The combined effect of the redemption-coerced bid (presumably near market value) and the possibility of postsale redemption was thought to eliminate any threat of an unfair deficiency.

Yet the effectiveness of the redemption period as adequate protection for the debtor soon was called into question. The consensus among commentators was, and is, that the mere existence of defeasible title deters third parties from bidding.<sup>241</sup> Lack of competitive bidding necessarily fails to guard the debtor's equity in the property through the foreclosure process. Only through a postforeclosure disposition of the right of redemption could the debtor have his equity tested by the market.<sup>242</sup>

Both nonredeemable title and third-party bidding at foreclosure sales played a role in the early development of California secured-lending practices. Through an anomaly in judicial development of secured-lending practices, postsale redemption was allowed only after judicial foreclosures.<sup>243</sup> In the nonjudicial foreclosure alternative, protection of the debtor's equity relied exclusively upon market forces—third-party bidding—at the nonjudicial sale.<sup>244</sup>

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238. Statutory postsale redemption periods are the predominant form of statutory "debtor protection" and are employed in over half the states. *Id.* at 930 & n.478.

239. CAL. CIV. PROC. CODE. §§ 729.010-.090 (West Supp. 1985).

240. See 1982 *Creditors' Remedies Legislation*, *supra* note 236, at 1115 & nn.380-81.

241. See Durfee & Doddridge, *Redemption From Foreclosure Sale—The Uniform Mortgage Act*, 23 MICH. L. REV. 825, 841 u.51 (1925) (The statutory postsale redemption period "certainly caps the wall we have built to keep the public away from the public sale. The best market for land is found among those who desire it for immediate use, and to them, obviously, the redemption feature is prohibitive."); Kidd, *Trust Deeds and Mortgages in California*, 3 CALIF. L. REV. 381, 401-02 (1915).

242. See generally G. OSBORNE, *HANDBOOK ON THE LAW OF MORTGAGES* § 8, (2d ed. 1970); Durfee & Doddridge, *supra* note 241.

243. *Koch v. Briggs*, 14 Cal. 256 (1859). See Kidd, *supra* note 241, at 383-90.

244. Professor Kidd argued in 1915 that third-party bidding for nonredeemable title would best protect the debtor's equity in mortgaged property being sold at foreclosure, if adequate notice were given of the sale. Kidd, *supra* note 241, at 402. Third-party bidding after nonjudicial sales, as practiced until the 1930's, was unfair to debtors because of the inadequacy of the notice of sale, both to debtors and third-party purchasers. "The dangerous possibility in the trust deed is in the power to sell the debtor's property without his knowledge. The notice provided is usually by publication in a newspaper . . . There is not one chance in ten thousand that the debtor will ever see the notice." *Id.* at 400.

During the Depression, neither the redemption period nor third-party bidding offered the debtor real protection from inadequate bidding at foreclosure. The actual market for real property was so small that the redemption right was unmarketable. For the same reason, little if any third-party bidding occurred at foreclosure sales. Consequently, there were no impediments to the creditor's taking advantage of the opportunities to improve his personal financial position. First, the resale surplus—of uncertain value during the Depression—could be acquired by a nominal credit bid at the foreclosure sale. Second, the inadequacy of the credit bid allowed a commensurate increase in the allowable deficiency judgment.

Sections 580a and 726(b) were enacted in 1933 partially to counteract the ineffectiveness of the redemption period and third-party bidding to generate adequate prices.<sup>245</sup> The single policy objective of the fair-value statutes was to limit an unfair increase in the deficiency judgment by the creditor's nominal bidding practices. The allowable deficiency was limited to the difference between the remaining indebtedness and the fair value of the property.

To understand the policy objectives behind the 1939 enactment of section 580d, it is necessary briefly to look at the pre-1939 integrated operation of the redeemable title/nonredeemable title mechanisms for insuring price adequacy. It is also important to examine the fair-value appraisal requirements operating within the creditor's alternative remedies of judicial and nonjudicial foreclosure. The purpose of section 580d can be understood only in context of the operation of the redemption period, for which section 580d was a substitute,<sup>246</sup> and the fair-value statutes.

In 1933, in the same legislative package that included the fair-value statutes,<sup>247</sup> judicial foreclosure procedures for the first time were made uniformly available to trust-deed beneficiaries.<sup>248</sup> As a result, all real-property security holders, whether trust-deed beneficiaries or conventional mortgagees, were free to choose between judicial and nonjudicial foreclosure procedures.<sup>249</sup> However, the consequences of electing the alternative forms of foreclosure varied in the extent to which the debtor-protection statutes operated. In electing judicial foreclosure, the creditor was faced with both section 726 fair-value appraisal, limiting the deficiency, and redeemable title, delaying and jeopardizing acquisition of the

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245. *Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 40, 378 P.2d 97, 99-100, 27 Cal. Rptr. 873, 875-76 (1963).

246. *Id.* at 43, 378 P.2d at 101-102, 27 Cal. Rptr. at 877-78.

247. *See generally* 22 CALIF. L. REV. 170 (1934) (analyzing details of the 1933 legislation).

248. CAL. CIV. PROC. CODE § 725a (West Supp. 1985).

249. J. HETLAND, *supra* note 124, § 613, at 248-50.

resale surplus. By contrast, in electing nonjudicial foreclosure, the creditor was faced with only the section 580a fair-value appraisal statute, for the redemption period had never been extended to nonjudicial sales. Any creditor would elect the nonjudicial foreclosure.

To equalize the foreclosure schemes, the legislature might have extended the redemption period to the nonjudicial foreclosure method. It also might have eliminated nonjudicial foreclosures altogether and imposed a single uniform foreclosure remedy.<sup>250</sup> Instead, the legislature retained the dual foreclosure methods, with redeemable title to insure price adequacy in judicial sales and nonredeemable title to generate third-party bidding and price adequacy in nonjudicial sales. To equalize substantially the creditor's choice of remedies, section 580d was enacted to bar deficiencies after nonjudicial sales.

There probably were two policy concerns behind the legislature's rejection of the more obvious equalizing alternatives mentioned above. First, the legislature had a strong interest in retaining the dual system of foreclosures. Nonjudicial foreclosure provided for an efficient disposition of the typical default in which a deficiency judgment was not required.<sup>251</sup> Consequently, section 580d would facilitate market functioning in the absence of an economic depression. Lenders would police their lending practices to guard against potential deficiencies, and could either abandon the deficiency right or foreclose judicially in the few instances where it was necessary.

Second, there were significant disadvantages associated with extending the redemption period to nonjudicial sales. It was widely recognized that the redemption period could not ensure fair market pricing of the debtor's equity at the foreclosure sale, whereas nonredeemable title could generate third-party bidding at the foreclosure sale.<sup>252</sup> Moreover, the institutional lenders had argued effectively that nonredeemable title would result in lower lending costs. These in turn would result in better

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250. See Morton, *Report of Legislative Committee*, 1939 CAL. LAND TITLE ASS'N PROC. 29, 30. The counsel to the C.L.T.A. reported that the final proposals in legislative committee were, first, to abolish all nonjudicial foreclosures, and/or second, to abolish deficiency judgments after both judicial and nonjudicial foreclosures. Instead of adopting either alternative, § 580d was devised as a compromise. See also Landels, *Report of Legislative Committee*, 1937 CAL. LAND TITLE ASS'N PROC. 83, 84 (stating that in 1937 legislative support was increasing for the elimination of nonjudicial sales in favor of judicial sales only).

251. See, e.g., Comm. on Trust Deeds—Northern Section, 1932 COMM. & SECTION REP., CAL. ST. B.J.—PART II 55, 58:

[I]t would not be for the best interest of the people of the State to enact legislation . . . abolishing deeds of trust and requiring all real estate security to be foreclosed by action in court. Foreclosure by court proceedings has been characterized by the Committee . . . appointed by the National Conference of Commissioners on Uniform State Laws, as "a needlessly expensive and cumbersome method which benefits neither party."

252. See, e.g., Durfee & Doddridge, *supra* note 241.

credit terms, thus promoting overall market efficiency.<sup>253</sup>

To establish substantial parity in the judicial and nonjudicial remedies, without extending the redemption period to nonjudicial sales, the legislature enacted section 580d as a redemption substitute. In a frequently quoted passage of *Roseleaf Corp. v. Chierighino*, Justice Traynor described the reasons for substituting section 580d for the redemption period.

The purpose of section 580d is apparent from the fact that it applies if the property is sold under a power of sale, but not if the property is foreclosed and sold by judicial action. Before the section was enacted in 1939 . . . , it was to the creditor's advantage to exercise a power of sale rather than to foreclose by judicial action. His right to a deficiency judgment after either was the same . . . , but judicial foreclosure was subject to the debtor's statutory right of redemption . . . , whereas the debtor had no right to redeem from a sale under the power. . . . [S]ection 580d was enacted to put judicial enforcement on a parity with private enforcement. This result could be accomplished by giving the debtor a right to redeem after a sale under the power. The right to redeem, like proscription of a deficiency judgment, has the effect of making the security satisfy a realistic share of the debt. . . . If the creditor wishes a deficiency judgment, his sale is subject to statutory redemption rights. If he wishes a sale resulting in nonredeemable title, he must forego the right to a deficiency judgment. In either case the debtor is protected.<sup>254</sup>

Before the enactment of section 580d, the creditor had two opportunities to improve his position. He could acquire deficiency rights and/or nonredeemable title. Prior to 1939, the creditor's ability to inflate the size of the deficiency judgment through nominal bidding was already limited. It theoretically was made equal in judicial and nonjudicial foreclosures by the appraisal requirements of sections 726(b) and 580a, respectively. However, there remained one inequality: the creditor's ability to influence the appraisal calculation.<sup>255</sup> In a nonjudicial foreclosure, the creditor could, without risk, enter an inadequate bid in an attempt to induce a lower appraisal, which in turn would result in a proportionate increase in the allowable deficiency. In a judicial foreclosure, the creditor could attempt to induce a lower appraisal with inadequate bidding only by assuming the substantial risk of redemption.

Section 580d eliminated that inequality in the alternative remedies.

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253. Elliot, *Proposition 3 Should Be Disapproved*, 9 THE COMMONWEALTH—PART TWO 188, 190-91 (1932); Lengfeld, *Discussion*, 9 THE COMMONWEALTH—PART TWO 191, 191-92 (1932); Pillsbury, *Proposition No. 3 (Foreclosure of Mortgages and Trust Deeds)*, 9 THE COMMONWEALTH—PART TWO 178, 182 (1932). *The Commonwealth—Part Two* was a publication of the Commonwealth Club of California.

254. *Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 43, 378 P.2d 97, 100-02, 27 Cal. Rptr. 873, 877-78 (1963).

255. See Hetland, *Deficiency Judgment*, *supra* note 8, at 28-31.

The equalizing effect was noted by Professor Hetland, who compared section 580d to the redemption period. Whereas redeemable title "shifted the [creditor's] incentive from a low bid to a realistic bid,"<sup>256</sup> when faced with fair-value appraisal in judicial foreclosure, section 580d entirely eliminated the creditor's opportunity for unfair profit. It entered a de facto full credit bid at foreclosure. It thus surpassed the effect of the redemption period, which only gave the creditor an incentive to shift from a low bid to a bid near the fair value. The enactment of section 580d also circumscribed the creditor's opportunity to profit from nonredeemable title. In effect, section 580d imposes a price on electing the immediate availability of the resale surplus through nonredeemable title: total loss of the deficiency right.

By enacting section 580d, the legislature "placed the [judicial and nonjudicial] remedies on a substantial par."<sup>257</sup> Within the legislative solution, two elements of policy can be identified. First, section 580d achieved the objective of eliminating the creditor's ability to induce a lower appraisal value and concomitantly larger deficiency. In substance, section 580d limits the actual deficiency to zero by the de facto full credit bid. Second, and more important, section 580d attempted to construct a substantively fair balance between debtor protection and the creditor's two opportunities to improve his financial position—the deficiency right and nonredeemable title. The creditor could elect the right to an appraisal-limited deficiency, offset by a devalued right to any resale surplus since the surplus would be unavailable for twelve months, and subject to extra expenses and risk of redemption. Alternatively, section 580d allowed the creditor to elect an immediate no-risk right to the potential resale surplus, offset by the absence of any deficiency rights.<sup>258</sup>

*ii. Policy advancement: section 580d.* The policies underlying section 580d and the fair-value statutes indicate that, in Professor Brilmayer's parlance, California has a regulatory interest<sup>259</sup> in the operation of foreclosure procedures in the state. The statutes create what the legislature determined to be fundamentally fair foreclosure remedies. The intended beneficiaries of the scheme are the owners/hypothecators of California real property, regardless of domicile. These beneficiaries are protected by regulating the creditor's options, once more regardless of the creditor's domicile. Brilmayer agrees with Currie's finding of a territorial, rather than a domiciliary, basis for regulatory interests.<sup>260</sup>

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256. *Id.* at 30.

257. *Id.*

258. Prior to 1983, a creditor could obtain nonredeemable title only through a nonjudicial sale. CAL. CIV. PROC. CODE § 726(e) (West Supp. 1985), enacted in 1983, now allows a creditor to obtain nonredeemable title after a judicial foreclosure, if deficiency rights are waived.

259. See *supra* note 182.

260. See Brilmayer, *supra* note 182, at 396-97.

Under the California statutory scheme, the creditor's and debtor's foreclosure rights flow from their association with California real property security.

Under the *Hersch* facts assumed here, the promissory note is governed by California law, but the foreclosure methods impliedly are governed by Colorado law. In the attempt to establish California's governmental interest in applying the California debtor-protection statutes following a Colorado foreclosure, the debtor, in effect, would be redefining the California interest as a domiciliary protective interest. The debtor would be forced to claim that section 580d represents a protective policy that attaches to every promissory note governed by California law for the benefit California domiciliaries, regardless of whether the security is taken in a foreign state.

But the policies underlying section 580d are territorially connected to California. This is evident from an inquiry into whether the policy objectives are advanced if extended to a Colorado foreclosure. The first policy objective of section 580d is to equalize nonjudicial and judicial foreclosures by eliminating the creditor's ability to induce a lower appraisal value and produce a larger deficiency.<sup>261</sup> However, in a nonjudicial foreclosure in Colorado, no fair-value appraisal limitations on deficiency judgments exist.<sup>262</sup> This California policy objective cannot be furthered meaningfully, because it is inextricably linked to California's internal procedure involving the appraisal limitation.

Even if it were assumed that California's fair-value statutes, sections 580a and 726(b), should be extended respectively to the Colorado nonjudicial and judicial foreclosures, the extension of section 580d still would not advance meaningfully this first policy objective. Section 580d operating in California's foreclosure scheme eliminates the possibility of inducing low appraisals in a single context—when third-party bidding is accompanied by nonredeemable title.<sup>263</sup> As noted, it was reasoned that redeemable title prevented the creditor from inducing low appraisals in judicial foreclosures. However, unlike in California, in Colorado, redeemable title accompanies third-party bidding in both nonjudicial and judicial foreclosures.<sup>264</sup> If section 580a were extended to the Colorado nonjudicial foreclosure, it merely would duplicate the effect of Colorado's statutory postsale redemption period in preventing the creditor from attempting to induce a low appraisal.<sup>265</sup> Thus, if section 580d

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261. See *supra* text accompanying notes 189-91.

262. See COLO. REV. STAT §§ 38-39-101 to -119 (1982).

263. See *supra* text accompanying notes 249-51.

264. COLO. REV. STAT §§ 38-38-102, 38-39-101 to -103 (1982).

265. It must be assumed that Colorado's statutes control all aspects of title to real property within that state, i.e., whether title is redeemable or nonredeemable. The United States Supreme Court has consistently reasoned that issues relating to land titles are peculiarly within the domain of

were to operate as a redemption substitute,<sup>266</sup> it could not advance meaningfully the first policy objective in a foreign foreclosure allowing post-sale redemption, even if sections 580a and 726(b) were applied extraterritorially.<sup>267</sup>

For similar reasons, the extension of section 580d to the Colorado foreclosure would not advance the second policy objective underlying section 580d—equalizing and restricting the creditor's foreclosure remedies. Section 580d is a single element in a comprehensive scheme that imposes two alternative foreclosure remedies, both restrictive: (1) deficiency rights offset by a delayed risk-laden right to redeemable title, or (2) nonredeemable title offset by the loss of deficiency rights. If section 580d were extended to the Colorado nonjudicial foreclosure, the California objectives of establishing these alternative remedies could not be realized. Following a nonjudicial sale, the creditor would be faced with redeemable title *and* the loss of deficiency rights. Following a judicial sale, the creditor would be faced only with the burden of redeemable title, while deficiency rights would remain available. From the creditor's perspective, the remedies would be unequal; the creditor would prefer judicial foreclosure accompanied by deficiency rights. The overriding California policy of equalizing remedies could be furthered only in the context of a Colorado foreclosure if there existed no redemption period following nonjudicial sales—the redemption period for which section 580d substitutes.

In sum, the theory that the extension of section 580d to the Colorado foreclosure would equalize or restrict creditor remedies places form over substance. Section 580d achieves its policy objectives within California only because of the preexisting uses of redeemable and nonredeemable title to insure price adequacy. Consequently, no legitimate California policies would be advanced by the extension of section 580d in the Colorado-security context. Interest analysis does not support a debtor's argument that California has a governmental interest in applying the statute. In the hypothetical California action to extend section 580d to the foreign foreclosure, therefore, the court should identify a false conflict—no California interests are implicated. It should apply Colorado's law allowing the deficiency action.<sup>268</sup>

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a situs state. Hence, California could not constitutionally impose a statute offering the debtor redeemable title onto Colorado's internal foreclosure regime. For a discussion and cogent criticism of the Supreme Court cases disapproving of one state's decrees affecting land titles in a foreign state, see Hancock, *Full Faith and Credit to Foreign Laws and Judgments in Real Property Litigation: The Supreme Court and the Land Taboo*, 18 STAN. L. REV. 1299 (1966); Hancock, *Equitable Conversion and the Land Taboo in the Conflict of Laws*, 17 STAN. L. REV. 1095 (1965).

266. See *supra* text accompanying note 254.

267. See *infra* text accompanying notes 269-85.

268. Only about half the states, including Colorado, utilize a statutory postsale redemption

iii. *Policy advancement: sections 580a and 726(b).* Like the redemption period and section 580d, the fair-value statutes invoke California's legitimate regulatory interest in controlling creditors' foreclosure remedies in cases involving California real-property security. California landowners/hypothecators are the intended beneficiaries. The governmental interest is therefore triggered by territorial connecting factors rather than domiciliary factors.<sup>269</sup> The appraisal statutes are a single element in a comprehensive debtor-protection scheme enacted in 1933, and revised since, which includes exhaustive notice provisions,<sup>270</sup> an expanded reinstatement period,<sup>271</sup> and a statute of limitations on bringing a deficiency action.<sup>272</sup>

In the *Hersch* paradigm, a debtor seeking to apply the fair-value statutes following a Colorado foreclosure would be attempting to extend the protection to Colorado property owners. California has an acknowledged interest in circumscribing a creditor's foreclosure remedy when the creditor's security is California property. It is a different matter to posit that California has an interest in affording a Colorado landowner protections equal to those offered in California, simply because he is connected to California by domicile or by the California choice-of-law provision in the promissory note.

An attenuated state *qua* state interest might yet exist in affording the debtor the benefit of the appraisal statute. It is appropriate then to consider the extent to which the policies underlying California's scheme would be advanced by such extraterritorial application. It must be understood that the intended beneficiaries of the fair-value statutes—hypothecators of California property—will remain unaffected by their extension to a Colorado foreclosure.

As a practical matter, it is probable that some creditors acquire property at Colorado foreclosure sales for less than fair value, which results in unfair deficiencies. Therefore, it may be true that the policy objective of limiting the creditor's deficiency judgment through the fair-value appraisal procedure would be advanced if the statutes were applied following a Colorado foreclosure. Assuming then that California's policy

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period to protect debtors. See Washburn, *supra* note 236, at 930 n.478. If a debtor were to argue that § 580d should bar a deficiency action after a foreign nonjudicial foreclosure in a state not utilizing a postsale redemption period, California's policy of equalizing judicial and nonjudicial remedies could not be advanced. In such a situation, from the creditor's perspective, the remedies would be unequal. The creditor would be allowed nonredeemable title no matter which foreclosure method was selected. However, a deficiency judgment would be barred following a nonjudicial foreclosure if § 580d were given effect. The creditor would simply elect judicial foreclosure and obtain both deficiency rights and nonredeemable title.

269. See Brilmayer, *supra* note 182, at 396-97.

270. CAL. CIV. CODE §§ 2924, 2924b, 2924f (West Supp. 1985).

271. *Id.* § 2924c.

272. CAL. CIV. PROC. CODE § 726 (West Supp. 1985).

would be incrementally advanced and that there exists a true conflict with Colorado law (which does not require a fair-value appraisal),<sup>273</sup> interest analysis requires a final step, an inquiry into comparative impairment.<sup>274</sup>

(a) *Comparative impairment: California policies.* Several factors suggest that California policies would *not* be greatly impaired if California's fair-value requirements were *not* extended to the Colorado foreclosure.<sup>275</sup> First, on the assumed facts, California policy would be advanced only in the limited sphere of foreclosures of existing California promissory notes secured by Colorado or other foreign property. Any decision to extend California's fair-value statutes extraterritorially would be objectionable to California lenders, who might otherwise contract for California law to govern the promissory note. If the extraterritorial application of the fair-value statutes took place, in all likelihood, California lenders would expressly contract to make the fair-value provisions of California law not be an integral part of the promissory note.<sup>276</sup> Alternatively, the lender could provide that the law of the foreign-secur-

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273. See COLO. REV. STAT. §§ 38-39-101 to -119 (1982).

274. See *supra* text accompanying note 52.

275. If the foreign security were not in Colorado, but in a state with a form of fair-value legislation, governmental interest analysis would probably determine that no substantial policy conflict existed. At least sixteen other states have a form of fair-value legislation. ARIZ. REV. STAT. ANN. § 33-814(A) (Supp. 1984); GA. CODE ANN. § 44-14-161 (1982); IDAHO CODE §§ 6-108 (1979), 45-1512 (1977); MICH. COMP. LAWS ANN. §§ 600.3170(1), .3280 (West 1968); NEB. REV. STAT. § 76-1013 (1981); NEV. REV. STAT. §§ 40.457(1), .459 (1983); N.J. STAT. ANN. § 2A:50-3 (West Supp. 1984); N.Y. REAL PROP. ACTS. LAW § 1371(2) (McKinney 1979); N.C. GEN. STAT. § 45-21.36 (1984); N.D. CENT. CODE § 32-19-06 (1976); OKLA. STAT. ANN. tit. 12, § 686 (West 1960); PA. STAT. ANN. tit. 12, § 2621.1 (Purdon 1967); S.D. CODIFIED LAWS ANN. §§ 21-47-16, -48-14 (1979); UTAH CODE ANN. § 57-1-32 (1974); WASH. REV. CODE ANN. § 61.12.060 (West 1961); WIS. STAT. ANN. § 846.165(2) (West 1977).

If the foreign security were in a state which allowed a form of statutory protection against inadequate bidding other than fair-value appraisal, California's governmental interest in applying its statutory scheme might be mitigated. At least six states have codified the power to withhold confirmation of foreclosure sales on grounds of price inadequacy. ARK. STAT. ANN. § 51-1118 (1971); GA. CODE ANN. § 44-14-161 (1982); KAN. STAT. ANN. § 60-2415(b) (1976); MINN. STAT. ANN. ch. 582, app. 2, pt. 1, § 3 (West 1947); NEB. REV. STAT. § 25-1531 (Supp. 1984); N.C. GEN. STAT. § 45-21.34 (1984); WASH. REV. CODE ANN. § 61.12.060 (West 1961). Also, at least two states have codified upset-value statutes. ARK. STAT. ANN. § 51-1112 (1971); LA. CODE CIV. PRO. ANN. art. 2336 (West 1961).

276. In domestic California secured lending transactions, there exists a statutory prohibition against prospective waiver of the protection of the antideficiency statutes as a means of protecting a debtor from a creditor's superior bargaining power. CAL. CIV. CODE § 2953 (West 1974). It would indeed be difficult, however, to refuse enforcement of an express waiver of the fair-value provisions in the context of a promissory note secured by foreign property. Asserting the application of § 2953 would imply that California-resident lenders were intended to be burdened by the fair-value provisions, irrespective of where the security was located. Of course, California lenders would have the alternative of including a foreign choice-of-law provision in the note to insure that the express waiver would be enforceable.

ity situs control the promissory note. The impact of extraterritorial application of the appraisal requirement therefore would be brief.

Second, the California Supreme Court has identified countervailing policy considerations that limit a court in the comparative impairment analysis. A court is not allowed to make judgments on the basis of whether the California balance of creditor-debtor rights is subjectively "better" than Colorado's scheme. In *Bernhard v. Harrah's Club*,<sup>277</sup> the court stated that in the comparative impairment process, a court does not

"weigh" the conflicting governmental interests in the sense of determining which conflicting law manifested the "better" or the "worthier" social policy on the specific issue. . . . [The process] can accurately be described as . . . accommodation of conflicting state policies, as a problem of allocating domains of law-making power in multi-state contexts—limitations on the reach of state policies—as distinguished from evaluating the wisdom of those policies. . . . [E]mphasis is placed on the appropriate scope of conflicting state policies rather than on the "quality" of those policies . . . .<sup>278</sup>

The *Bernhard* court's limitations on the comparative impairment inquiry suggest that a California court should respect Colorado's exclusive domain over its internal foreclosure procedures, even though Colorado policy apparently favors the creditor more than does California policy. Secured-lending practices involving Colorado property might be aptly described as within Colorado's legitimate domain "of law-making power."<sup>279</sup>

Finally, concluding that California has a governmental interest in attaching fair-value appraisal requirements to every promissory note governed by California law could have undesirable consequences.<sup>280</sup> The same rationale which supports the attachment of the fair-value statutes to a note governed by California law also would support the conclusion that a promissory note governed by a foreign state's law is subject to foreign internal foreclosure methods. Under such reasoning, California's complex debtor-protection scheme could be void any time a California landowner hypothecating California land was coerced into agreeing that a foreign state's law should govern the promissory note.<sup>281</sup> Institutional

277. 16 Cal. 3d 313, 546 P.2d 719, 128 Cal. Rptr. 215, cert. denied, 429 U.S. 859 (1976), overruled on other grounds, *Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984).

278. *Id.* at 320-21, 546 P.2d at 723-24, 128 Cal. Rptr. at 219-20 (quoting Horowitz, *The Law of Choice of Law in California—A Restatement*, 21 U.C.L.A. L. REV. 719, 753 (1974)).

279. *Id.* at 320, 546 P.2d at 723, 128 Cal. Rptr. at 220.

280. In other words, the debtor, whether a California domiciliary or other party transacting business in California, should not be able to invoke California's governmental interest in protecting him in out-of-state transactions. "Interest analysis, of course, does not mean that 'each individual carries around with him his home state's law.'" Sedler, *supra* note 155, at 633 (quoting Ely, *Choice of Law and the State's Interest in Protecting Its Own*, 23 WM. & MARY L. REV. 173, 211 (1981)).

281. For example, in an entirely domestic lending transaction secured by California property, a

lenders might be expected to establish sufficient contacts with a foreign state to require that foreign law govern the promissory note. This would import foreign foreclosure methods that offer weaker debtor protection than the California statutory scheme.

In conclusion, California's policies and interests would not be impaired if the fair-value requirements were not extended to the Colorado foreclosure in the *Hersch* paradigm. Moreover, it must be stressed that the advancement of California's fundamental policy of regulating its internal foreclosure practices, and derivatively the California secured-lending climate, is not at issue in the *Hersch* paradigm. Rather, the government's interest is limited to the aid of a narrow class of debtors who might attempt to invoke California's fair-value requirements simply because a promissory note was governed by California law.

(b) *Comparative impairment: Colorado policies.* Colorado's attitude toward a fair-value appraisal is reflected in the content of its substantive laws regarding foreclosure procedures. No appraisal is required to limit the deficiency.<sup>282</sup> It is likely these policies reflect the Colorado legislature's belief that creditor's foreclosure remedies are fair and debtor's rights are adequately protected in the context of Colorado's internal lending climate. One possibility is that the Colorado scheme, which might be deemed procreditor compared with California's debtor-protection scheme, is designed to attract institutional lenders to the Colorado market. The imposition of California's fair-value requirements would upset the balance in Colorado's legislative scheme.

It also could be possible to derive Colorado policy objectives from the state's common law adoption of *Restatement (Second) of Conflict of Laws*. *Restatement (Second)* includes in the Reporter's Note to section 229 a statement that appraisal statutes are an issue collateral to the domestic foreclosure method, which is controlled by the law which governs the promissory note (in this case, California).<sup>283</sup> Cutting against the application of the Reporter's Note, however, is the directive in section 6

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California domiciliary debtor should be protected by the antideficiency statutes, including §§ 580a and 726(b), even if the creditor has some contacts with a foreign state and inserts a foreign choice-of-law provision in the promissory note.

The California Supreme Court has disallowed certain sequences of actions which might otherwise have developed into mechanisms to avoid the integrated effects of the antideficiency statutes. See, e.g., *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974) (in multiple personal and real property security context, eliminating the possibility of using a first judicial action on personal property security to obtain a money (deficiency) judgment followed by a nonjudicial foreclosure of real property security to obtain nonredeemable title); *Freedland v. Greco*, 45 Cal. 2d 462, 289 P.2d 463 (1955) (eliminating the possibility of using two security instruments for the same debt, one to secure personal property and the other to secure real property, to obtain a money (deficiency) judgment in a judicial foreclosure of the personal property interest followed by a nonjudicial foreclosure of the real property interest thereby obtaining nonredeemable title).

282. See COLO. REV. STAT. §§ 38-39-101 to -119 (1982).

283. *Restatement (Second)* § 229.

of the *Restatement (Second)* to evaluate Colorado's internal policies.<sup>284</sup> Colorado's apparent procreeitor policy thus might override the Reporter's Note. Whatever the strength of policy implicated in Colorado's internal foreclosure procedures, it is fair to say that the policy would be completely impaired by imposing California's fair-value requirement.

The comparative impairment analysis shows that, on balance, California's policies intended to protect California landowners would not be significantly impaired if Colorado's law disallowing fair-value appraisals were applied. California would respect Colorado's domain "of law-making power"<sup>285</sup> over its internal foreclosure procedures. Colorado's procreeitor policy, on the other hand, would be significantly impaired by the imposition of California's appraisal requirements, notwithstanding the policy content that might be attributed to the Reporter's Note in *Restatement (Second)*. Hence, Colorado law should be applied.

#### *B. The Kerivan Paradigm: Avoidance of the Antideficiency Statutes in California Security Transactions*

Section A of this part examined the applicability of California's antideficiency statutes in the *Hersch* paradigm, in which a promissory note was governed by California law, but the security was foreign, and the foreclosure remedies were governed by foreign law. Different conflict of laws issues arise, however, when the promissory note is governed by foreign law, but the security is California real property and the foreclosure methods are governed by California law. These were the facts giving rise to *Kerivan v. Title Insurance & Trust Co.*<sup>286</sup> In the *Kerivan*

284. "[T]he factors relevant to the choice of the applicable rule of law include . . . the relevant policies of the forum." *Id.* § 6(2)(c). Further, "the court will take account of the factors listed in [§ 6] . . . in determining the state whose local law will be applied to determine the issue at hand. . . . Varying weight will be given to a particular factor, or to a group of factors, in different areas of choice of law." *Id.* § 6 comment c. Thus, a strong procreeitor policy might override the categorization of fair-value statutes in the *Restatement (Second)*. *Id.* § 229 Reporter's Note.

285. *Bernhard v. Harrah's Club*, 16 Cal. 3d 313, 320, 546 P.2d 719, 724, 128 Cal. Rptr. 215, 220 (1976) (citation omitted), *cert. denied* 429 U.S. 859 (1976), *overruled on other grounds*, *Strang v. Cabrol*, 37 Cal. 3d 720, 691 P.2d 1013, 209 Cal. Rptr. 347 (1984).

286. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983). *Kerivan* arose out of a controversy originally litigated in Colorado. The debtor had hypothecated California real property as security for a preexisting note governed by Colorado law. (Pleadings on file with the *California Law Review*). The deed of trust called for the application of California law. After default, the creditor foreclosed nonjudicially in California. The California trustee thereafter released the promissory note to the creditor since the amount received at the trustee's sale did not satisfy the indebtedness. The creditor then brought an action on the note in Colorado and obtained a judgment for the deficiency. *See Union Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), *cert. denied*, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*). The Colorado court ignored the effect of § 580d by reliance on RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 comment c (1971). The Colorado money judgment was then entered in California,

paradigm, the principal issue is how California's debtor-protection statutes should operate when foreign law governs the indebtedness, but California law governs the foreclosure remedies.

### 1. *California Security: Avoidance of Sections 726 and 580b*

This Comment has argued that California's governmental interest in applying sections 726 and 580b derives from California's connection to the initial financing transaction.<sup>287</sup> Such a connection could involve either the parties' California domiciles at the time of contracting, or the parties' express contract provision that California law controls the debtor's and creditor's rights.<sup>288</sup> Either situation could allow California law to govern the promissory note. In either setting, California's policy objective of debtor protection could be invoked. The *Kerivan* paradigm presents the obverse situation. The promissory note is governed by foreign law as contracted for by foreign parties, even though secured by California real property. California here would defer to the foreign law governing the debt in accordance with its policies of fairness and respecting the justified expectations of the contracting parties,<sup>289</sup> even if the controversy arose in a California forum. Hence, the *Kerivan* paradigm raises no avoidance issues involving sections 726 or 580b.

There are also California-security transactions in which California law governs the promissory note—in other words, wholly domestic transactions. Even when the transaction is entirely domestic, conflicts issues have arisen when a creditor attempts to evade the effects of sections 726 and 580b by bringing an action on the note in a foreign forum. Since this Comment has argued that the rights afforded to the debtor by operation of sections 726 and 580b inhere at the time of contracting,<sup>290</sup> foreign courts should give effect to the statutes.

The leading federal court of appeals precedents cannot be reconciled with this Comment's conclusion that sections 726 and 580b afford a

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and given effect in accordance with the full faith and credit clause. The debtor contested whether California owed full faith recognition to the Colorado judgment. *See Union Bank v. K & W Trucking Co.*, 147 Cal. App. 3d 217, 195 Cal. Rptr. 49 (1983).

In the *Kerivan* case, the debtor sued the trustee, Title Insurance and Trust Co., for negligence in releasing the uncanceled promissory note to the creditor which allowed (or facilitated) the Colorado action for the deficiency.

287. *See supra* notes 148-62, 219-29 and accompanying text.

288. *See supra* text accompanying note 120.

289. This Comment argues that in a fact pattern such as *First-Trust Joint Stock Land Bank v. Meredith*, 5 Cal. 2d 214, 53 P.2d 958 (1936), in which foreign substantive law impliedly governs the promissory note, § 726 should not apply. *See supra* note 71 and text accompanying notes 160-62. This Comment also argues that in fact patterns such as *Yunker v. Reseda Manor*, 255 Cal. App. 2d 431, 63 Cal. Rptr. 197 (1967), in which foreign law governed the purchase-money transaction, § 580b should not have been applicable, absent policy-based reasoning why California law should have been made part of the contract from its inception. *See supra* text accompanying notes 227-29.

290. *See supra* notes 148-62, 219-29 and accompanying text.

debtor substantive contract rights when California law governs the promissory note. In *Maxwell v. Ricks*<sup>291</sup> and *Commercial National Bank v. Catron*,<sup>292</sup> the federal courts reasoned in absolute conformity with the vested rights theory. They characterized section 726 as a California procedural remedy. They held that section 726 need not be given effect when California law impliedly governed the debt and the action was brought outside a California forum. Hence *Maxwell* and *Catron* should no longer be good law since California has abandoned the vested rights precepts.

Similarly, *Martin v. Midgett*,<sup>293</sup> which allowed a creditor to avoid the effect of the section 580b deficiency bar by resort to a foreign forum, cannot be considered to have precedential value. In *Martin*, the Arizona Supreme Court, relying on the traditional vested rights theory, characterized section 580b as a California procedural remedy having no effect outside a California forum.<sup>294</sup>

## 2. California Security: Avoidance of Section 580d

California has an interest in applying section 580d and the fair-value requirements whenever California real property is foreclosed and California's regulatory interest is invoked. Thus, even though the promissory note is governed by foreign law, California has a legitimate interest in regulating the California foreclosure via section 580d and the fair-value requirements. Therefore, there will be a conflicts issue in any case in which a creditor claims that a foreign law at odds with section 580d, 580a, or 726(b) is implicated by the foreign choice-of-law provision in the promissory note.

In fact, the *Restatement (Second)* has been interpreted to posit that a promissory note governed by non-California law can displace the operation of section 580d—and impliedly the fair-value requirements—in the foreclosure of a California-security interest.<sup>295</sup> Such a conflict may arise in the *Kerivan* paradigm whenever the foreign state strictly follows the black letter rules of the *Restatement (Second)*. Accordingly, the following discussion will evaluate the *Kerivan* paradigm only in the context of a conflict with a state which has adopted the *Restatement (Second)* as its conflict of laws methodology.

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291. 294 F. 255 (9th Cir. 1923).

292. 50 F.2d 1023 (10th Cir. 1931).

293. 100 Ariz. 284, 413 P.2d 754 (1966).

294. See *supra* note 98.

295. In *Union Bank v. K. & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), cert. denied, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*), the court held that *Restatement (Second)* § 229 comment e allowed Colorado to ignore § 580d. That Colorado case led to the controversy in *Kerivan*. See *supra* note 286.

a. *California Policies*

i. *Policies underlying section 580d.* This Comment evaluated the policies underlying section 580d<sup>296</sup> and found that section 580d placed the nonjudicial foreclosure remedy on a substantial par with the judicial foreclosure remedy: It requires the creditor to choose between (1) deficiency rights plus a delayed right to the resale surplus, and (2) nonredeemable title to the property offset by the lack of deficiency rights. That balance between alternative foreclosure remedies was intended to offer a creditor taking California security a substantively fair remedy while protecting the debtor from unfair bidding practices.

ii. *Policy advancement in the multistate context.* In the *Kerivan* paradigm, the conflicts issue involving section 580d could arise after either of two sequences of actions by a creditor holding a note governed by Colorado law. First, the creditor could foreclose nonjudicially in California and subsequently obtain a deficiency judgment in a Colorado forum.<sup>297</sup> Alternatively, the creditor could obtain a personal money judgment in Colorado for the amount of the debt, and then foreclose nonjudicially in California. Either sequence appears possible under Colorado law, which allows concurrent or successive actions on the note and in foreclosure of the security interest.<sup>298</sup>

The first sequence appears similar to avoidance schemes which California courts have struck down because the creditor obtained both a deficiency judgment and nonredeemable title.<sup>299</sup> The same result, however, can be attained by following the second sequence, which would be more palatable to a California court. Since the note is not governed by

296. See *supra* text accompanying notes 240-58.

297. This fact pattern resulted in the controversy in *Kerivan*. See *supra* note 286.

298. See COLO. REV. STAT. §§ 38-38-101 to -110, 38-39-101 to -119 (1982).

299. In *Freedland v. Greco*, 45 Cal. 2d 462, 289 P.2d 463 (1955), the creditor held two notes and security instruments which secured the same unfractionalized debt, one on personal property and the other on real property. In a first judicial action on the chattel mortgage, the creditor obtained a money judgment. Then the creditor attempted to foreclose nonjudicially on the real property which would have allowed acquisition of nonredeemable title.

In *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974), the creditor brought a first judicial foreclosure action on personal property security where the note was secured by both personal and real property. The creditor obtained a final money judgment. Subsequently, the creditor attempted to foreclose nonjudicially on the real property. The *Walker* court noted how California's "debtor protection" policies could be evaded if the one-action sanction were not imposed:

[A] creditor accepting substantial real property security for an obligation, by merely requiring an insignificant amount of personal property as additional security, could proceed to a judicial foreclosure of the latter security only, obtain a deficiency judgment in such action and thereafter proceed to a nonjudicial foreclosure of the real property security, thereby circumventing both the statutory requirements of judicial foreclosure [redemption period and fair-value hearing] and the statutory bar against deficiency judgments [§ 580d].

*Id.* at 736-37, 518 P.2d at 334, 111 Cal. Rptr. at 902.

California law, the security-first policies underlying section 726 should play no part in controlling the enforcement of the promissory note. Colorado's rule of substantive law governs the indebtedness and allows successive actions on the note and in foreclosure of the security interest. Therefore, the creditor can obtain a personal money judgment in Colorado. With a de facto deficiency judgment in hand, he then can foreclose nonjudicially in California, thus acquiring nonredeemable title and the deficiency judgment. This result is not permitted by the integrated operation of section 580d and the other California statutes.

In either of these sequences, California's debtor-protection policies would be advanced by applying California's statutory scheme. The policies are designed to regulate the foreclosures of security interests in California real property and to protect the California landowner/hypothecator.<sup>300</sup> California therefore has a legitimate governmental interest in applying the statutory scheme, irrespective of Colorado law governing the promissory note.

In an action in a California court in the *Kerivan* paradigm, California's integrated foreclosure policies, including section 580d, could be implemented exactly as they would be implemented in entirely domestic contexts. A creditor in the *Kerivan* paradigm would be forced to elect either judicial or nonjudicial foreclosure in California. If the creditor sought a deficiency judgment, he would be required to foreclose judicially and be burdened with redeemable title. If the creditor elected the nonjudicial foreclosure alternative, section 580d would bar any future deficiency action, but nonredeemable title would be available. In the event that the creditor had already obtained a de facto deficiency judgment through a first action on the note in Colorado, California law should require that redeemable title accompany the deficiency right. The debtor should be empowered to compel the creditor to foreclose judicially, thus allowing postsale redemption.

#### *b. Colorado Policies*

*i. Policies underlying Colorado's prodeficiency rule.* Colorado's domestic rule of law allows a deficiency action following either a judicial or nonjudicial sale in Colorado.<sup>301</sup> The question is whether Colorado has a governmental interest in extending its policy allowing deficiency rights

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300. See *supra* note 131. Section 580d should be characterized as a territorially based regulatory policy. All foreclosures of California property are regulated by the nonjudicial/judicial foreclosure sale scheme, which in turn implicates § 580d.

301. *Union Bank v. K & W Trucking Co.*, No. 81CA0241 (Colo. Ct. App. Dec. 31, 1981) (opinion not selected for publication) (opinion on file with the *California Law Review*), *cert. denied*, No. 82SC95 (Colo. Sup. Ct. June 28, 1982) (denial of certiorari on file with the *California Law Review*). See COLO. REV. STAT. §§ 38-38-101 to -110, 38-39-101 to -119 (1982).

after nonjudicial sales to the multistate context involved in the *Kerivan* paradigm.

ii. *Policy advancement in the multistate context.* Assuming Colorado has a strong prodeficiency policy in its domestic transactions, there is an issue whether the policy should extend to the *Kerivan* paradigm, in which the creditor has agreed that California law governs the foreclosure remedies. A claim by the creditor that Colorado has a policy of allowing deficiency rights following a nonjudicial sale can be understood only in the context of Colorado's domestic foreclosure scheme. In Colorado, the debtor's right to redeem the property accompanies deficiency rights which are allowed after a nonjudicial sale.<sup>302</sup> The policy actually parallels California's policy, which couples deficiency rights with redeemable title in order to protect debtors.<sup>303</sup> It thus would appear that Colorado's domestic policy toward protecting debtors parallels California's interest in requiring that judicial foreclosure (deficiency rights) be accompanied by redeemable title. Under this line of reasoning, a false conflict exists.

Alternatively, Colorado's policy might be derived from the black letter rules of the *Restatement (Second)*. On the discrete issue of foreclosure methods, Section 229 states: "The method for the foreclosure of a mortgage on land and the interests in the land resulting from the foreclosure are determined by the local law of the situs."<sup>304</sup> Comment a to that section states: "The courts of the situs would apply their own local law to determine the method of foreclosure, such as whether the mortgage may be foreclosed by sale without a judicial proceeding . . . ."<sup>305</sup>

If Colorado referred to the rules of the *Restatement (Second)*, it would thus find support for the operation of California foreclosure procedures. This should include the central tenet of California foreclosure law: the election of either a judicial or a nonjudicial foreclosure and the accompanying aspects of title (redeemable or nonredeemable). Since the *Restatement (Second)* suggests that Colorado policy would respect California's foreclosure method, the creditor should be able to raise no legitimate Colorado governmental interest in relieving the creditor of the California foreclosure election requirement.

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302. COLO. REV. STAT. §§ 38-38-102, 38-39-101 to -103 (1982).

303. CAL. CIV. PROC. CODE §§ 729.010-.090 (West Supp. 1985). Thus, in Colorado's domestic lending context, any time the creditor forecloses he obtains only redeemable title. Colorado, unlike California, has no mechanism by which the foreclosing creditor might obtain nonredeemable title. In California, § 580d allows nonredeemable title after nonjudicial sales, with the creditor paying the price of forfeiting deficiency rights. CAL. CIV. PROC. CODE § 726(e) (West Supp. 1985) allows the creditor in a California transaction to obtain nonredeemable title in a judicial sale by waiving the right to a deficiency.

304. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 (1971).

305. *Id.* § 229 comment c.

In sum, both California and Colorado have an identical policy with respect to deficiency rights: they are available to any creditor. A false conflict exists on the deficiency issue. With respect to the foreclosure methods required to obtain a deficiency judgment in the *Kerivan* paradigm, again, both California and Colorado have identical policies and there is a false conflict. In both states, redeemable title accompanies deficiency rights. Interest analysis would direct the application of California law.

Application of governmental interest analysis suggests that a creditor should not be able to displace section 580d merely by providing that foreign law governs the promissory note. *Kerivan v. Title Insurance & Trust Co.*,<sup>306</sup> which would allow such a displacement, therefore, must be considered suspect.

### 3. *Avoidance of Sections 580a and 726(b)*

#### a. *California Policies*

This Comment has argued that California regulatory policies underlying the fair-value requirements are invoked in any foreclosure of California property.<sup>307</sup> The policy objective of protecting a California landowner from an unfair deficiency judgment thus would be advanced whether or not the note contains a Colorado choice-of-law provision. Interest analysis requires identification of Colorado's policies and examination of whether they would be advanced by application of Colorado law in the multistate context.

#### b. *Colorado Policies*

i. *Policy advancement in the multistate context.* Assuming that Colorado has a strong domestic procreeitor policy which does not require fair-value appraisals,<sup>308</sup> it is not clear what policy mandates imposing its no-appraisal rule on a California foreclosure. Colorado could consider the appraisal requirement a part of California's foreclosure method, integrated by implication into California's internal foreclosure procedures. Accordingly, Colorado could consider its no-appraisal scheme to be directed only toward foreclosures of Colorado property, not toward foreclosures by any Colorado resident creditors regardless of property situs.

On the other hand, Colorado might consider that the appraisal issue should be determined by the Colorado law which governs the promissory note. In support of such a theory, Colorado could identify its policy con-

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306. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

307. See *supra* text accompanying notes 269-81.

308. See COLO. REV. STAT. §§ 38-39-101 to -119 (1982).

cerning appraisal requirements by reference to its adopted conflict of laws methodology, the *Restatement (Second)*. The Reporter's Note to Section 229 of the *Restatement (Second)* categorizes as "the law which governs the debt," statutes which "restrict the amount recoverable on a deficiency judgment by requiring that the true value of the land, rather than the amount realized on foreclosure, be deducted from the face amount of the personal obligation."<sup>309</sup> Reliance on this rule would suggest a Colorado governmental interest in applying Colorado law, since it governs the note.

(a) *Comparative impairment.* Since both California and Colorado could identify a governmental interest in applying their rules of law, a true conflict arises, requiring an evaluation of the comparative impairment of the competing states' policies.<sup>310</sup>

If California's fair-value appraisal were not required, at least two factors suggest that California's policies would be substantially impaired. First, the fair-value requirement is pertinent to the foreclosure situation in the *Kerivan* paradigm. The statute was designed to protect California landowners from creditors' unfair bidding practices. Because it is against public policy to coerce a debtor to waive the protection of the fair-value requirements,<sup>311</sup> the waiver should not be effectuated simply by the foreign choice-of-law provision in the note. Second, any deviation from application of the fair-value requirements might allow evasion of other debtor-protection statutes. For example, a foreign creditor's avoidance of the fair-value requirement would allow other foreign creditors to argue for nonredeemable title and a deficiency judgment pursuant to foreign law governing a note.<sup>312</sup>

By contrast, if Colorado's law were not applied, Colorado's policy impairment would appear insignificant. Colorado's legislative scheme for balancing creditor-debtor rights should be considered directed toward domestic Colorado transactions. Colorado should discount its policies when a Colorado party "expose[s] [it]self to the risks of the [California] territory . . ."<sup>313</sup> when it elects to acquire a security interest in California real property. A Colorado resident creditor should not reasonably expect that Colorado law would displace a foreign foreclosure scheme. Also, Colorado's policies might be identified by reference to the section 6 factors<sup>314</sup> in the *Restatement (Second)*. Section 6(2)(c), urging

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309. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 229 Reporter's Note (1971).

310. See *supra* text accompanying note 52.

311. See *supra* text accompanying notes 280-81.

312. See *supra* note 214.

313. *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978) (citation omitted).

314. See *supra* note 57.

respect for "relevant policies of other interested states,"<sup>315</sup> would direct Colorado to take notice of California's strong policy toward affording its landowners the right to an appraisal limitation on any deficiency judgment. Further, section 6(2)(d) would direct Colorado to consider the "protection of justified expectations"<sup>316</sup> of the California landowner who reasonably thought that California's law would govern a debtor's rights regarding a security contract governed by California law. These factors suggest that Colorado's legitimate governmental interest would not be impaired significantly if the California appraisal requirement were applied.

Further, it is questionable whether a legitimate Colorado interest in disallowing the fair-value appraisal can be derived from the Reporter's Note in the *Restatement (Second)*. Reporter Reese's note to section 229, addressing foreclosure methods, represents an attempt to support the black letter rules generated by the most significant relationship theory with case law decided under the traditional vested rights theory.<sup>317</sup> Such early cases do not support meaningfully the concept that an appraisal statute is more significantly connected with the promissory note than with the security contract. It should be noted that the conclusion that the law governing the debt governs appraisal rights is found only in the Reporter's Note to section 229. Hence, the section 6 factors in *Restatement (Second)* arguably could override the policy suggested in the Reporter's Note.

In as close a case as this, guidance can be sought in the California Supreme Court's statement that the comparative impairment process seeks the "maximum attainment of underlying purpose by all governmental entities"<sup>318</sup> in the conflict. In the *Kerivan* paradigm, only a limited impairment of Colorado's legitimate policies would occur if California law were applied. California policies, by contrast, would be completely impaired if Colorado law were applied. Applying California law therefore would achieve the greatest substantive policy advancement. In sum, a foreign choice-of-law provision in a promissory note should not be able to void the fair-value requirements.

### CONCLUSION

The landmark opinion of *Reich v. Purcell*<sup>319</sup> in 1967 should have

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315. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(2)(c) (1971).

316. *Id.* § 6(2)(d).

317. The cases cited by Reese included *Belmont v. Cornen*, 48 Conn. 338 (1880); *Hewitt v. Dredge*, 133 Minn. 171, 157 N.W. 1080 (1916); *Hall v. Hoff*, 295 Pa. 276, 145 A. 301 (1929).

318. *Offshore Rental Co. v. Continental Oil Co.*, 22 Cal. 3d 157, 583 P.2d 721, 148 Cal. Rptr. 867 (1978).

319. 67 Cal. 2d 551, 432 P.2d 727, 63 Cal. Rptr. 31 (1967).

exorcised the ghost of the vested rights methodology from modern conflict of laws opinions on California's antideficiency statutes. Justice Traynor, in 1976, wrote:

A conflict of laws must be resolved much like any other legal dispute, by rational inquiry into a complex of considerations. If judges fulfill that obligation there can be a new Age of Enlightenment in law. We are coming to the end of a long Dark Age that was in great measure sustained by the enshrinement of mechanical concepts in the first Restatement of Conflict of Laws . . . .<sup>320</sup>

Yet two recent cases, *Hersch & Co. v. C & W Manhattan Associates*<sup>321</sup> and *Kerivan v. Title Insurance & Trust Co.*,<sup>322</sup> again raised vested rights arguments and precedents regarding the extraterritorial application and avoidance of sections 726, 580b, and 580d. It is disheartening to see courts, in what Justice Traynor had hoped to be an "Age of Enlightenment," resurrect mechanical concepts from the "Dark Age" of vested rights theory.

The application of governmental interest analysis to the *Hersch* and *Kerivan* facts reveals that reliance on vested rights precedents does not lead to results which give effect to the legitimate policies underlying California's antideficiency legislation. This Comment concludes that sections 726 and 580b afford a debtor valuable protections which inhere to any promissory note impliedly or expressly governed by California law, regardless of the security situs. In any such situation, California legitimately may assert a governmental interest in applying sections 726 and 580b. Conversely, in foreign contracts without connection to California, again without regard to the security situs, California should not assert an interest in applying either section 726 or section 580b.

With respect to sections 580d and the fair-value requirements, California's legitimate governmental interest is invoked any time California real property is hypothecated. The policies underlying the statutes are designed to protect California landowners/hypothecators, regardless of whether foreign law governs the promissory note. Conversely, California has no significant governmental interest in applying section 580d or the fair-value requirements when foreign security is being foreclosed, even when California law governs the promissory note.

It is hoped that this Comment will further the use of governmental interest analysis in the field of real-property security conflicts cases. Other conflicts issues relating to California's antideficiency statutes inevitably will arise.<sup>323</sup> Governmental interest analysis offers a means for

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320. Traynor, *War and Peace*, *supra* note 46, at 121 (footnote omitted).

321. 700 F.2d 476 (9th Cir. 1982).

322. 147 Cal. App. 3d 225, 195 Cal. Rptr. 53 (1983).

323. It is questionable whether third-party purchase-money lenders in foreign owner-occupied

principled resolutions of such future controversies.

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residential property transactions should be barred from a deficiency judgment by § 580b. *See supra* note 212.

Complex antideficiency problems will also arise in multiple security situations where both California and foreign real property secure a debt. For example, California's internal rule allows piecemeal nonjudicial foreclosures of multiple security interests but considers that § 580d voids the creditor's deficiency rights after the completion of the first nonjudicial sale. *Hatch v. Security-First Nat'l Bank*, 19 Cal. 2d 254, 120 P.2d 869 (1942). The judicially developed internal rule will conflict with other states' laws that allow piecemeal nonjudicial foreclosures in addition to deficiency rights. If the creditor first forecloses on the California property, any deficiency right should probably be barred, although the creditor would be allowed to foreclose the foreign security interests. In other words, to obtain deficiency rights, the creditor would be required to foreclose judicially in California. However, it could be argued that California has a mitigated governmental interest in imposing § 580d in the multiple foreign and domestic security context when its internal foreclosure scheme must be integrated with a foreign foreclosure scheme since property is located in both states. Such an argument could be furthered by applying the § 580a fair-value requirements to the California property foreclosure, perhaps adequately protecting the debtor without the operation of § 580d.

Also, § 726 will be involved in the multiple domestic and foreign security transactions. For example, if the promissory note were governed by California law so that § 726 were operative, and the creditor first judicially foreclosed the foreign property and thereby obtained a money (deficiency) judgment, it could be argued that the § 726 one-action sanction should be imposed to disallow the foreclosure of the California security interest. This is a context in which a California court will first be forced to define the parameters of the primary-fund policy as herein defined. Although the single-action policy would be inoperative due to the necessity of multiple actions, the one-action sanction might be appropriate to enforce the primary-fund policy. *See supra* note 134. The question is what event should trigger the sanction. Acquisition of the foreign money judgment should not trigger the sanction. Neither should the encumbering of nonprimary-fund assets be allowed to trigger the one-action sanction. Such an encumbrance might more fairly be reversed (in effect an affirmative defense to an attempted violation of the primary-fund policy). Actual execution on nonprimary-fund assets, however, would require imposition of the one-action sanction under the reasoning in *Bank of Am. v. Daily*, 152 Cal. App. 3d 769, 199 Cal. Rptr. 557 (1984). *See supra* note 134.

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