

What Is An *Action* For Purposes Of California Civil Procedure Code Section 726?

In the 1984 case, Bank of America v. Daily,¹ the California Court of Appeal held that a bank's setoff was an action for purposes of California Civil Procedure Code section 726 (the one action rule). The bank lost over \$170,000 in security due to this \$10,000. California courts have circumvented the policies behind section 726 by interpreting the one action rule expansively. This Comment argues that debtor protection is not achieved through inequitable creditor remedies and that legislative reform is necessary to achieve the protection that section 726 intended to provide California debtors.

I. INTRODUCTION

A debtor owed a bank \$340,000 as evidenced by a note secured by common stock and a deed of trust on real property. When the debtor defaulted on the note, the bank sold the stock, setoff² \$10,412.50 from a checking account which the debtor held with the bank, and then initiated a judicial foreclosure sale under the deed of trust to collect the remaining balance.³ The California court of appeal held that the bank's setoff was an action⁴ for recovery of a debt within the meaning of California Civil Procedure Code section 726⁵ (one

1. 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984).

2. See *infra* note 85 and accompanying text.

3. Bank of America v. Daily, 152 Cal. App. 3d 767, 770, 199 Cal. Rptr. 557, 558 (1984).

4. The term "action" hereinafter refers to an action for purposes of California Civil Procedure Code section 726, otherwise known as the "one action rule."

5. *Daily*, 152 Cal. App. 3d at 772-73, 199 Cal. Rptr. at 559-60. The California Code of Civil Procedure discusses the one action rule in section 726:

There can be but one form of action for the recovery of any debt, or the enforcement of any right secured by mortgage upon real property, which action must be in accordance with the provisions of this chapter. In such action the court may, by its judgment, direct the sale of the encumbered property (or so much thereof as may be necessary), and the application of the proceeds of the sale to the payment of the costs of court, and the expenses of the sale, and the amount due plaintiff, including, where the mortgage provides for the payment of attorney's fees, such sum for such fees as the court shall find reasonable, not exceeding the amount named in the mortgage.

action rule), and that the bank waived its right to judicial foreclosure. Thus, the bank lost approximately \$170,000 of remaining security on a note due to a \$10,000 setoff.

The one action rule was promulgated as an attempt to protect debtor interests.⁶ California courts have interpreted the one action rule expansively, protecting the debtor and, at the same time, imposing harsh sanctions on the creditor.⁷ This problem arises in part from the nebulous definition of the term "action." Once a court decides that certain conduct is an action, that single action constitutes the creditor's sole source of relief, precluding additional recovery from the debtor.⁸ Courts are thus unsure of application of section 726 and are hesitant to qualify conduct as an action.⁹

Some commentators,¹⁰ argue that the term action should be consistent with the definition of action within California Civil Procedure Code section 22 which seems to contemplate only judicial proceedings.¹¹ But courts have interpreted an action for purpose of section 726 to include some non-judicial activities¹² and exclude some judicial activities.¹³ An action for purposes of section 726 should be redefined to effectuate the policies behind the one action rule as well as to allow creditor recovery.

This Comment will first discuss the historical background of deeds of trust. Furthermore, the Comment will analyze and suggest solutions for California's expansive interpretation of section 726. The Comment will conclude that the definition of an action as stipulated in section 22 should be read into section 726. Additionally, this Comment will discuss the policy reasons which compel the creditor

CAL. CIV. PROC. CODE § 726(a) (West 1980 & Supp. 1987) [hereinafter One-Action Rule].

6. *Pacific Valley Bank v. Schwenke*, 189 Cal. App. 3d 134, 141-42, 234 Cal. Rptr. 298, 302 (1987), (citing *Salter v. Ulrich*, 22 Cal. 2d 263, 266, 138 P.2d 7, 9 (1943)).

7. Arnold, *Anti-Deficiency in the Eighties: The "Sanction Aspect," Fair Value and Where the Action Is (And Isn't)*, 5 CAL. REAL PROP. J. Spring 1987, at 1.

8. *Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557. However, a deficiency judgment may be recovered after a judicial foreclosure sale has failed to satisfy the debt. *Winkleman v. Sides*, 31 Cal. App. 2d 387, 406, 88 P.2d 147, 156 (1939) (citing *Birkhofer v. Krumm*, 4 Cal. App. 2d 43, 40 P.2d 553 (1935)).

9. See, e.g., *Schwenke*, 189 Cal. App. 3d at 141-42, 234 Cal. Rptr. at 302. The court of appeal held that the lender's unilateral divestiture of collateral violated section 726. However, the court stated that this "release of security needn't be characterized as an 'action.'" *Id.*

10. See, e.g., Mertens, *California's Foreclosure Statutes: Some Proposals for Reform*, 26 SANTA CLARA L. REV. 533, 577-79 (1986); Arnold, *supra* note 7, at 10.

11. Section 22 states that an action is "an ordinary proceeding in a court of justice by which one party prosecutes another for the declaration, enforcement, or protection of a right, the redress or protection of a wrong, or the punishment of a public offense." CAL. CIV. PROC. CODE § 22 (West 1980 & Supp. 1987). See also Arnold, *supra* note 7, at 10.

12. See *infra* notes 83-104 and accompanying text.

13. See *infra* notes 105-113 and accompanying text.

to foreclose on the secured property before reaching the debtor's other assets. The remedy proposed by this Comment sanctions a creditor who fails to first foreclose on the security by disallowing the creditor to obtain a personal judgment on the underlying debt. Instead, the creditor would be forced to first foreclose on the security.¹⁴

II. BACKGROUND-REAL ESTATE FINANCING DEVICES

Most real property purchases are financed.¹⁵ Generally, the purchaser borrows an amount in excess of the down payment from the seller or a third party lender. The mortgage is the traditional security instrument used in real estate secured transactions. However, in California the deed of trust is the preferred security instrument.¹⁶ The deed of trust is treated as a mortgage because it performs the same economic function.¹⁷ The remaining differences between these instruments are the number and designation of the parties¹⁸ and the statute of limitations period regarding the power of sale.¹⁹

Throughout its history, mortgage law attempted to reach equitable results by balancing the interests of the mortgagor and mortgagee. Nevertheless, courts, legislatures and legal draftsmen have not accomplished this goal. The creditor or debtor have each received favorable treatment, depending upon which group's problems are perceived as more pressing at the time.²⁰

At early common law, title theory was in effect. Under this doctrine, title passed to the creditor. If the debtor did not pay the obligation when due, a forfeiture took place.²¹ The debtor had no prop-

14. This "sanction" was raised but not imposed by the court. *Daily*, 152 Cal. App. 3d at 772, 199 Cal. Rptr. at 559.

15. Mertens, *supra* note 10, at 536-47.

16. A. PERRY, CALIFORNIA CASES AND MATERIALS ON SECURED LAND FINANCING 111 (rev. 1984).

17. *Bank of Italy Nat'l Trust & Sav. Ass'n v. Bentley*, 217 Cal. 644, 657 20 P.2d 940, 945 (1933).

18. The parties to a mortgage are mortgagor (debtor or obligor) and mortgagee (creditor or obligee) whereas the parties to a deed of trust are trustor (debtor or obligor), beneficiary (creditor or obligee) and trustee (usually a bank or title insurance company, or escrow company). For purposes of this Comment, the terms creditor, debtor and trustee will be used to denote the above-mentioned parties. A. PERRY, *supra* note 16. The trustee in a deed of trust retains the title and also has power to foreclose on the security. *See Bank of Italy*, 217 Cal. at 655-656, 20 P.2d at 944-945.

19. The statute of limitations does not run against a deed of trust but does run against a mortgage. *Bank of Italy*, 217 Cal. at 655, 20 P.2d at 944.

20. G. THOMPSON, 3 COMMENTARIES ON THE MODERN LAW OF REAL PROPERTY 693 (1958).

21. *Bank of Italy*, 217 Cal. at 654, 20 P.2d at 943.

erty interest until he paid the debt in full.²² Later, equitable relief was granted for those debtors who tendered the amount due on the debt owed within a reasonable amount of time.²³ Although California initially adopted a lien theory²⁴ for mortgages whereby the creditors obtain a lien only, it adopted a title theory in reference to deeds of trust.²⁵ Today, both instruments have the same effect on titles.²⁶ A standard deed of trust includes a grant of property to a named trustee in trust for the benefit of a named creditor, coupled with a trustee's power of sale in the event of the debtor's default.²⁷ These trustee sales are one kind of foreclosure sale.²⁸ Although foreclosure

22. In 14th century England, the dominant form of a mortgage was the conveyance of the fee to the mortgagee upon the condition subsequent that if the mortgagor paid in full, on or before the due date (law day), he regained his estate. The mortgagor retained only a right of entry. No excuse existed for late payment. If the mortgagor failed to perform then the title absolutely vested in the mortgagee and the mortgagor irrevocably lost his land. G. NELSON & D. WHITMAN, *REAL ESTATE FINANCE LAW* §§ 1-2, at 6-8 (1985).

23. At first, relief was granted based on a special showing of fraud or oppression. By the end of the 17th century, equity courts routinely intervened and provided for equitable redemption. All mortgagors could redeem their land by tendering the amount due within a reasonable time after law day.

By granting relief to mortgagors, equitable redemption created new problems for mortgagees. Mortgagees were uncertain as to when redemption might occur because the mortgagor was permitted a reasonable time within which to redeem the property. Eventually, equity allowed mortgagees to petition for foreclosure and terminate the mortgagor's right to redeem the property. Common law transfer of title essentially left the mortgagor with a right of entry plus equitable protections. Even when the mortgagor remained in possession, he had no legal estate in the land and he could be ejected by the mortgagee, even prior to default. G. OSBORNE, *MORTGAGES* §§ 5-8 at 9-17 (1970).

24. The lien theory evolved in recognition of the commercial nature of the mortgage and the unjust results which emanated from the title theory of mortgages. Under the lien theory, the mortgagee only has a lien with the legal title held by the mortgagor. See 3 R. POWELL & P. ROHAN, *POWELL ON REAL PROPERTY* ch. 37, ¶ 454.1[2] (1987).

25. *Bank of Italy*, 217 Cal. at 655, 201 P.2d at 944.

26. *Id.* at 657, 20 P.2d at 945.

27. A. PERRY, *supra* note 16, at 118.

28. Foreclosure by sale takes two forms. First, a judicial sale may be conducted by an officer of the court. Alternatively, a power of sale may be conferred on the mortgagee by the mortgagor. Many states permitting mortgages to contain a power of sale clause provide that the creditors may sell the property without a judicial proceeding. This is referred to as a private sale.

The fundamentals are the same in both the judicial and private sale. The mortgaged property is sold under certain safeguards to ensure fair conduct, and the proceeds are used to pay the expenses of the proceedings and the claim of the creditor. Any surplus goes to the debtor. If the proceeds are insufficient to pay the mortgage claim, the creditor may obtain a judgment for the deficiency. See generally Washburn, *The Judicial and Legislative Response to Price Monopoly in Mortgage Foreclosure Sales*, 53 S. CAL. L. REV. 843, 844-51 (1980). California bars the creditor from obtaining a deficiency judgment after a private sale (non-judicial foreclosure). CAL. CIV. PROC. CODE § 580(d) (West 1976 & Supp. 1988). See also *infra* note 33 and accompanying text.

Hence, foreclosure by sale protects the debtor's equity in the property yet allows the mortgagee to recover a deficiency judgment when proceeds of the sale are insufficient to pay the mortgage debt. A judicial sale differs from a private sale in this respect. Theoretically, a price equivalent to the property's market value is determined through the competitive bidding process. Moreover, the court ensures that the sale is at a fair price. See

sales theoretically assume a price equivalent to market value, such sales have actually been ineffective in achieving this goal.²⁹

State legislatures responded to these problems by providing more effective relief for mortgagors through the enactment of a wide variety of anti-deficiency laws.³⁰ These laws protect debtors from foreclosure sales at depressed prices and deficiency judgments measured by those prices.³¹ The California legislature enacted the fair value provisions,³² the anti-deficiency protection,³³ and the one action

Washburn, at 846.

In California, fair value is achieved through procedures under the California Code of Civil Procedure. CAL. CIV. PROC. CODE § 580(a)(West 1976 and Supp. 1988) and CAL. CIV. PROC. CODE § 726(b)(West 1980 & Supp. 1988) (fair value provisions). *See also infra* note 32 and accompanying text.

29. The economic depression of the 1930's emphasized the public's willingness to pay only bargain prices at foreclosure sales. Properties regularly sold for nominal amounts at foreclosure sales. Furthermore, the creditor could purchase the property at a sub-market price and simultaneously obtain a deficiency judgment for the difference between the price the property sold for and the amount of the mortgage debt. The result was double recovery for the creditor and a double burden to the debtor who had to lose the property and pay a deficiency judgment. *See generally* Washburn, *supra* note 28, at 843-50; *see also* G. OSBORNE, *supra* note 23, at 702.

30. G. OSBORNE, *supra* note 23, § 335, at 702-05.

31. *Id.*

32. CAL. CIV. PROC. CODE § 580(a) requiring a fair value hearing and limitation, provides in pertinent part:

The court may render judgment for not more than the amount by which the entire amount of the indebtedness due at the time of sale exceeded the fair market value of the real property or interest therein sold at the time of sale with interest thereon from the date of the sale; provided, however, that in no event shall the amount of said judgment, exclusive of interest after the date of sale, exceed the difference between the amount for which the property was sold and the entire amount of the indebtedness secured by said deed of trust or mortgage.

CAL. CIV. PROC. CODE § 580(a) (West 1976 & Supp. 1988).

CAL. CIV. PROC. CODE § 726(b) limits a deficiency judgment to: ". . . the amount of the indebtedness . . . exceeds the fair value of the property . . . as of the date of sale. In no event shall the amount of the judgment . . . exceed the difference between the amount for which the property was sold and the entire amount of the indebtedness . . ." CAL. CIV. PROC. CODE § 726(b) (West 1980 & Supp. 1988).

Sections 580(a) and 726(b) limit the size of the deficiency judgment to either (1) the difference between the unpaid debt and the fair value of the security, or (2) the difference between the debt and the sale price of the security, whichever is smaller. The one action rule, the focus of this Comment, precludes the creditor from avoiding the restrictions of the fair value provisions. Without section 726, the creditor could merely file an action on the note, obtain a personal judgment, and then foreclose on the secured property. However, because the one action rule forces secured creditors to foreclose, the rule also forces them into a fair value hearing whenever they seek more than the value of their security. *See generally* R. BERNHARDT, CALIFORNIA MORTGAGE AND DEED OF TRUST PRACTICE §§ 4.15-4.19, (1979 & Supp. June 1987).

33. CAL. CIV. PROC. CODE § 580(d) provides:

No judgment shall be rendered for any deficiency upon a note secured by a

rule³⁴ to regulate creditor remedies. However, the statutes are not part of any comprehensive plan.³⁵ Meanwhile, the courts have filled the legislative gaps, often interpreting these statutes in ways which are contrary to their intended purposes.

III. CALIFORNIA'S ONE ACTION RULE

A. History of the One Action Rule

The one action rule³⁶ embodies the central axiom of the real property system in the state of California.³⁷ The policies and philosophy of real property provisions are most readily discernible from this section.³⁸ The one action rule begins: "There can be but one form of action for the recovery of any debt or the enforcement of any right secured by a mortgage upon real property."³⁹ This section is contro-

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 contained in such mortgage or deed of trust.

The provisions of this section shall not apply to any deed of trust, mortgage or other lien given to secure the payment of bonds or other evidences of indebtedness authorized or permitted to be issued by the Commissioner of Corporations, or which is made by a public utility subject to the provisions of the Public Utilities Act.

CAL. CIV. PROC. CODE § 580(d) (West 1976 & Supp. 1988).

This section imposes a complete bar against any deficiency judgment when the creditor has elected to foreclose by power of sale rather than judicially. If the foreclosure sale proceeds, there is no further recovery. See R. BERNHARDT, *supra* note 32 §§ 4.13-4.15.

CAL. CIV. PROC. CODE § 580(b) states:

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

Where both a chattel mortgage and a deed of trust or mortgage have been given to secure payment of the balance of the combined purchase price of both real and personal property, no deficiency judgment shall lie at any time under any one thereof if no deficiency judgment would lie under the deed of trust or mortgage on real property.

CAL. CIV. PROC. CODE § 580(b) (West 1976 & Supp. 1988).

The basic rule of section 580(b) precludes deficiency judgments when purchase money security is involved (money loaned by the seller to the purchaser, or if loaned by a third party, money used to pay all or part of the purchase price of a dwelling of not more than four units occupied entirely or in part by the purchaser). See R. BERNHARDT, *supra* note 32, at §§ 4.20-4.23.

34. See One Action Rule, *supra* note 5.

35. See R. BERNHARDT, *supra* note 32, at § 4.1.

36. See One Action Rule, *supra* note 5.

37. Hetland & Hansen, *The "Mixed Collateral" Amendments to California's Commercial Code — Covert Repeal of California's Real Property Foreclosure and Antideficiency Provisions or Exercise in Futility?*, 75 CALIF. L. REV. 185, 199 (1987).

38. *Id.*

39. See One Action Rule, *supra* note 5.

versial and provides the greatest potential for harm to a creditor.⁴⁰

The one action rule traces its roots to the proposed New York Code of Civil Procedure of 1850.⁴¹ This provision was never specifically enacted in California but was incorporated into section 246 of the Civil Practice Act through an 1860 amendment.⁴² The proposed New York code section never became law in that state nor in any other state deriving their laws from the New York Civil Code.⁴³ The one action rule exists in several states today.⁴⁴ However, the rule in these states is patterned after California law rather than that of New York.⁴⁵ California's one action rule has not changed materially in the one hundred years it has been in force,⁴⁶ even though a 1933 amendment to section 726 changed the first sentence from one action to one form of action.⁴⁷

B. Purpose and Effect of the One Action Rule

Much of the confusion regarding the one action rule may be ascribed to the failure of the courts to distinguish between its purpose and its effect. The one action rule appears to have been adopted with the purpose of avoiding multiple actions against a debtor.⁴⁸ The express purpose of section 905 of the New York Code of Civil Procedure of 1850, from which section 726 originated, was to prevent a multiplicity of actions arising under common law.⁴⁹

40. *Bank of America v. Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984) (if the creditor chooses to foreclose or setoff property and the court views this activity as an *action*, the creditor is precluded from further recovery, whether the *action* satisfies the debt or not). See *supra* text accompanying notes 1-5.

41. Comment, *Mortgages and Trust Deeds: Enforcement of a Secured Debt in California*, 31 CALIF. L. REV. 429, 430 (1943).

42. *Id.* at 429.

43. *Id.* at 430.

44. IDAHO CODE § 6-101 (1979 & Supp. 1987); MONT. CODE ANN. § 71-1-222 (1987); N.J. STAT. § 2A:50-2 (1952 & Supp. 1987); NEV. REV. STAT. § 40.430 (1986); UTAH CODE ANN. § 78-37-1 (1987).

45. See Comment, *supra* note 41, at 430.

46. See Comment, *Mortgages and Trust Deeds: Foreclosure Sale of a Portion of the Mortgaged Premises: Remedies Open to the Mortgagee When the Security is Valueless: Pleading the Existence of Security*, 25 CALIF. L. REV. 469, 470 (1937).

47. *Id.*

48. *Bank of Italy Nat'l Trust & Sav. Ass'n v. Bentley*, 217 Cal. 644, 20 P.2d 940 (1933); *Felton v. West*, 102 Cal. 266, 36 P. 676 (1894); *Ould v. Stoddard*, 54 Cal. 613 (1880).

49. At common law the creditor had a choice of three actions which he could bring against the debtor in case of debtor default. The creditor could sue on the note, foreclose the mortgage, or bring an action of ejectment. These actions could be brought separately or concurrently. See Comment, *supra* note 41, at 430 n.8. The proposed New York Civil Code of 1850 allowed the creditor to sue on the underlying note or on the

By contrast, California and other states⁵⁰ enacting California's one action rule require the creditor to foreclose on the secured property before undertaking any other method of recovering on the debt.⁵¹ A creditor may only recover from a debtor's personal estate by first foreclosing on the property and then recovering a deficiency judgment for the difference between the amount due on the note and the proceeds from the sale of the property.⁵² Effectively, the security becomes the primary fund from which the debt is satisfied. The security must be exhausted before the creditor recovers on the underlying obligation. Thus, section 726 is a security first rule, as well as a one action rule.⁵³

The courts have considered the effect of the statute as an expression of legislative purpose and policy, and as a consequence, it has become a settled rule of judicial construction in California that where a debt is secured by real property the security must first be exhausted.⁵⁴ A California debtor is not unconditionally promising to pay on the underlying note. Instead, the trustor is promising to render the secured property to the creditor in case of default, and then pay to the creditor any deficiency judgment remaining after the sale of the encumbered property.⁵⁵

Multiplicity of suits is avoided under the choice of remedies doctrine of the proposed New York Code as well as the security first principle of California's one action rule. However, the legislative history behind the enactment of the one action rule signifies the legislature's concern for the debtor's inability to bargain effectively for his or her rights in a loan transaction, and to prevent the sale of real property security at below market prices.⁵⁶ Additionally, if the creditor secures real property for the underlying note, this security should be exhausted so that the debtor is not burdened even further when

security, but the mortgagee was precluded from recovery under both. Thus, the New York one action principle would have limited the mortgagor to one remedy of his choice. See R. BERNHARDT, *supra* note 32, at § 4.3.

50. See statutes cited *supra* note 44.

51. *Winklemen v. Sides*, 31 Cal. App. 2d 387, 88 P.2d 147 (1939); *Porter v. Muller*, 65 Cal. 512, 4 P. 531 (1884); *Jeppesen v. Rexburg State Bank*, 57 Idaho 94, 99, 62 P.2d 1369, 1371 (1936); *Thirteenth Ave., Ltd. v. De Marco*, 44 N.J. 525, 529, 210 A.2d 401, 403 (1965); *Bank of Ephraim v. Davis*, 581 P.2d 1001 (Utah 1978); *Boucofski v. Jacobsen*, 36 Utah 165, 104 P. 117 (1909); *Jensen v. Lichtensen*, 45 Utah 320, 145 P. 1036 (1915).

52. *Id.*

53. See R. BERNHARDT *supra* note 32, at § 4.3.

54. See Comment, *supra* note 41, at 431.

55. *Otto v. Long*, 127 Cal. 471, 59 P. 895 (1900); *Commercial Bank v. Kershner*, 120 Cal. 495, 52 P. 848 (1898).

56. *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974) (Section 726 was intended to prevent a multiplicity of actions, to compel exhaustion of all security before entry of a deficiency judgment, and to require the debtor to be credited with the fair market value of the secured property before being subjected to personal liability).

experiencing financial hardship.⁵⁷ These policies are not effectuated by the choice of remedies doctrine because the creditor could collect on the underlying note even when he took a security interest in the real property, leaving the financially troubled debtor in an even more precarious position.

Although the creditor is confined to one remedy, the scope of this remedy is expanded under the one action rule to provide the creditor with more comprehensive relief than was previously available at common law. At common law, the creditor was required to file separate actions when seeking a deficiency judgment. Under California's one action rule, the creditor may have both a foreclosure and a deficiency judgment in the same action.⁵⁸

Most significantly, the one action rule impacts the creditor's recovery of a deficiency judgment. Without section 726, a secured creditor could avoid most of the limitations on deficiency judgments by obtaining a judgment on the note, and then foreclosing on the property. The one action rule bars this result. Instead of trying to recover first on the note or on personal property, and then foreclosing on the security, the mortgagee must first foreclose on the secured property and then recover a deficiency judgment for the difference between the fair market value sales price and debt obligation.

C. *Exceptions to the One Action Rule*

The courts have developed exceptions to the one action rule, thus permitting the creditor to proceed directly on the note in certain circumstances. Such exceptions include situations where the security has become valueless through economic decline,⁵⁹ the property has been physically destroyed,⁶⁰ the security has become exhausted as a result of a sale pursuant to a senior encumbrance,⁶¹ the subject property is nonexistent,⁶² or the subject property cannot be encumbered by the debtors.⁶³ Hence, the exceptions only apply if the property is

57. *Id.*

58. *Felton v. West*, 102 Cal. 266, 36 P. 676 (1894); *Ould v. Stoddard*, 54 Cal. 613 (1880).

59. *Barbieri v. Ramelli*, 84 Cal. 154, 23 P. 1086 (1890) (Unless the security is totally lost or otherwise without value, the creditor must exhaust it).

60. *Cohen v. Marshall*, 197 Cal. 117, 239 P. 1050 (1925).

61. *Roseleaf v. Chierighino*, 59 Cal. 2d 35, 378 P.2d 97, 27 Cal. Rptr. 873 (1963); *Savings Bank v. Central Market Co.*, 122 Cal. 28, 54 P. 273 (1898); *but cf. Brown v. Jensen*, 41 Cal. 2d 193, 259 P.2d 425 (1953).

62. *Dyer Law & Collection Co. v. Abbot*, 52 Cal. App. 545, 199 P. 340 (1921).

63. *Curtin v. Salmon River Hydraulic Gold Mining & Ditch Co.*, 141 Cal. 308, 74 P. 851 (1903).

subsequently worthless and proceeding against the security first would be meaningless. Yet, if the property was originally valueless and has not changed in value, the creditor is still forced to proceed against the security first.⁶⁴

D. *Waiver of the One Action Rule*

Rights under the one action rule may in certain circumstances be waived. California Civil Code section 2953⁶⁵ expressly invalidates waivers of the benefits conferred by California Civil Procedure Code sections 580(a) and 726, if the waivers were agreed upon at the time of making or renewing a loan secured by a mortgage or deed of trust on real property.⁶⁶ Although this statute does not specifically address other sections of the anti-deficiency rules, this prohibition against waivers is said to apply to all. Whether the waiver is valid is determined by when the waiver is made, who made it, and in some cases, how it is made.⁶⁷

The courts refuse to allow the borrower to waive his mortgage rights at the time of making his loan because the courts view a necessitous borrower as willing to waive all of his rights in order to obtain a loan.⁶⁸ However, waivers subsequent to default are permitted.⁶⁹

E. *The Affirmative Defense and Sanction Aspects of the One Action Rule*

Under the one action rule, the debtor has two ways to challenge the creditor who fails to foreclose on the secured property. Section 726 may be raised as an affirmative defense⁷⁰ or as a sanction.⁷¹ When the debtor raises section 726 as an affirmative defense in a judicial foreclosure action, the creditor is forced to foreclose on all of the security first.⁷² This, however, does not preclude the creditor

64. Kendall, *Effect of the One Action Rule on Real Property Security Interests*, 44 L.A. B. BULL. 116, 119 (1969).

65. CAL. CIV. CODE § 2953 (West 1980 & Supp. 1988).

66. Riesenfeld, *California Legislation Curbing Deficiency Judgments*, 48 CALIF. L. REV. 705, 721 (1960).

67. R. BERNHARDT, *supra* note 32, § 4.63, at 191.

68. *See* Salter v. Ulrich, 22 Cal. 2d 263, 267, 138 P.2d 7, 9 (1943).

69. *Id.* at 267, 138 P.2d at 9 (Since necessity often drives debtors to make ruinous concessions when a loan is needed, section 726 should be applied to protect them and prevent a waiver in advance. This reasoning, however, does not apply after the loan is made, when all rights have been established and there remains only the enforcement of those rights).

70. *Id.* at 263, 138 P.2d at 7.

71. *See* Walker v. Community Bank, 10 Cal. 3d 729, 735-36, 518 P.2d 329, 333, 111 Cal. Rptr. 897, 901 (1974).

72. *See* Salter, 22 Cal. 2d at 263, 138 P.2d at 7; Barbieri v. Ramelli, 84 Cal. 154, 23 P. 1086 (1890). *See also* *In re* Kristad, 758 F.2d 454 (9th Cir. 1985).

from obtaining a deficiency judgment following the sale.⁷³

If the debtor does not raise the statute as an affirmative defense, the debtor may still invoke the statute as a sanction. The debtor raises the sanction effect on the basis that by not foreclosing on the security in the action to enforce the debt, the creditor has elected the remedy, thus waiving the security.⁷⁴

This sanction effect is based on the policies evident in the language of the statute. These rationales include the avoidance of successive actions arising out of the same transaction as well as an election of remedies for the creditor.⁷⁵ A creditor is deemed to have made an election at the time he obtains a judgment on the note because he chose to recover a personal judgment instead of resorting to the security for satisfaction of the debt.⁷⁶ However, some commentators argue that it is more accurate to say the debtor makes the election because the debtor can choose whether or not to raise section 726 as an affirmative defense.⁷⁷

The effect of both the affirmative defense and sanction aspects are devastating to the creditor's interests if the debt is secured by more than one item of collateral and the lender does not include the entire security in the one foreclosure action allowed by section 726. The affirmative defense aspect of section 726 would preclude an attempt to collect the balance of the debt without exhausting the security; the sanction aspect prevents the lender from relying on additional security after the foreclosure decree.⁷⁸

IV. JUDICIAL INTERPRETATION OF AN ACTION UNDER THE ONE ACTION RULE

The California courts have consistently construed the one action rule as requiring the exhaustion of any real property security prior to permitting personal recovery from the debtor's unsecured assets. This expansive construction of the one action rule may carry out the

73. Mertens, *supra* note 10, at 554, n.2. *But cf.* J. HETLAND, CALIFORNIA REAL ESTATE SECURED TRANSACTIONS § 6.18, at 257-58 (1970) (cited in *Walker*, 10 Cal. 3d at 733, n.2, 518 P.2d at 331-32, n.2, 111 Cal. Rptr. at 899-900, n.2 (Professor Hetland said the creditor is not entitled to a deficiency)).

74. *Walker*, 10 Cal. 3d at 734, 518 P.2d at 331, 111 Cal. Rptr. at 899; *Ould v. Stoddard*, 54 Cal. 613, 614 (1880).

75. Leipziger, *Deficiency Judgments in California: The Supreme Court Tries Again*, 22 UCLA L. REV. 753, 788 (1975).

76. *See, e.g., Salter*, 22 Cal. 2d at 263, 138 P.2d at 7.

77. Leipziger, *supra* note 75, at 788.

78. *Id.* at 789.

intended purpose of section 726, but many times produces unjust results for the creditor.⁷⁹ This problem may be partially attributed to the fact that no precise definition of an action is ascertainable. Thus, the courts look to the policies⁸⁰ behind section 726 and find for the debtor. However, the policies behind the one action rule do not promote inequitable treatment for the creditor. California Civil Procedure Code section 22 should be read into section 726. This would give the courts guidance in applying section 726 and achieving the rule's purposes. The language of section 22 suggests that judicial proceedings constitute actions. However, courts have interpreted an action for purposes of section 726 to include some non-judicial activity and exclude some judicial activity.

*A. Non-Judicial Activity not an Action
for Purposes of Section 726*

In *Hatch v. Security First National Bank*,⁸¹ the debtors asserted that section 726 was triggered by a non-judicial foreclosure. Accordingly, the trial court held that the creditor waived his right to exhaust the additional security. The California Supreme Court reversed the trial court's decision, stating that successive piecemeal extrajudicial foreclosure sales in multiple security cases are allowed.⁸²

*B. Non-Judicial Activity as an Action
for Purposes of Section 726*

Although *Hatch* equates judicial activity with action for purposes of section 726, other cases view non-judicial endeavors as constituting an action under the one action rule.⁸³ The California Supreme Court in *McKean v. German-American Savings Bank*,⁸⁴ held that the one action rule barred the creditor from effecting a setoff to a debt secured by a mortgage. The court recognized that the underlying setoff⁸⁵ was not an action in the classical sense. However, under

79. See, e.g., *Bank of America v. Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984).

80. See *supra* note 56-57 and accompanying text.

81. 19 Cal. 2d 254, 120 P.2d 869 (1942).

82. *Id.* at 258, 120 P.2d, at 872.

83. *McKean v. German-American Savings Bank*, 118 Cal. 334, 50 P. 656 (1897); *Gnarni v. Swiss-American Savings Bank*, 162 Cal. 181, 121 P. 726 (1912); *Woodruff v. California Republic Bank*, 75 Cal. App. 3d 108, 141 Cal. Rptr. 915 (1977); *Daily*, 151 Cal. App. 3d at 767, 199 Cal. Rptr. at 557 (In *McKean*, *Gnarni* & *Woodruff*, the setoffs were filed judicially. The conduct (setoff) was considered nonjudicial even though judicial proceedings were undertaken). See *Arnold*, *supra* note 7, at 10.

84. 118 Cal. 334, 50 P. 656 (1897).

85. The exercise of a bank's right to apply its depositor's funds to the payment of a debt (the underlying note in the mortgage transaction) owed by the depositor. See

section 726 the mortgaged premises constituted the primary fund out of which the debt must be paid. Thus, the security had to be exhausted first.⁸⁶

In *Gnarni v. Swiss-American Savings Bank*,⁸⁷ the California Supreme Court relied on *McKean* and held that the one action rule barred a setoff because it required that all security be exhausted before a personal action may be instigated against the debtor or property of the debtor, such as the bank account. In *Gnarni*, the court did not explicitly term this conduct an action for purposes of section 726. However, the court determined that the setoff ran counter to the one action rule.⁸⁸ Thus, the court imposed the sanction aspect, precluding the bank from foreclosing on the secured property.⁸⁹ The *Gnarni* decision was affirmed in *Woodruff v. California Republic Bank*,⁹⁰ which held that a setoff of a bank account against a debt secured by a deed of trust on real property was precluded by the one action rule.⁹¹

More recently, *Bank of America v. Daily*,⁹² held that a setoff constituted an action within the meaning of the one action rule.⁹³ Commentators contend that *Daily* promotes the policy of section 726, but the court's rationale raises questions as to whether the correct deci-

Annotation, *Post-Sniadach Status of a Banker's Right to Setoff Bank's Claim Against Depositor's Funds*, 65 A.L.R. 3d 1284 (1975); see, e.g., *Daily*, 152 Cal. App. 3d at 767, 199 Cal. Rptr. at 557, where debtor was also a bank depositor. When debtor defaulted on the note, bank setoff (applied the funds of the checking account toward the payment of the defaulted note) approximately \$10,000 from debtor's checking account and then attempted to foreclose on the property secured by the deed of trust.

86. *McKean* 118 Cal. at 339-40, 50 P. at 659.

87. 162 Cal. 181, 121 P. 726 (1912).

88. *Id.* at 184, 121 P. at 728.

89. *Id.*

90. 75 Cal. App. 3d 108, 141 Cal. Rptr. 915 (1977).

91. *Id.*

92. 151 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984).

93. In 1966, Daily owed the Bank of America \$340,000 evidenced by a note secured by common stock. The stock declined in value and the bank subsequently requested that Daily provide additional collateral. Daily then gave a deed of trust on his interest in real property as security and subsequently defaulted on the note. The bank initiated several proceedings to collect the balance due on the note. First, the bank sold the pledged stock at a private sale. Secondly, the bank setoff \$10,412.50 from a checking account that Daily had with the bank. Finally, the bank undertook judicial foreclosure proceedings on the deed of trust. Daily opposed the foreclosure sale by contending that the bank already had its one action under section 726 by setting off funds from the checking account and that by virtue of the sanction, the bank effectively waived the balance of its security. The appellate court, reversing the trial court, held that a setoff constituted an "action" under section 726. Further, the court imposed the "sanction" aspect of section 726 stating that the Bank waived its right to a foreclosure proceeding because the bank already had its "action" by the setoff.

sion was reached.⁹⁴ The court in *Daily* held that a non-judicial exercise of a setoff is an action for purposes of section 726. But a setoff is not an action in any traditional sense, because it involves neither court proceeding nor judicial decree.⁹⁵ Moreover, *Daily* creates confusion in other areas of the law. For example, if a setoff is determined to be an action, it is logical that a nonjudicial sale be considered an action also. Under *Hatch v. Security First National Bank*,⁹⁶ a creditor may non-judicially foreclose on several parcels he or she holds as security. Both the non-judicial foreclosure sale and the setoff are not actions in any traditional sense. If courts hold setoffs as actions, this could logically lead to a reversal of *Hatch*, which held that a non-judicial foreclosure sale was not an action.⁹⁷

The sanctions which *Daily* imposed are even more troubling than the characterization of the setoff as an action. Because section 726 requires a secured creditor to foreclose first, *Daily* reached the correct result insofar as it prohibited foreclosure after setoff.⁹⁸ However, the remedy of prohibiting foreclosure or the right to the unpaid balance is unjust punishment to the creditor.⁹⁹ Although the court recognized that the fairest sanction would be to require the bank to refund the money with interest, the court rejected this sanction and instead imposed a loss of security sanction. This sanction was unduly harsh.¹⁰⁰ Other commentators suggest that such a sanction grants an unwarranted windfall to the debtor which section 726 does not contemplate, and goes beyond promoting the public policies of section 726.¹⁰¹ If section 726 is to have any validity in this situation, the debtor should be given the right to force the creditor to foreclose on the security. The debtor must have the right to raise the one action rule as an affirmative defense. This problem is complicated even further when the creditor's loan is secured by both real and personal property.¹⁰²

If the setoff in *Daily* was not viewed as an action, the creditor would have been able to setoff the amount owed in the checking ac-

94. See Arnold, *supra* note 7, at 11; Mitchell, *Setoff Imperils Foreclosure*, 102 BANKING L. J. 60 (1985); Rowan & Mertens, *Bank of America v. Daily: Setoff Versus the Right to Foreclose* 8 REAL PROP. L. REP. 73 (1985); Mertens, *supra* note 10, at 555-56.

95. See *supra* note 85 and accompanying text.

96. 19 Cal. 2d 254, 120 P.2d 869 (1942).

97. Rowan & Mertens, *supra* note 94, at 76.

98. *Id.*

99. *Id.* at 78.

100. *Id.* at 77.

101. *Id.*

102. *Enterprise Leasing Corporation v. Epstein*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676 *reh'g denied & nonpub.* (May 14, 1987); *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974). (The amendments of Cal. Com. Code § 9501(4) will affect the application of the one action rule in a mixed collateral context). See generally *Hetland & Hansen*, *supra* note 37, at 199-215.

count and subsequently foreclose on the security. Thus, the creditor would have been able to recover the entire amount by foreclosing on the property interest securing the debt. However, the creditor would not have been permitted to recover under the setoff, because the bank account was not taken as security.¹⁰³ Instead, the setoff would be returned to the debtor with interest, and the creditor would be forced to first foreclose on the security.¹⁰⁴

C. Judicial Proceedings which are not Actions

In *In re Rivers*¹⁰⁵ a creditor held a note secured by two pieces of real property. The debtor filed for protection under the Bankruptcy Act,¹⁰⁶ while the creditor sought relief from the stay to foreclose on both properties. The trial court granted leave to foreclose on one of the properties and the creditor proceeded to do so without a judicial proceeding. When the creditor returned to court to foreclose on the second property, the court determined that the creditor had taken his one action against the debtor by filing the original petition for relief. Because the creditor did not pursue the hearing before seeking foreclosure on the second property, the creditor violated the one action rule and thereby waived the balance of his security.¹⁰⁷ The federal district court reversed the bankruptcy court and determined there was no action for two reasons: (1) there was no judicial foreclosure; and (2) the creditor was not seeking a deficiency judgment.¹⁰⁸ *Rivers* stresses the importance of recovery of a debt in a judicial proceeding before an action can exist.¹⁰⁹

*Passanisi v. Merit McBride Realtors, Inc.*¹¹⁰ also focused on the issue of what type of judicial conduct by the creditor constitutes an action for purposes of section 726. The court of appeal in *Passanisi* held that a judgment for attorney's fees awarded to a trust deed ben-

103. Arguably, the bank would have a security interest in any account where it acts as lender.

104. See *infra* notes 121-31 and accompanying text.

105. 39 Bankr. 608 (Bankr. C.D. Cal. 1984), *rev'd*, 55 Bankr. 699 (Bankr. C.D. Cal. 1984).

106. 11 U.S.C. § 362 (1987).

107. 39 Bankr. 608 (Bankr. C.D. Cal. 1984).

108. 55 Bankr. 699 (Bankr. C.D. Cal. 1984).

109. "In retrospect, it appears that the Bankruptcy Court must have viewed the motion for relief from stay as somehow transforming the non-judicial trustee's sale which followed into judicial foreclosure, thereby activating the deficiency procedure of Section 726." This notion is wrong and does not promote any of the goals of Section 726. See Arnold, *supra* note 7, at 11-12.

110. 190 Cal. App. 3d 1496, 236 Cal. Rptr. 59 (1987).

eficiary who successfully blocked the trustor's efforts to enjoin a trustee's sale was not an action under section 726.¹¹¹

In *Rivers*, the creditor did not recover under his motion for relief. In *Passanisi*, there was a recovery in a judicial proceeding for fees. If the court found either proceeding to be an action, there would have been no recovery on the debt. Although facially these proceedings fit within the definition of a judicial proceeding,¹¹² since there is no recovery on the debt, finding an action cannot be justified.¹¹³

V. SOLUTIONS

A. Implementation of the Uniform Land Transactions Act

There is a need to clarify what an action is for purposes of section 726. Some commentators suggest that the one action rule be rejected by implementing the Uniform Land Transactions Act ("ULTA").¹¹⁴ The ULTA expressly rejects the one action rule by providing the creditor with two sets of rights, one under the note and one under the security agreement.¹¹⁵ The ULTA was proposed in 1975 and approved by the National Conference of Commissioners on Uniform State Laws. It has received little support in individual states. ULTA is structured to parallel Article 3 of the Uniform Commercial Code,¹¹⁶ which governs secured transactions. Section 3501 of ULTA specifically addresses foreclosures. According to this section, a secured creditor can proceed under the note or foreclose on the security. It further provides that if the creditor sues on the note before foreclosing, the judgment lien may relate back to take a priority position over the security interest.¹¹⁷ Under ULTA, deficiency judg-

111. *Id.* The trustor in this case initially obtained a preliminary injunction halting the trustee's sale. The beneficiary prevailed at trial. He sought recovery for the \$15,473.50 in attorney's fees pursuant to a provision within the deed of trust obligating the trustor to pay attorney's fees incurred by the lender. However, the trial court didn't award the full amount of attorney's fees requested. The plaintiffs, on appeal, argued that the lender's judgment for attorney's fees was an "action" for purposes of Section 726. The court reasoned that the determination of attorney's fees was not an "action," because the one "action" rule only applied when the creditor beneficiary had brought an action against the debtor to recover a debt or enforce some debt secured by a deed of trust. Since the underlying "action" (enjoining the exercise of power of sale) was initiated by the trustor, section 726 was inapplicable.

112. CAL. CIV. PROC. CODE § 22 (West 1982 & Supp. 1988). See *supra* note 10 and accompanying text.

113. Since the amount of fees recoverable in most settings will be but a small fraction of the overall debt, it seems unlikely that the court would hold that recovery of fees constitutes an "action".

114. Leipziger, *supra* note 75, at 758; Bruce, *Mortgage Law Reform Under the Uniform Land Transactions Act (as amended)*, 65 GEO. L. J. 1245 (1976).

115. Bruce, *supra* note 114, at 1279.

116. Comment, *Secured Transactions Under Article 3 of the Uniform Land Transactions Act*, 3 WIS. L. REV. 899 (1976).

117. Bruce, *supra* note 114. (The relation back will only occur if the judgment

ments are significantly altered in two ways. First, a debtor is liable for any deficiency remaining after the sale of the collateral. Second, a creditor may not obtain a deficiency judgment against a protected party on an obligation secured by a purchase money mortgage.¹¹⁸

Although ULTA achieves uniformity among secured transactions in different states, it violates the policy of protecting the debtor which is the impetus behind section 726. By providing the creditor two separate rights, one on the note and one on the secured property, the creditor is in an extremely advantageous position while the debtor is disadvantaged.

B. Legislative Clarification of the One Action Rule

1. Incorporation of California Civil Procedure Code Section 22 into the One Action Rule

The term *action* of the California Civil Procedure Code section 22 should be incorporated into section 726.¹¹⁹ This section contemplates the occurrence of an *action* in judicial proceedings only,¹²⁰ and if incorporated into section 726 it would prevent a holding such as *Daily*. The setoff which, in the *Daily* case, was found to be an "action" is not a judicial proceeding for the recovery of a debt.¹²¹ Therefore, the incorporation of California Civil Procedure Code section 22 into Section 726 would alleviate some of the mystery as to exactly what constitutes an action.

a. Policy Statement of the One Action Rule

Additionally, a policy statement of section 726 should be added stating the following: "The legislature declares that it is the express policy of the state to require a creditor to look to the real property security first before reaching a debtor's other assets. This section shall be liberally construed to effectuate this purpose."¹²² One com-

specifies that the obligation was secured by real estate identified in the judgment. *Id.* at 1279 n. 260).

118. CAL. CIV. PROC. CODE § 580(b) provides the same protection; *see supra* note 33.

119. Mertens, *supra* note 10, at 577-78.

120. *See supra* note 11 and accompanying text.

121. *Id.*

122. Mertens, *supra* note 10, at 578. This provision essentially provides that the debtor may use section 726 as an affirmative defense to force the creditor to look to the secured property first. This proposal clarifies the sanction which the court imposes if the creditor fails to foreclose on all of the security first. Unlike *Daily*, which held that the

mentator suggests a debtor's remedy section.¹²³ This section essentially provides that a creditor who fails to foreclose on all of the security first may obtain a personal judgment against the debtor but not recover the security.

This proposal does not promote the security first principle of the one action rule. The proposal is similar to that of the proposed New York Civil Procedure Code from which California's section 726 is derived.¹²⁴ The proposal does prevent a multiplicity of actions.¹²⁵ However, the New York Code provides for an election of remedies whereas the California section limits both the choice of remedies and the remedy itself.¹²⁶ California Civil Procedure Code, as interpreted by the courts for over one hundred years,¹²⁷ bars this type of independent action upon the note and requires the creditor to look to the security first.¹²⁸ The proposal suggests recovery of the debt instead of foreclosure on the property if the debtor fails to raise section 726 as an affirmative defense. This is actually a preferred sanction to the creditor. There is a need to clarify the meaning of the sanction aspect. However, enforcing section 726 as a choice of remedies does not fulfill the purpose of the security first principle, enabling the debtor to dispose of the secured property before the creditor can recover on the underlying debt.

A section providing for debtor's remedies is necessary. This section should expressly provide for sanctions against a creditor who fails to foreclose on all the security first. The creditor should not be permitted to obtain a personal judgment on the underlying debt. Instead, the proper sanction should be to refund the amount of money the creditor obtained (if the procedure of obtaining funds was a setoff),

creditor could neither reach the security nor obtain a personal judgment against the debtor, this proposed sanction provides that a creditor who fails to foreclose on all the security first may obtain a personal judgment against the debtor, but may not recover the security.

123.

The creditor or trustee at the creditor's direction shall sell all the property which is security for a debt before seeking a deficiency judgment pursuant to subsection (b). If a creditor does not do so, a debtor may compel the creditor to foreclose by pleading and proving that the debt was secured by real property. If the debtor does not compel the creditor to foreclose on all the security in the creditor's one action, the creditor may obtain a judgment against the debtor for the balance due but may not foreclose on the security at a later date. The security shall be declared free of the mortgage or deed of trust at the debtor's request.

Id. at 579.

124. *See supra* notes 41-43 and accompanying text.

125. *See supra* notes 48-58 and accompanying text.

126. *Id.*

127. *Winklemen v. Sides*, 31 Cal. App. 2d 387, 88 P.2d 147 (1939); *Porter v. Muller*, 65 Cal. 512, 4 P. 531 (1884).

128. *Winklemen*, 31 Cal. App. 2d at 387, 88 P.2d at 147.

and force the creditor to exhaust the security.¹²⁹ This is the most equitable means of achieving the policies behind section 726(a): exhaustion of the security first, and the avoidance of a multiplicity of suits against the debtor. This also enables the debtor to recover on the debt by foreclosing and obtaining a deficiency judgment as the one action rule contemplates.

VI. CONCLUSION

Courts have interpreted the one action rule expansively to protect debtors' rights. The question of what is an action for purposes of section 726 is left unanswered. Courts will likely continue to construe policies to protect the debtor. Debtor protection is not achieved through inequitable creditor remedies.¹³⁰ A solution to this problem rests in defining and applying the term action. Policy and debtor's remedies subsections advocating a security first principle are also necessary to guide the courts in their application of section 726.

This Comment has proposed the incorporation of section 22 into section 726. Section 22's definition provides that only judicial proceedings for recovery upon a debt are considered an action for purposes of section 726. This would alleviate the *Daily* problem in which the California Supreme Court determined that a setoff (a non-judicial proceeding) was an action. Further, policy and debtor's remedies subsections should be added requiring the creditor to look to the security first, exhausting such security before reaching the debtor's other assets.

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129. This sanction was raised by the court in *Daily*, 152 Cal. App. 3d at 772, 199 Cal. Rptr. at 559, but the court refused to implement it.

130. See, e.g., *Daily*, 152 Cal. App. 3d at 767, 199 Cal. Rptr. at 557. Such inequitable creditor remedies ultimately increase the cost of financing real property transactions, harming rather than helping the debtor.

