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The Montana Judicial and Non-judicial Foreclosure Sale: Analysis and Suggestions for Reform

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THE MONTANA JUDICIAL AND NON-JUDICIAL FORECLOSURE SALE: ANALYSIS AND SUGGESTIONS FOR REFORM

David J. Dietrich*

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I. INTRODUCTION

The recent decline in the value of real property collateral securing residential and commercial loans in Montana has spawned litigation over the procedures used by creditors in foreclosure actions.¹ This activity is natural because the law governing the mortgage, deed of trust and land sales contract foreclosures in Montana is an attempted balance. It seeks to balance the protection the law affords to a debtor whose personal assets may ultimately be subject to a deficiency judgment and the restrictions imposed on a foreclosing creditor who must obtain the collateral in partial or total satisfaction of the defaulted loan.

This article examines restrictions placed on creditors who judicially or non-judicially foreclose a Montana deed of trust or mortgage. Specifically it examines the judicial construction of Montana's "One Action Rule" that governs a traditional Montana real estate mortgage foreclosure. Additionally, the article examines the interrelationship between Montana's Uniform Commercial Code and Montana's judicial and non-judicial foreclosure scheme when a creditor forecloses on personal and real property securing a single promissory obligation. The article also outlines the various prohibitions Montana places on deficiency judgments and outlines the protections Montana affords to the debtor at the foreclosure sale. It concludes with some suggested legislative reforms.

II. HISTORY

An understanding of the terminology and principal protections of Montana's mortgage foreclosure law requires a brief explanation of the development of modern mortgage law.² In fourteenth century England, the common law mortgage was an actual conveyance of fee simple ownership from the borrower to the creditor. If the borrower paid the loan, title would revert in the borrower.³ The common law mortgage was harsh; if for any reason the payment was not made on "law day," the mortgagor forfeited all interest in the mortgaged property.⁴

By the seventeenth century, courts of equity created certain borrower protections: the borrower was entitled, as a matter of course and right, to redeem his land from the mortgage if he ten-

1. *First State Bank v. Chunkapura*, ___ Mont. ___, 734 P.2d 1203 (1987).
 2. G. NELSON & D. WHITMAN, *REAL ESTATE FINANCE LAW* § 1.2, at 6 (2nd ed. 1985).
 3. Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure—An Empirical Study of Mortgage Foreclosure and Subsequent Resale*, 70 *CORNELL L. REV.* 850, 855 (1985).
 4. Wechsler, *supra* note 3, at 856; NELSON & WHITMAN, *supra* note 2, § 1.2, at 6.

dered the principal and interest within a reasonable time after law day.⁵ Because the borrower-mortgagor's right of "tardy" redemption resulted in a hardship on the mortgagee, equity developed the mortgagee's right to foreclose the equity of redemption.⁶ At the request of the mortgagee in a bill setting forth the details of the mortgage and default, equity would order the mortgagor to pay the debt, interest, and costs within a fixed period. That failing, a decree would be issued forever barring the mortgagor's equity of redemption.⁷

Because the mortgagee already had legal title to the land, subject only to the mortgagor's right to redeem, the mortgagee became the absolute owner of the land.⁸ This kind of foreclosure action left the mortgagee with clear title to the property and resulted, in effect, with the mortgagee exchanging the debt for the mortgagor's land.⁹ This type of foreclosure is referred to as "strict foreclosure" because it often resulted in an exchange of land for a disproportionate smaller debt.¹⁰

Because of the harshness of strict foreclosure to the borrower, by the nineteenth century the common law added procedural protections to the foreclosure process.¹¹ These protections included notice to all parties interested, open decree of court, and publicity of sale. In theory, they decreased the loss to the borrower and permitted the creditor to recover a deficiency judgment if the sale price fell short of the debt.¹²

Like England under the common law, the United States legal system also rejected the "strict foreclosure" method.¹³ In its stead, the two predominant, contemporary foreclosure methods developed:¹⁴ judicial foreclosure by public sale and non-judicial foreclosure by power of sale.¹⁵ Under the judicial method, a public sale

5. The right was recognized as an estate in land and is known as the "equity of redemption." Wechsler, *supra* note 3, at 856; NELSON & WHITMAN, *supra* note 2, § 1.3 at 7.

6. Wechsler, *supra* note 3, at 856; NELSON & WHITMAN, *supra* note 2, § 1.3 at 8.

7. NELSON & WHITMAN, *supra* note 2, § 1.3, at 8.

8. Wechsler, *supra* note 3, at 857; NELSON & WHITMAN, *supra* note 2, § 1.3, at 8.

9. *Id.*

10. "Under strict foreclosure the mortgagee might acquire land far more valuable than the mortgage debt, a result considered harsh, oppressive, and unfair." Wechsler, *supra* note 3, at 859; NELSON & WHITMAN, *supra* note 2, § 1.3, at 8.

11. Wechsler, *supra* note 3, at 857-58.

12. Barth v. Ely, 85 Mont. 310, 318, 278 P. 1002, 1005 (1929); "Foreclosure by sale was viewed as a logical way of protecting the debtor's equity in the property while still allowing the mortgagee to recover a deficiency judgment when the proceeds of the sale fell short of the amount owed by the mortgagor." Wechsler, *supra* note 3, at 859.

13. Wechsler, *supra* note 3, at 858.

14. NELSON & WHITMAN, *supra* note 2, § 1.4, at 9.

15. *Id.*

results after a full judicial proceeding. All interested persons must be made parties.¹⁶ Under the power of sale method, no judicial proceeding is usually required and, after varying types and degrees of notice to the borrower and other interest holders, a public official, sheriff, or trustee sells the property at public sale.¹⁷ The foreclosure processes required under the principal real estate security devices used in Montana are examined below.

III. AN OVERVIEW OF THE PRINCIPAL REAL PROPERTY SECURITY DEVICES IN MONTANA

The principal real property security devices in Montana are the contract for deed (or land sales contract), the deed of trust (or trust indenture), and the mortgage.

A. *Contract for Deed*

Under the contract for deed, the record owner of the real property delivers a warranty deed to the immediately succeeding purchaser when the purchaser or his successor has completed the last payment.¹⁸ Pending payment by the purchaser, legal title to the property remains vested in the seller.¹⁹ A warranty deed from the seller to the purchaser typically remains in escrow together with a quitclaim deed from the purchaser to the seller with instructions for its delivery to the seller for recording in the event of default.²⁰

The terms and provisions (price, down payment, interest rate, etc.) and collateral protection provisions (insurance requirements, limitations on releasing of tracts of the collateral) differ according to the kind of real estate involved. However, the contract usually contains two mutually exclusive remedies: release of the deeds by the escrow agent causing a termination of the contract or acceleration of the principal balance together with delivery by the seller of

16. For Montana's judicial foreclosure procedures see *infra* notes 37-44 and accompanying text.

17. For Montana's non-judicial foreclosure procedures see *infra* notes 52-69 and accompanying text.

18. See *Aveco Properties, Inc. v. Nicholson*, ___ Mont. ___, 747 P.2d 1358 (1987) and MONT. CODE ANN. § 70-20-115 (1987).

19. The seller retains legal title whereas the buyer holds equitable title. *Greenup v. United States*, 239 F. Supp. 330 (D. Mont. 1965).

20. This non-judicial remedy of termination or forfeiture is not automatic, however, because the buyer can usually force legal action to enforce the contract by informing the escrow agent that the buyer has equity in the property causing the escrow agent to interplead the account under MONT. R. CIV. P. 22(b).

the warranty deed to the buyer.²¹ The Montana Supreme Court does not require a contract for deed to be foreclosed as a mortgage,²² and has refused to characterize the contract as a purchase money mortgage.²³ Thus, if the seller elects specific performance, sells the property at sheriff's sale to satisfy the accelerated balance, and incurs a "deficiency,"²⁴ the purchaser is personally liable for the resulting deficiency judgment.²⁵

B. Mortgage and Deed of Trust

While in some states title is actually transferred from the debtor-mortgagor to the creditor-mortgagee,²⁶ in Montana a mortgage of real property is a lien from the borrower to the creditor.²⁷ As such, Montana falls into the substantial majority of states that follow the lien theory of mortgages.²⁸ Montana also allows for a deed of trust security device where the borrower-grantor²⁹ grants fee title³⁰ to a trustee³¹ (usually a title company) to secure repayment of the grantor's obligation to the beneficiary-creditor.³² Chapter 1, title 71 of the Montana Code Annotated codifies the following mortgages: the traditional mortgage,³³ the traditional mortgage with a power of sale provision,³⁴ the purchase money

21. This latter option is sometimes referred to as specific performance. *Glacier Campground v. Wild Rivers, Inc.*, 182 Mont. 389, 597 P.2d 689 (1979).

22. *White v. Jewett*, 106 Mont. 416, 420, 78 P.2d 85, 87 (1938) (holding that the predecessor to MONT. CODE ANN. § 71-1-222 governing mortgage foreclosures had no application to a contract for deed terminated by cancellation); *See also Aveco*, ___ Mont. at ___, 747 P.2d at 1361.

23. *Aveco*, ___ Mont. at ___, 747 P.2d at 1360; *Glacier Campground*, 182 Mont. at 405, 597 P.2d at 698.

24. The accelerated debt and interest, plus certain costs and fees, less the sales price.

25. *Aveco*, ___ Mont. at ___, 747 P.2d at 1360; *Glacier Campground*, 182 Mont. at 405, 597 P.2d at 698.

26. This is the "title theory" of mortgage law having its roots in the common law, discussed above. *See NELSON & WHITMAN, supra note 2, § 1.5, at 10.*

27. "The lien of a mortgage is special, unless otherwise expressly agreed, and is independent of possession." MONT. CODE ANN. § 71-1-103 (1987).

28. *NELSON & WHITMAN, supra note 2, § 4.2, at 145.*

29. The term "grantor" means "the person conveying real property by a trust indenture as security for the performance of an obligation." MONT. CODE ANN. § 71-1-303(3) (1987). It is synonymous with the mortgagor, except a third party trustee holds title for the benefit of the beneficiary-mortgagee and is the practical equivalent of a mortgage with a power of sale provision. *NELSON & WHITMAN, supra note 2, § 1.6, at 11-12. See also MONT. CODE ANN. § 71-1-305 (1987).*

30. MONT. CODE ANN. § 71-1-303(5) (1987).

31. MONT. CODE ANN. § 71-1-303(5) 1987.

32. MONT. CODE ANN. §§ 71-1-303(1) to -304 (1987).

33. MONT. CODE ANN. §§ 71-1-101 to -103, 71-1-203 (1987).

34. MONT. CODE ANN. § 71-1-223 (1987).

mortgage,³⁵ and the deed of trust.³⁶

1. *Traditional Mortgage*

The traditional mortgage foreclosure requires a full judicial proceeding under the Montana Rules of Civil Procedure.³⁷ Upon foreclosure, the proceeding eliminates the debtor's equity of redemption³⁸ and results in a decree of foreclosure and sale of the property for partial or total satisfaction of the accelerated debt plus interest, costs, fees, and other charges.³⁹ It is governed by Montana's one action rule, a procedural and substantive protection that forces the creditor to foreclose all collateral in one "judicial" action.⁴⁰ If foreclosed in compliance with the one action rule, the debtor can be liable for a deficiency judgment.⁴¹ The creditor can purchase at the sheriff's sale,⁴² and the court need not confirm the sale price.⁴³ For up to one year after the sheriff's sale, the debtor may redeem the property upon payment of the sale price, plus interest and assessments.⁴⁴

35. MONT. CODE ANN. § 71-1-232 (1987).

36. A deed of trust, in legal effect and theory, is the practical equivalent of a mortgage with a power of sale provision. *Bank of Italy Nat'l Trust & Savings Ass'n v. Bentley*, 217 Cal. 644, 20 P.2d 940 (1933).

37. Montana's statutory mortgage foreclosure scheme is one of four "One Action" statutes (Nevada, Utah, and Idaho are the others) patterned after California's statute. NELSON & WHITMAN, *supra* note 2, § 8.2, at 598. Additionally, Montana, like thirty-one other states, authorizes both the traditional judicial foreclosure scheme and the non-judicial foreclosure in all or some circumstances. Bauer, *Judicial Foreclosure and Statutory Redemption: The Soundness of Iowa's Traditional Preference for Protection Over Credit*, 71 IOWA L. REV. 1, 5 (1985). In contrast, nine other states require judicial foreclosure as the sole means of foreclosure by statute or rule prohibiting non-judicial foreclosure. *Id.* at 4 n.8. In ten other states, judicial foreclosure is impliedly required by the absence of any statute or rule authorizing or recognizing non-judicial foreclosure. *Id.* Thus, the Montana judicial and non-judicial scheme affords greater flexibility for the foreclosing creditor than in some states.

38. See *supra* text accompanying notes 5-6 for the definition of the "equity of redemption." Most mortgage instruments contain acceleration clauses enabling the creditor to accelerate the remaining principal balance of the debtor's installment promissory obligations thus prohibiting the debtor from repeatedly repaying only arrearage amounts. See NELSON & WHITMAN, *supra* note 2, § 7.6, at 488. Prior to the sale, however, the debtor always has the right to pay the accelerated balance of the debt and retain the property. NELSON & WHITMAN, *supra* note 2, § 3.1, at 33. See also *Bohan v. Harris*, 71 Mont. 495, 230 P. 586 (1924).

39. MONT. CODE ANN. § 71-1-222 (1987).

40. See *infra* notes 100-134 and accompanying text for an in-depth discussion of this rule.

41. MONT. CODE ANN. § 71-1-222 (1987).

42. MONT. CODE ANN. § 25-13-704 (1987) only refers to the "highest bidders" as being entitled to purchase.

43. *Interior Securities Co. v. Campbell*, 55 Mont. 459, 466, 178 P. 582, 584 (1919).

44. See MONT. CODE ANN. § 25-13-801 through -825 (1987). Montana, like about half the states, requires all judicial mortgage foreclosure sales to be subject to some form of statutory redemption. NELSON & WHITMAN, *supra* note 2, § 8.4, at 616. In Montana, the

2. Traditional Mortgage with Power of Sale

A traditional mortgage can contain a power of sale provision that enables the mortgagee to conduct a summary sale of the mortgaged property, without judicial foreclosure or sale by the sheriff.⁴⁵ It is not the same device as a trustee's sale under a deed of trust.⁴⁶ Unlike the foreclosure of a traditional mortgage that is subject to the general notice provisions of execution sales,⁴⁷ the power of sale foreclosure requires more stringent notice, publication, and posting of the sale.⁴⁸ At the sale, the mortgagee cannot purchase⁴⁹ and the debtor has the same one-year right of redemption as under a judicial foreclosure.⁵⁰ The creditor cannot obtain a deficiency judgment under a power of sale foreclosure.⁵¹

3. The Deed of Trust—Non-Judicial Foreclosure

Montana's Small Tract Financing Act creates a distinct non-judicial foreclosure procedure "by advertisement and sale" for deeds of trust less than fifteen acres.⁵² The Act supplements the judicial mortgage foreclosure procedures.⁵³ Under the Act, the creditor has the option to judicially foreclose a deed of trust.⁵⁴ Specifically, the Act provides that "at the option of the beneficiary,"⁵⁵ the trust indenture may be foreclosed "by judicial procedure as provided by law for the foreclosure of mortgages on real property."⁵⁶ The Act also provides that "[a] trust indenture is deemed to be a mortgage on real property and is subject to all laws relating

mortgagor has one year's right of redemption after the sheriff's foreclosure sale of the traditional or power of sale mortgage, and under a deed of trust securing any kind of property occupied other than as a single family residence. See MONT. CODE ANN. § 71-1-228 (1987); *First State Bank v. Chunkapura*, ___ Mont. ___, ___, 734 P.2d 1203, 1210 (1987). However, the debtor has no redemption rights after a judicial sale of an occupied, single family residential property under a deed of trust, or after any deed of trust property sold non-judicially at a trustee's sale. *Id.* See MONT. CODE ANN. §§ 71-1-228 through -304 (1987).

45. MONT. CODE ANN. § 71-1-223 (1987).

46. Compare MONT. CODE ANN. §§ 71-1-223 and 71-1-304 (1987).

47. MONT. CODE ANN. § 25-13-701 (1987).

48. MONT. CODE ANN. § 71-1-224 (1987) requires advertisement for thirty days or posting in five conspicuous places in the county, additional posting requirements, and personal service on the property occupant, the mortgagor if within Montana, and all other interested persons if within Montana.

49. *Union Central Life Ins. Co. v. Jensen*, 74 Mont. 70, 237 P. 518 (1925).

50. MONT. CODE ANN. § 71-1-228 (1987).

51. *First Nat'l Corp. v. Perrine*, 99 Mont. 454, 43 P.2d 1073 (1935).

52. MONT. CODE ANN. § 71-1-304 (1987).

53. MONT. CODE ANN. § 71-1-305 (1987).

54. MONT. CODE ANN. § 71-1-304(3) (1987).

55. MONT. CODE ANN. § 71-1-304(3) (1987).

56. MONT. CODE ANN. § 71-1-304(3) (1987).

to mortgages . . . except to the extent that such laws are inconsistent with [the Small Tract Financing Act]."⁵⁷

To foreclose by advertisement and sale, the mortgagee-beneficiary must meet certain conditions.⁵⁸ General conditions for non-judicial foreclosure of the deed of trust include: proper recordation of the trust indenture at the appropriate clerk and recorder's office, a default under the obligation secured by the deed of trust, and recordation of the notice of the trustee's sale, which must include certain statutorily required information.⁵⁹

The Act also contains specific "advertisement and sale" requirements.⁶⁰ At least 120 days prior to the sale date, the creditor must send, by certified or registered mail, a copy of the recorded notice of trustee's sale to statutorily designated parties.⁶¹ The creditor must also post the recorded notice of the trustee's sale on the property at least twenty days before the sale date,⁶² publish the notice of sale in a newspaper of general circulation for a required period,⁶³ and record with the local clerk and recorder affidavits of mailing, posting, and publication showing compliance with the foregoing requirements.⁶⁴

The strict notice provisions of the advertisement and sale foreclosure method insure compliance with fourteenth amendment due process notice requirements under the United States Constitution.⁶⁵ No Montana court has ruled on the constitutionality of the notice provisions of the Act. The acreage limitations⁶⁶ of the Act, however, do not constitute an unconstitutional classification under the equal protection clause of the fourteenth amendment.⁶⁷ Upholding its constitutionality, the Montana Supreme Court held that the acreage classification was reasonable, in light of the financial-development objective of the Act.⁶⁸ The court also noted that it created a means for the lender to obtain title to collateral outside the judicial process, avoiding the cost of traditional foreclo-

57. MONT. CODE ANN. § 71-1-305 (1987).

58. MONT. CODE ANN. § 71-1-313 (1987).

59. See MONT. CODE ANN. § 71-1-313(3) (1987) (listing requirements).

60. MONT. CODE ANN. § 71-1-315 (1987).

61. See MONT. CODE ANN. § 71-1-315(1)(a) (1987) (listing designated parties).

62. MONT. CODE ANN. § 71-1-315(1)(b) (1987).

63. MONT. CODE ANN. § 71-1-315(1)(c) (1987) (specifying time requirements).

64. MONT. CODE ANN. § 71-1-315(2) (1987).

65. NELSON & WHITMAN, *supra* note 2, § 7.24, at 562.

66. MONT. CODE ANN. § 71-1-304(1) (1987) limits the deed of trust to no greater than fifteen-acre tracts (formerly three acres).

67. Great Falls Nat'l Bank v. McCormick, 152 Mont. 319, 323, 448 P.2d 991, 993 (1968).

68. *Id.*

sure methods.⁶⁹

4. *The Deed of Trust—Comparison of Judicial and Non-Judicial Foreclosure*

The non-judicial foreclosure method affords the beneficiary-mortgagee the option to foreclose the deed of trust by invoking the operation of the judicial foreclosure procedures.⁷⁰ These procedures include compliance with the one action rule, the primary debtor protection under the judicial foreclosure scheme.⁷¹

The advertisement and sale foreclosure method and the judicial foreclosure method differ in several fundamental respects. In contrast to Montana's one action rule, which permits the docketing of a deficiency judgment after compliance with that rule,⁷² the "no further action" rule of the non-judicial foreclosure scheme⁷³ prohibits any:

[o]ther or further action, suit, or proceedings, . . . taken or judgment entered for any deficiency against the grantor or his surety, guarantor, or successor in interest, if any, on the note, bond, or other obligation secured by the trust indenture or against any other person obligated on such note, bond, or other obligation.

Primarily, a facial reading of the no further action statute prohibits any deficiency judgment against the debtor after a non-judicial sale. It also protects "any other person" obligated on "such . . . other obligation" from any "other or further action or proceedings" after the advertisement and sale foreclosure. The statute therefore extends specifically to guarantors and co-makers of the obligation secured by the trust indenture.⁷⁴ In contrast, the judicial one action rule does not provide, on its face, such extensive protection although the "one action" requirement of the rule makes its protection at least as extensive as the no further action rule.⁷⁵

The non-judicial and judicial foreclosure methods also differ with respect to the debtor's right to avoid acceleration of installment payments not yet due. Under the provisions in the standard mortgage, the mortgagee has power to accelerate the outstanding

69. *Id.*

70. MONT. CODE ANN. § 71-1-304(3) (1987).

71. MONT. CODE ANN. § 71-1-222(1) (1987).

72. MONT. CODE ANN. § 71-1-222(2) (1987).

73. MONT. CODE ANN. § 71-1-317 (1987).

74. In this respect the statute mirrors the judicial foreclosure requirements that the note merges into the judgment and is thereby exonerated. *Lepper v. Jackson*, 102 Mont. 259, 57 P.2d 768 (1936).

75. See *infra* notes 100-134 and accompanying text.

principal amount secured by the mortgage, to refuse any tendered reinstatement payments, and to commence foreclosure.⁷⁶ Under the non-judicial procedure, however, the mortgagor-grantor has the right "at any time prior to the time fixed by the trustee for the trustee's sale to *reinstate* the entire amount then due under the terms of the trust indenture and the obligation secured thereby."⁷⁷ At such time, the advertisement and sale foreclosure method ceases and the trust indenture "shall be reinstated . . . and remain in force and effect the same as if no acceleration had occurred."⁷⁸

Under Montana's judicial foreclosure statutes, the mortgagor has a nonwaivable⁷⁹ one-year right of redemption⁸⁰ after the sheriff's sale that includes the right to remain in possession if the debtor personally occupies the property.⁸¹ The advertisement and sale foreclosure procedure affords no such right of redemption to the grantor-mortgagor in the event of non-judicial sale.⁸² *Chunkapura* explains the rationale for the elimination of the debtor's right of redemption:

The banking and lending industry came to the legislature in 1963, contending that the "one action" rule and the attendant right of redemption and right of possession rules hampered the financing of improvements on small tracts in Montana because banks and investors were unwilling to invest in mortgages when on default their funds would be tied up during the period of redemption. A quid pro quo was proposed to the legislature: the lenders would give up their deficiency judgment rights on default, if the borrowers would give up their rights of possession and redemption. The result was the adoption by the legislature of the Small Tract Financing Act of Montana, originally limited to tracts of three

76. NELSON & WHITMAN, *supra* note 2, § 7.6, at 488-89. The lender, however, must accept tender of the entire accelerated balance. *See supra* note 38.

77. MONT. CODE ANN. § 71-1-312(1) (1987).

78. MONT. CODE ANN. § 71-1-312(2) (1987).

79. MONT. CODE ANN. § 71-1-229 (1987) (prohibiting waiver prior to sale).

80. MONT. CODE ANN. § 25-13-802 (1987).

81. MONT. CODE ANN. § 25-13-821 (1987).

82. The purchaser at the trustee's sale is entitled to possession ten days following the sale. MONT. CODE ANN. § 71-1-319 (1987). The foregoing presents only a partial comparison between the judicial and non-judicial foreclosure methods in Montana. Other major differences include the use of receivers in judicial foreclosure actions to preserve the value of the collateral or collect rents and profits. *See* MONT. CODE ANN. § 27-20-102 (1987). *See also* *Hastings v. Wise*, 89 Mont. 325, 297 P. 482 (1931); *Long v. W.P. Devereux Co.*, 87 Mont. 198, 286 P. 402 (1930); *Masterson v. Hubbert*, 54 Mont. 613, 173 P. 421 (1918). Because an "action" for the appointment of a receiver must be made in the foreclosure action, arguably a creditor must foreclose a deed of trust judicially and request a receiver in that action rather than independently of a request for a receiver. *See* MONT. CODE ANN. § 71-1-222 (1987); *Hartnett v. St. Louis Mining & Milling Co.*, 51 Mont. 395, 153 P. 437 (1915).

acres, but now may involve tracts as large as fifteen acres.⁸³

5. *Chunkapura: Foreclosing the Deed of Trust Judicially*

Prior to *Chunkapura*, judicial and non-judicial foreclosure methods were distinct in Montana. If the mortgagee-beneficiary judicially foreclosed the deed of trust, it could obtain a deficiency judgment subject to the one action rule and trigger the debtor's statutory redemption rights.⁸⁴ In *Chunkapura*, however, the court was required to decide whether a lender could obtain a deficiency judgment after a judicial foreclosure of a residential deed of trust where the value of the residential property had declined.⁸⁵ The *Chunkapuras'* deed of trust property was originally an occupied, single-family residence.⁸⁶ At the time of sale, the *Chunkapuras* owed First Bank Of Forsyth approximately \$18,000.00, including sheriff and attorney fees.⁸⁷ The bank bid \$10,000 on the property leaving a net deficiency judgment in the amount of \$8,556.93.⁸⁸ The parties stipulated to a sale of the property but submitted to the court the issue of the bank's ability to pursue a deficiency judgment.⁸⁹ The district court ordered that the "no further action" rule of the non-judicial foreclosure statutes prohibited the docketing of a deficiency judgment, even though the bank had elected to judicially foreclose the deed of trust.⁹⁰

Statutorily, the court found a contradiction between the non-judicial statutes eliminating the right of redemption and the lender's right to a deficiency judgment on one hand and the statute allowing the lender to elect judicial foreclosure on the other hand.⁹¹ Based on this stated inadequacy of Montana's statutes, the court made a roaming examination of certain fair market value, anti-deficiency, and upset price statutes in other western states.⁹²

83. ___ Mont. ___, ___, 734 P.2d 1203, 1205 (1987).

84. The State Bank of Forsyth advanced this argument. *Id.* at ___, 734 P.2d at 1206.

85. *Id.* at ___, 734 P.2d at 1208.

86. However, by the time of foreclosure sale, the improvements on the property had been removed leaving the collateral as a vacant lot. Letter from John Houtz (counsel for the *Chunkapuras*) to David Dietrich (Dec. 10, 1987). At the time the loan was granted to the *Chunkapuras*, the loan and deed of trust were for a single family residence. Eventually, due to the deteriorating condition of the house, the house was torn down and an empty lot remained. The *Chunkapuras* relocated and continued to pay on the loan, and when they stopped paying on the loan, the bank started foreclosure proceedings.

87. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1204.

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.* at ___, 734 P.2d at 1206.

92. *Id.* at ___, 734 P.2d at 1207-08.

The court concluded its analysis by finding that Montana and Alaska do not have any protective legislation limiting the deficiency amount to the difference between the amount of the indebtedness sought and the fair market value of the property at the time of the sale.⁹³

In its initial opinion, the court simply denied the creditor any right to pursue a deficiency judgment after judicial foreclosure of any Montana deed of trust and stripped the debtor of any right of redemption on the property.⁹⁴ In reaching the decision, the court noted the absence of any statutory limit on the price bid by the purchaser at the foreclosure sale, exposing the residential borrower to a double liability: the loss of the residence and exposure to a deficiency judgment.⁹⁵ As later modified in the Order On Rehearing, the court limited the application of its decision to occupied single family residential deeds of trust,⁹⁶ excluding more complicated loans secured by agricultural or commercial deeds of trust.⁹⁷

In its analysis, the court stated that "prior to 1963 Montana was a one action rule state"⁹⁸ implying that the adoption of the non-judicial foreclosure statutes displaced Montana law governing judicial foreclosure.⁹⁹ The remaining applicability of the judicial foreclosure scheme and its interrelationship with article 9 of the Uniform Commercial Code are dealt with in the following two sections in this article.

IV. MONTANA'S ONE ACTION RULE

A. Introduction

Section 71-1-222 of the Montana Code Annotated governs the foreclosure of the traditional mortgage in Montana.¹⁰⁰ The Mon-

93. *Id.* at ____, 734 P.2d at 1208.

94. *Id.*

95. *Id.*

96. *Id.* at ____, 734 P.2d at 1210.

97. *Id.*

98. *Id.* at ____, 734 P.2d at 1204.

99. The court noted that since the adoption of the Small Tract Financing Act, enabling non-judicial deed of trust foreclosures, the use of deeds of trust has become nearly exclusive. *Id.* at ____, 734 P.2d at 1205. Nothing in the record supported that conclusion and mortgages subject to the one action rule continue to be used in a variety of commercial and agricultural contexts.

100. MONT. CODE ANN. § 71-1-222 provides in part as follows:

(1) There is but one action for the recovery of debt or the enforcement of any right secured by mortgage upon real estate, which action must be in accordance with the provisions of this part. In such action the court may, by its judgment, direct:

(a) a sale of the encumbered property (or so much thereof as may be

tana Supreme Court has repeatedly acknowledged that with the statute's adoption from the California Code of Civil Procedure, Montana also adopted the construction given to the statute by the Supreme Court of California.¹⁰¹

As originally enacted and prior to the adoption of article 9 of the Montana Uniform Commercial Code, the statute required that one action alone be initiated "for the recovery of debt, or the enforcement of any right secured by mortgage upon real estate *or personal property*"¹⁰² The reference to personal property was excluded from the statute by amendment during the 1963 legislative session,¹⁰³ presumably so that the enforcement scheme of article 9 would apply without conflict with the irreconcilable one action provision. The California legislature similarly amended section 726 of the California Code of Civil Procedure.¹⁰⁴

B. *Purpose of One Action Rule*

The one action rule compels the creditor with mortgage security to exhaust that security before having recourse to the general assets of the debtor.¹⁰⁵ Otherwise stated, the rule means that in the event of a default, the mortgagee's sole remedy is a foreclosure action and that any deficiency claim must be brought in that proceeding.¹⁰⁶ The rule also protects the mortgagor against a multiplicity of actions when two separate actions, though theoretically distinct, are so closely connected that normally they can and should be decided in one suit.¹⁰⁷

necessary);

(b) the application of the proceeds of the sale; and

(c) payment of the costs of the court, the expenses of the sale, and the amount due the plaintiff.

(2) If it appears from the sheriff's return that the proceeds are insufficient and a balance still remains due, judgment can then be docketed for such balance against the defendant or defendants personally liable for the debt, and it becomes a lien upon the real estate of such judgment debtor, as in other cases on which execution may be issued.

101. See *Barth v. Ely*, 85 Mont. 310, 278 P. 1002 (1929). *Brophy v. Downey*, 26 Mont. 252, 67 P. 312 (1902); *Largey v. Chapman*, 18 Mont. 563, 46 P. 808 (1896).

102. MONTANA REVISED CODES § 9467 (1935) (emphasis added) [hereinafter R.C.M.].

103. Uniform Commercial Code, 1963 Mont. Laws 264, § 11-166.

104. Hetland, *The "Mixed Collateral" Amendments to California's Commercial Code*, 75 CAL. L. REV. 185, 195 n.43 (1987).

105. *Barth v. Ely*, 85 Mont. 310, 320, 278 P. 1002, 1006 (1929).

106. NELSON & WHITMAN, *supra* note 2, § 8.2, at 598.

107. *Id.* See also *Stallings v. Erwin*, 148 Mont. 227, 233, 419 P.2d 480, 483 (1966).

C. Construction of the One Action Rule—Debtor's Protections

1. Adequacy of Security is Lender's Risk

In 1929, in *Barth v. Ely*,¹⁰⁸ the Montana Supreme Court reconciled the restrictions contained in Montana's one action rule with the predecessor to section 71-3-110 that provided that "the existence of a lien, as security for the performance of an obligation, does not affect the right of the creditor to enforce the obligation without regard to the lien" ¹⁰⁹ The creditor in that case attempted to waive the mortgage security, sue on the note alone, and avoid the requirement of the one action rule that the mortgage security be foreclosed.¹¹⁰ The court thus faced the question of whether the creditor must foreclose on inadequate, although not valueless security.¹¹¹ Holding for the debtor, the court determined that the more specific statute, the one action rule, prevailed over the lien waiver provision.¹¹² In so doing, the court provided a clearer definition as to the use of the term "secured" in the one action rule statute:

The word "secured" . . . does not mean that the security shall be adequate, or that in case prior liens upon it would exhaust the money derived from the land conveyed as security on a sale of it, then the plaintiff is relieved from bringing the action to foreclose. The proper construction of the language of the statute is, that if the mortgage on its face purports to be a security to the plaintiff, then he must bring his action for foreclosure.¹¹³

2. Suit on Note Alone Prohibited; Waiver

Two years later in *Coburn v. Coburn*,¹¹⁴ the Montana court confronted the question of whether a creditor's prior personal judgment on a promissory note secured by a mortgage constituted a waiver of the mortgage security in a subsequent action to foreclose. The court prohibited the creditor from maintaining the subsequent foreclosure action.¹¹⁵ It noted that to hold otherwise would be to sanction two actions where the statute limits the creditor to one. The court reasoned that "the tendency of modern legislation

108. 85 Mont. 310, 278 P. 1002 (1929).

109. *Id.* at 317, 278 P. at 1005.

110. *Id.*

111. *Id.* at 326, 278 P. at 1008.

112. *Id.* at 323, 278 P. at 1007.

113. *Id.* at 326, 278 P. at 1008 (citations omitted).

114. 89 Mont. 386, 298 P. 349 (1931).

115. *Id.* at 389, 298 P. at 350.

is to prevent a multiplicity of suits, and no one doubts the wisdom of it."¹¹⁶

3. *Mortgagee Cannot Maintain Separate Action for Taxes Secured by Mortgage*

In *Stallings v. Erwin*,¹¹⁷ the mortgagee purchased a tax sale certificate for taxes the mortgagor failed to pay.¹¹⁸ After a third party purchased the property at the sheriff's sale of the mortgagee's mortgage foreclosure action, the third party moved to quiet title to the property to eliminate the mortgagee's tax lien.¹¹⁹ The mortgagee argued that its tax lien survived the foreclosure sale and was subrogated to the county's first lien position.¹²⁰ The Montana Supreme Court rejected that argument on the basis that the one action rule prohibited *any* subsequent action for "any right" secured by the mortgage.¹²¹ Thus, the court required the mortgagee "to satisfy all claims arising out of the mortgage in a single foreclosure action."¹²²

D. *Construction of the One Action Rule—The Change in Circumstances Exception*

Another line of cases protects the creditor from engaging in a needless foreclosure action if the security is valueless through no fault of the creditor. The Montana Supreme Court explained this rule in *Bailey v. Hansen*:¹²³ "where there has been a change of circumstances, after the taking of the mortgage resulting in the fact that it has become valueless, this fact may be shown without resorting to the useless procedure of foreclosure."¹²⁴ Thus, in *Brophy v. Downey*,¹²⁵ a second lienholder whose lien was extinguished by the foreclosure of a first lien mortgage could maintain a direct action on the note even after the expiration of the redemption period.¹²⁶ Similarly, in *Bailey* where the mortgagor defrauded the mortgagee, representing that no prior encumbrances existed on

116. *Id.*

117. 148 Mont. 227, 419 P.2d 480 (1966).

118. *Id.* at 228, 419 P.2d at 481.

119. *Id.* at 229, 419 P.2d at 481.

120. *Id.*

121. *Id.* at 231, 419 P.2d at 482.

122. *Id.* at 233, 419 P.2d at 483.

123. 105 Mont. 552, 74 P.2d 438 (1937).

124. *Id.* at 556, 74 P.2d at 440. See also Annotation, *Action on Secured Debt—When Permissible*, 108 A.L.R. 397 (1937).

125. 26 Mont. 252, 67 P. 312 (1902).

126. *Id.* at 258, 67 P.2d at 315.

the premises when in fact a prior mortgage existed making the second lienholder's security valueless,¹²⁷ the mortgagee was entitled to maintain a direct action on the note. The exception to the one action rule also applies where a tax lien foreclosure renders the security of the second lienholder valueless.¹²⁸ The exception further applies where the debtor-mortgagor is not the real party raising the one action rule as a defense; indeed, in *Leffek v. Luedeman*¹²⁹ the unsecured creditors in an estate unsuccessfully raised the one action rule as a defense to an action by a creditor who failed to file the required renewal affidavit on a mortgage and sought to maintain a direct action on the note in the estate.¹³⁰

The doctrine of estoppel, however, limits the creditor's ability to claim the change in circumstances exception: "where plaintiff voluntarily takes security for a debt, whether a first or second mortgage, and there is no change of circumstances, he must foreclose and cannot assert that the security has become valueless."¹³¹ Thus, "so long as the security has value, the only action that will lie on the mortgage debt is the statutory action on foreclosure."¹³²

No recent Montana cases address the current application of this exception. However, a recent Utah case, construing that state's similar one action rule, refused to allow a second-position mortgagee to sue directly on the note prior to the senior lienholder's foreclosure sale. The creditor merely estimated a deficiency by affidavit on summary judgment.¹³³ It reasoned as follows: "It is not enough to speculate that the security is valueless, or might become valueless if foreclosed by the senior lienholder. Rather, the security must be, in fact, exhausted and a deficiency established to a certainty in order for the exception to apply."¹³⁴ The mortgagee must show that the security has been foreclosed and sold or otherwise lost by no fault of the mortgagee prior to the commencement of the action on the note.

127. *Bailey*, 105 Mont. at 558, 74 P.2d at 441.

128. *Id.* at 557, 74 P.2d at 441. See also *Quickenden v. Hulbert*, 83 Mont. 501, 509-10, 272 P. 994, 998 (1928); *Richardson v. Lloyd*, 90 Mont. 127, 131, 300 P. 254, 256 (1931).

129. 95 Mont. 457, 27 P.2d 511 (1933).

130. *Id.*

131. *Bailey*, 105 Mont. at 557, 74 P.2d at 441.

132. *Id.*

133. *Lockhart Co. v. Equitable Realty, Inc.*, 657 P.2d 1333, 1335 -36 (Utah 1983).

134. *Id.* at 1336. See also *Gebrueder Heidemann K.G. v. A.M.R. Corp.*, 107 Idaho 275, 282, 688 P.2d 1180, 1187 (1984); *Keever v. Nicholas Beers Co.*, 96 Nev. 509, 611 P.2d 1079 (1980).

V. THE MIXED COLLATERAL PROBLEM

A. *Nature of the Problem*

The requirement that the creditor exhaust all real property security in one action raises complications when the debt is secured by both a mortgage on real property and a security interest in personal property.¹³⁵ Montana has developed little case law in this area. California case law construing its substantially similar "one action rule" and provisions of article 9 of the Uniform Commercial Code¹³⁶ provide important warnings to the Montana creditor.

As noted above, after the adoption by Montana of the Uniform Commercial Code in 1959, the one action rule was amended in 1963 to exclude any reference to personal property. Additionally, section 30-9-501(4) of the Montana Code Annotated, of the Montana Commercial Code effectively subordinates a creditor's judicial remedies under article 9 of that code to the one action rule. That section provides:

If the security agreement covers both real and personal property, the secured party may proceed (under part 5 of article 9) as to the personal property, or he may proceed as to both the real and the personal property in accordance with his rights and remedies in respect of the real property, in which case the provisions (part 5 of article 9) do not apply.

Furthermore, section 30-9-508 of the Montana Code Annotated, also part of article 9, provides:

An action for the foreclosure of a security interest in personal property may be commenced and conducted in the same manner as provided by law for the foreclosure *by action* of mortgages upon real property, and the same may be joined in an action for the recovery of the possession of the property subject to the security interest, but the remedial scope of proceedings for the foreclosure of interests subject to this chapter is governed by [part 5 of article 9].¹³⁷

B. *Mixed Collateral and Judicial Foreclosure*

Under these statutes, together with the unequivocal, exclusive language of the one action rule,¹³⁸ a creditor holding a single promis-

135. See generally Hetland, *supra*, note 104.

136. *Id.*

137. MONT. CODE ANN. § 30-80-508 (1987) (emphasis added).

138. MONT. CODE ANN. § 71-1-222 (1987) unequivocally states "[t]here is but one action for the recovery of debt or the enforcement of any right secured by mortgage upon real

sory note secured by, for example, a mortgage and a security interest in the debtor's farm machinery has several choices. In the event of default, the creditor can employ the self-help remedy of article 9 and repossess¹³⁹ the tractor without resort to judicial process, crediting the outstanding amount on the note paid by the sum received at the commercially reasonable sale of the machinery.¹⁴⁰ If, however, the creditor files a provisional remedy action and obtains, for example, claim and delivery of the personal property to preserve its value pending foreclosure, in California that creditor has waived any right to sue on the mortgage in a subsequent judicial action.¹⁴¹

Procedurally, in California the debtor may compel the creditor to include all the security he has for that debt in a single judicial foreclosure by raising the one action rule as an affirmative defense.¹⁴² Montana also holds that the debtor's raising of the one action rule is an affirmative defense.¹⁴³ When the creditor fails to exhaust all his security in one action and the debtor fails to compel him to do so by affirmatively raising his one action rule defense, a problem arises. When the creditor tries to recover the balance owing or take the remaining security, the one action rule triggers the following questions:¹⁴⁴

1. Does the creditor's failure to exhaust all security in one action affect his right to realize on the additional security?¹⁴⁵
2. Can he take a deficiency or personal judgment on the balance owing?¹⁴⁶
3. May the creditor bring another action to foreclose on the balance of the security?¹⁴⁷

estate"

139. MONT. CODE ANN. § 30-9-503 (1987). Private repossession of article 9 property should not invoke the "one action" rule unless the creditor requires the debtor to respond in a judicial action. *But see* *Bank of America v. Daily*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984), holding that a checking account offset triggers the one action rule, waiving the real property security and the balance of the debt.

140. MONT. CODE ANN. § 30-9-504 (1987).

141. *Epstein v. Enterprise Leasing Corp.*, 189 Cal. App. 3rd 834, 234 Cal. Rptr. 676 (1987) (Ordered not officially published. Rule 967, Cal. Rules of Court). *But see* *Forbush v. San Diego Fruit & Produce Co.*, 46 Idaho 231, 266 P. 659 (1928).

142. CAL. CIV. PROC. CODE § 726 (1987); *Pacific Valley Bank v. Schwenke*, 189 Cal. App. 3d 134, 234 Cal. Rptr. 298 (1987).

143. *Brophy*, 26 Mont. at 256, 67 P. at 314.

144. *Walker v. Community Bank*, 10 Cal. 3d 729, 733 n.2, 518 P.2d 329, 331-32 n.2, 111 Cal. Rptr. 897, 899-900 n.2 (1974). *See also Epstein*, 189 Cal. App. 3d 834 n.4, 234 Cal. Rptr. 676, 680 n.4.

145. *Walker*, 10 Cal. 3d at 733 n.2, 518 P.2d at 332 n.2, 111 Cal. Rptr. at 900 n.2.

146. *Id.*; *see also Epstein*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676; *Pacific Valley Bank*, 189 Cal. App. 3d 134, 234 Cal. Rptr. 298; *Bank of America*, 152 Cal. App. 2d 767, 199 Cal. Rptr. 557.

147. *Walker*, 10 Cal. 3d at 734 n.2, 518 P.2d at 332 n.2, 111 Cal. Rptr. at 900 n.2. *See*

4. Can he foreclose the balance by nonjudicial sale?¹⁴⁸

5. If the creditor foreclosed on none of his security but instead took a personal judgment against the debtor, does he retain his former lien priority when he attempts to execute on the real property that previously was his security?¹⁴⁹

To each of these questions but the first, commentators examining the relationship between the one action rule and the identified article 9 provision answer "No."¹⁵⁰ Consequently, the most expansive construction of the one action rule imposes a strict requirement that the creditor be forced to exhaust all security in one action to prevent a multiplicity of suits. The rule also encourages competitive bidding to test the value of all the security for the debt, thus forcing the creditor to look to all security as a primary fund for payment of the indebtedness before looking to the debtor's personal assets.¹⁵¹ If the debtor does not raise the one action rule as an affirmative defense, he may still invoke it as a sanction under California law against the creditor.¹⁵² Courts reason that since the creditor has not foreclosed on its security in the action brought to enforce the debt,¹⁵³ the creditor has made an election of remedies and has waived the security,¹⁵⁴ and, in some cases, the balance of the debt.¹⁵⁵

C. Mixed Collateral and Non-judicial Foreclosure

1. *Walker v. Community Bank*

Walker v. Community Bank,¹⁵⁶ the seminal California case on the mixed collateral security problem, expanded the rule to prohibit a trustee's non-judicial sale after a judicial action on personal property.¹⁵⁷ In *Walker*, both real and personal property secured a single debt and the creditor judicially foreclosed only on the personal property and obtained a deficiency judgment.¹⁵⁸ In a later

also *Salter v. Ulrich*, 22 Cal.2d 263, 138 P.2d 7 (1943); *Epstein*, 189 Cal. App. 3d at 834, 234 Cal. Rptr. at 676.

148. *Walker*, 10 Cal.3d at 734 n.2, 518 P.2d at 332 n.2, 111 Cal. Rptr. at 900 n.2.

149. *Id.*

150. *Id.*; See also *Epstein*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676.

151. *Epstein*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676.

152. *Id.*

153. *Pacific Valley Bank*, 189 Cal. App. 3d 134, 234 Cal. Rptr. 298; *Bank of America*, 152 Cal. App. 3d at 771, 199 Cal. Rptr. at 559.

154. *Walker*, 10 Cal. 3d at 733, 518 P.2d at 331, 111 Cal. Rptr. at 899.

155. *Pacific Valley Bank*, 189 Cal. App. 3d 134, 234 Cal. Rptr. 298; *Bank of America*, 152 Cal. App. 3d at 772, 199 Cal. Rptr. at 559.

156. 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897.

157. *Id.* at 732, 518 P.2d at 331, 111 Cal. Rptr. at 899.

158. *Id.* at 732, 518 P.2d at 331, 111 Cal. Rptr. at 899.

action to foreclose the deed of trust nonjudicially, the court permitted the debtor to invoke the "sanction" aspect of section 726(4) of the California Civil Code.¹⁵⁹ The court held that the creditor lost its security interest in the real property as against all parties.¹⁶⁰ Importantly, the *Walker* court prohibited a non-judicial trust indenture trustee's sale.¹⁶¹ The court relied on section 580(d) of the California Civil Code, the anti-deficiency provision governing non-judicial foreclosures of deeds of trust,¹⁶² similar in effect to section 71-1-317 of the Montana Code Annotated.¹⁶³ The court reasoned that to permit the creditor to file a judicial action on the personal property and seek a deficiency judgment would allow the creditor to circumvent the one action rule and anti-deficiency protections.¹⁶⁴ In so ruling, the court prevented the creditor from merely acquiring an insignificant amount of personal property, proceeding to judicially foreclose the personal property, and obtaining a deficiency judgment in such action and thereafter nonjudicially foreclosing the real property security.¹⁶⁵ Consequently, the *Walker* court imposed a sanction on the creditor even though the debtor did not raise the one action rule and anti-deficiency statutes as affirmative defenses: the creditor lost its security interest in the real property.¹⁶⁶

2. *Walker and Montana's No Further Action Rule*

Section 71-1-317 of the Montana Code Annotated invites application of *Walker* to Montana non-judicial foreclosures. That section provides that after a non-judicial "advertisement and sale" sale, "no other or further action, suit, or proceedings shall be taken or judgment entered for any deficiency against the grantor or his surety, guarantor, or successor in interest, if any, on the note, bond, or other obligation secured by the trust indenture." This section is the non-judicial "one action rule" without the "action" requirement; it requires an exoneration of the note and prevents any further action or proceedings on it after the trustee's sale.

Under *Walker*, if a creditor judicially forecloses on a selected item of personal property collateral securing a single promissory

159. *Id.* at 741-42, 518 P.2d at 337, 111 Cal. Rptr. at 905.

160. *Id.*

161. *Id.* at 735, 518 P.2d at 333, 111 Cal. Rptr. at 901.

162. *Id.* at 736, 518 P.2d at 333-34, 111 Cal. Rptr. at 901-02.

163. *See supra* notes 73-74 and accompanying text.

164. *Walker*, 10 Cal. 3d at 736-37, 518 P.2d at 334, 111 Cal. Rptr. at 902.

165. *Id.*

166. *Id.* at 741, 518 P.2d at 337, 111 Cal. Rptr. at 905.

note and later seeks a deficiency judgment, the anti-deficiency language of the "no further action" statute would void the creditor's security interest in the deed of trust and preclude any further non-judicial trustee's sale.¹⁶⁷ If, however, the creditor exercises non-judicial article 9 self help remedies and does not seek a deficiency judgment, lenders have successfully argued that the creditor does not lose the right to pursue additional security.¹⁶⁸ Although there are no Montana cases on point, this result could obtain under the "no further action" rule because the "action or proceeding" preceded the non-judicial sale and did not result in the lender pursuing a deficiency. If the creditor attempts to sell the personal property judicially or nonjudicially after the trustee's sale, he is barred from any remedies as to the personal property ("no other or further action or proceeding").¹⁶⁹ Thus, if a creditor has cross-collateralized a single obligation with both personal and real property collateral, he must sequence his judicial or non-judicial article 9 repossession of the property before the non-judicial trustee's sale.¹⁷⁰

3. *Avco: Limits on the No Further Action Rule*

The Montana case of *Avco Financial Services v. Christiaens*¹⁷¹ provides a limited exception to this rule, however, in the event a junior deed of trust lienholder's interest has been foreclosed nonjudicially by a senior lienholder.¹⁷² In that case, the debtor granted a personal property security interest and a second position trust deed to *Avco*.¹⁷³ Nationwide held the first position trust indenture.¹⁷⁴ *Avco* purchased the property at Nationwide's trustee's sale and subsequently sold the property.¹⁷⁵ Because the senior

167. *Walker*, 10 Cal. 3d 729, 735, 518 P.2d 329, 333, 111 Cal. Rptr. 897, 901.

168. *Freedland v. Greco*, 45 Cal. 2d 462, 289 P.2d 463 (1955) permitted the lender to pursue additional security after a non-judicial power of sale foreclosure on the basis that "the pursuit of additional security is not the pursuit of a deficiency judgment . . ." By extension, if the creditor pursues non-judicial article 9 remedies prior to pursuing its real estate mortgage and does not seek any deficiency judgment (there being no action resulting in a judgment), a subsequent action to foreclose real estate security does not violate either Montana's one action rule or its no further action rule. See MONT. CODE ANN. §§ 71-1-222, -317 (1987). *But see* note 188 and cases cited therein.

169. The "no other or further action, suit, or proceedings" language of section 71-1-317 (emphasis added) requires this result. *But see Avco Fin. Servs. v. Christiaens*, 201 Mont. 117, 652 P.2d 220 (1982).

170. *See also infra* note 190.

171. 201 Mont. 117, 652 P.2d 220 (1982).

172. *Id.* at 120, 652 P.2d at 222.

173. *Id.* at 118, 652 P.2d at 221.

174. *Id.*

175. *Id.* at 119, 652 P.2d at 221.

lienholder's trustee's deed eliminated the security position of Avco, the court held that Avco was not prevented from waiving its personal property collateral and suing on the note.¹⁷⁶ The court reasoned that the creditor under article 9 could waive its security interest in the personal property, obtain a judgment on the note, and proceed by execution and levy.¹⁷⁷ The court also reasoned that because the senior lienholder's (Nationwide) foreclosure extinguished the junior lienholder's lien, the second position lienholder should be relieved from the restrictive requirements of the "no further action" rule and allowed to sue on the note alone.¹⁷⁸

4. Avoidance of the Mixed Collateral Problem

The one action rule has no application if the creditor makes separate debts with separate security.¹⁷⁹ Thus, the creditor can avoid the one action rule by breaking the single transaction into obligations secured separately by real and personal property at the outset.¹⁸⁰ The one action rule does not apply to recovery on a separate, unsecured note, although the note was part of a transaction where real property or property collateral secured other notes.¹⁸¹ Thus, a lender can finance the purchase of a hotel by breaking the single purchase price into separate debts, evidenced by separate notes, each a part of the total price, securing one note by the hotel, another by personal property and fixtures, and leaving still another unsecured.¹⁸² The result would be that the real property foreclosure and deficiency limitations would apply only to the notes secured by the hotel.¹⁸³ The separate note secured by the personal property and fixtures would be subject only to the Uniform Commercial Code. The unsecured note would be fully collectible with no security-related procedural or substantive limitations on the creditor's judicial or self-help enforcement of the debt.¹⁸⁴

However, if the debt is structured as an obligation that is not validly broken up into separate debts, the one action rule applies. If the nominally separate notes either duplicated each other or

176. *Id.* at 120, 652 P.2d at 222.

177. *Id.*

178. *Id.* at 122, 652 P.2d at 223.

179. *Roseleaf Corp. v. Chierighino*, 59 Cal. 2d 35, 38-39, 378 P.2d 97, 100-01, 27 Cal. Rptr. 873, 876-77 (1963).

180. *Id.*

181. *Christopherson v. Allen*, 190 Cal. App. 2d 848, 851-52, 12 Cal. Rptr. 658, 660 (1961).

182. *Hetland*, *supra* note 104, at 196.

183. *Id.* See also *Kistler v. Vasi*, 71 Cal. 2d 261, 455 P.2d 106, 78 Cal. Rptr. 170 (1969).

184. *Hetland*, *supra* note 104, at 196.

represented the same consideration, creditors must comply with the rule.¹⁸⁵ Similarly, if one separate note was cross-collateralized or secured even in small part by real property, then the mixed collateral problem exists.¹⁸⁶

5. Summary on How To Avoid the Mixed Collateral Problem

To summarize, the following are options available to a Montana creditor seeking to foreclose a single note secured by both personal and real property security:

1. The lender can proceed non-judicially¹⁸⁷ by private repossession of the collateral prior to the filing of any judicial mortgage foreclosure action and credit the amount received after sale.¹⁸⁸

2. The lender may include all personal property collateral contemporaneously with the judicial real property foreclosure of the deed of trust or mortgage, or consciously waive any claim as to such personal property collateral.¹⁸⁹

3. If the trustee is able to obtain possession of the personal property collateral and conduct an article 9 public sale, the lender may include both personal and real property security as part of the non-judicial trustee's sale.¹⁹⁰

4. If the value of the real property has become worthless through no fault of the creditor, usually through foreclosure by a senior lienholder, the creditor can proceed judicially or non-judicially as to the personal property. In addition, the creditor can waive pursuit of the personal property in favor of a levy and execu-

185. *Freedland v. Greco*, 45 Cal. 2d 462, —, 289 P.2d 463, 465 (1965).

186. *Walker v. Community Bank*, 10 Cal. 3d 729, 518 P.2d 329, 111 Cal. Rptr. 897 (1974). See also *Hetland*, *supra* note 104, at 193 n.33.

187. Sale of certain kinds of personal property collateral requires a judicial foreclosure action, however.

188. Caveat: Any recourse to collateral by the lender prior to a judicial or non-judicial foreclosure under California law prior to the 1986 amendments resulted in possible waiver of not only the security but also the debt. See *Epstein v. Enterprise Leasing Corp.*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676 (1984) (private sale of collateral after claim and delivery held to violate the one action rule); see also *Bank of America v. Dailey*, 152 Cal. App. 3d 767, 199 Cal. Rptr. 557 (1984) (exercise of self help remedy of banker's offset violated the one action rule).

189. This method is probably the safest because it assures the lender of compliance with the various protections underlying the one action rule. See generally *Epstein*, 189 Cal. App. 3d 834, 234 Cal. Rptr. 676.

190. Nothing in Montana's non-judicial foreclosure scheme prohibits a trustee from selling personal property collateral at the trustee's sale; however, practicalities may prevent the trustee from delivery of possession of the personal property at a trustee's sale or conducting the personal property sale so as to maximize the return on the collateral, thus not meeting the "commercially reasonable" standard of section 30-9-504(3) of the Montana Code Annotated.

tion against other property owned by the debtor.¹⁹¹ However, the waiver of the real property collateral should not be initiated prior to consummation of the foreclosure proceedings by the first lienholder where there is a "mere speculated deficiency."¹⁹²

6. Legislative Reforms

As the foregoing discussion points out, Montana's one action rule, as construed in California, imposes severe penalties on the creditor holding a single obligation secured by both personal and real property collateral. Recognizing the severity of the problem, in 1986 California legislation amended that state's counterpart to section 30-9-501(4) of the Montana Code Annotated.¹⁹³ The amendment now permits the creditor, upon the debtor's default, to apportion the single obligation according to the ratable portion secured by real property and the ratable portions secured by personal property.¹⁹⁴ As drafted, the amendment intended to permit the creditor to judicially foreclose on as much of the personal property collateral as the creditor desired, risking only loss of real property collateral not included in the action.¹⁹⁵ However, California did not amend its one action rule, and commentators have questioned whether the sanction aspect of the one action rule still would nullify the existence of the remaining obligation in addition to causing a waiver of the remaining real property collateral.¹⁹⁶

The severe penalties imposed by California law on the creditor holding a single obligation secured by real and personal property collateral, when applied by extension to Montana's judicial mortgage foreclosure scheme, creates sufficient cause for amendment using California's recent amendments as a starting point. Such amendments should clarify whether the balance of the creditor's obligation remains in place if a creditor forecloses solely on personal property when remaining real property collateral exists. Such amendments should also clarify the circumstances under which a creditor will be denied recourse to a deficiency judgment if it has

191. By extension, if the real property security is valueless, the creditor should be able to waive the real property security in favor of the personal property security or a direct action against the debtor. See *supra* notes 123-134 and accompanying text; *Avco Fin. Servs. v. Christiaens*, 201 Mont. 117, 652 P.2d 220 (1982).

192. Whether the creditor can waive the real property security prior to actual sale is unclear in Montana; the more cautious practice would be to wait until the sale and eliminate any speculation. See *Lockhart Co. v. Equitable Realty, Inc.*, 652 P.2d 1333 (Utah 1983).

193. CAL. COM. CODE § 9-501(4) (West Supp. 1988).

194. Hetland, *supra* note 104, at 190.

195. Hetland, *supra* note 104, at 205.

196. Hetland, *supra* note 104, at 206.

not included all collateral in one "action."

VI. SUBSTANTIVE ANTI-DEFICIENCY LAW IN MONTANA

The restrictions imposed by the one action rule, the no further action rule, and article 9 of Montana's Uniform Commercial Code are procedural restrictions on the foreclosure process. Montana law also provides substantive prohibitions on deficiency judgments. Those rules are examined in this section.

A. *The Deed of Trust and Chunkapura: More Questions Than Rules?*

1. *Questions Raised by Chunkapura*

The Montana Supreme Court in *Chunkapura* confused the procedures used in judicial and non-judicial foreclosures by applying the non-judicial anti-deficiency statute to a judicial foreclosure.¹⁹⁷ The court's unclear distinction between residential and commercial deeds of trust compounds this confusion.¹⁹⁸ In its order on rehearing, the court limited its ruling to "occupied single-family residential deeds of trust,"¹⁹⁹ reasoning that the "quid pro quo" sacrifice by the lender of its right to pursue a deficiency judgment for the borrower's sacrifice of its possessory redemption rights did not obtain in the commercial context.²⁰⁰ But the court held that the possessory right of redemption only applies to a debtor and his family who personally reside on the property.²⁰¹

It is unclear whether *Chunkapura* applies to a residential deed of trust no longer "occupied" by the mortgagor (for example, who has rented the property). Arguably, it does not because no "quid pro quo" applies: the mortgagor is no longer entitled personally to any possessory redemption right.²⁰² Under *Chunkapura*, it is also unclear whether the creditor is limited to recourse to the occupied, single-family deed of trust where personal property also secures the same note.²⁰³ Additionally, if a lender forecloses on a multi-

197. See *supra* notes 85-99 and accompanying text.

198. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1210.

199. *Id.*

200. *Id.*

201. MONT. CODE ANN. § 25-13-821 (1987).

202. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1210.

203. *Chunkapura* raises this question because it applied the no further action rule to a judicial foreclosure of a deed of trust. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1210. The "no other proceeding" language of MONT. CODE ANN. § 71-1-317 may preclude recourse to personal property collateral even if the creditor includes it as part of a judicial action to foreclose the deed of trust. The lender, however, is not so precluded if the one action rule governs the procedure. See MONT. CODE ANN. § 71-1-222 (1987).

family apartment complex, secured by a deed of trust, one unit of which is occupied by the debtor's family, *Chunkapura* raises the question of whether the complex is an occupied, residential deed of trust. *Chunkapura* provides no definition of "commercial property" outside the scope of its ruling.

2. Proposed Legislation

Legislation is needed to clarify the meaning of a "commercial deed of trust." Oregon's statute serves as a starting point.²⁰⁴ Any definition of the term "commercial deed of trust" should identify whether the defined commercial use begins at the execution of the deed of trust or at the time of the entry of foreclosure judgment.²⁰⁵ Any such definition should also identify that group of residential occupants entitled to anti-deficiency protection.²⁰⁶ Further, the definition should limit the number of the multi-residential dwellings above which the property becomes commercial, the threshold number being measured at either the time of the loan transaction or entry of the default of judgment.²⁰⁷ Finally, the definition of commercial should exclude vacant property at the time of the execution of the deed of trust to promote development,²⁰⁸ thus enhancing the overall developmental object of the Small Tract Financing Act.²⁰⁹

Legislative clarification of *Chunkapura* should also address whether the non-judicial no further action rule or the one action rule of Montana's judicial foreclosure procedure governs the judicial foreclosure of a deed of trust.²¹⁰ By extending non-judicial anti-deficiency protections to the judicial foreclosure of a deed of

204. OR. REV. STAT. § 86.770 (1987).

205. OR. REV. STAT. § 86.770(4)(a) (1987) defines a commercial trust indenture "at the time of the execution of the trust indenture."

206. The definition in OR. REV. STAT. § 86.770.4(b) 1987, provides:

A trust deed covering real property which, at the time of entry of the judgment foreclosing the trust deed, is not occupied by the grantor, the grantor's spouse or the grantor's child as the primary residence of such person unless the property was occupied by such person at the time the foreclosure action was commenced and the grantor establishes the property was the only real property in which the grantor had any interest at the time.

207. OR. REV. STAT. § 86.770(4)(c) (1987) also provides the following definition of a commercial deed of trust: "A trust deed covering real property upon which are situated four or more residential units, either at the time of execution of the trust deed or at the time of entry of the judgment foreclosing the trust deed . . ."

208. OR. REV. STAT. § 86.770(4)(d) (1987) excludes vacant property from its definition of a commercial deed of trust by defining it as: "A trust deed covering real property which is more than one acre in size and which is vacant at the time of execution of the trust deed."

209. MONT. CODE ANN. § 71-1-302 (1987).

210. See *supra* note 203 and accompanying text.

trust, *Chunkapura* cast doubt on the lender's ability to combine all collateral in one foreclosure action under the one action rule.²¹¹

B. Purchase Money Mortgage Protections

1. Montana's Two-Party Statute

Montana's purchase money mortgage statute prohibits any deficiency judgment in favor of a seller-lender against the purchaser of a purchase money mortgage as follows:

Upon the foreclosure of any mortgage, executed to any *vendor* of real property or to his heirs, executors, administrators, or assigns for the balance of the purchase price of such real property, the mortgagee shall not be entitled to a deficiency judgment on account of such mortgage or note or obligation secured by the same.²¹²

Passed in 1935,²¹³ this section prohibits a deficiency judgment in the two-party context where the mortgagee-vendor takes back a mortgage to secure repayment of a loan advanced for the sale of the property to the mortgagor.²¹⁴ Such statutes provide a "deficiency cushion" in the event of falling land values and the consequent deficiency exposure to a defaulting purchaser.²¹⁵ Supposedly, the rule also discourages overvaluation by sellers;²¹⁶ that objective is subject to serious question since the rule may actually encourage overvaluation to compensate for the vendor's inability to obtain anything other than the land.²¹⁷

2. Application to Contracts for Deed

In *Aveco Properties, Inc. v. Nicholson*,²¹⁸ the Montana Supreme Court refused to extend the application of this section to prohibit a vendor under contract of deed from obtaining a deficiency judgment after a sheriff's sale of the real property where the vendor had opted to accelerate the balance of the contract and sold

211. See *supra* note 203 and accompanying text.

212. MONT. CODE ANN. § 71-1-232 (1987) (emphasis added).

213. 1935 Mont. Laws 2, § 1.

214. Facially, the term "vendor" in the statute does not include the "third party" lender who advances money to the borrower to enable payment to the seller. *But see* Pulse v. North Am. Title Co., ___ Mont. ___, 707 P.2d 1105 (1985).

215. *Bargioni v. Hill*, 59 Cal. 2d 121, 123, 378 P.2d 593, 594, 28 Cal. Rptr. 321, 322 (1963).

216. *Id.*

217. NELSON & WHITMAN, *supra* note 2, § 8.3, at 608-09.

218. ___ Mont. ___, 747 P.2d 1358 (1987).

the property in partial satisfaction of that balance.²¹⁹ Although arguably the functional equivalent of a purchase money mortgage,²²⁰ the court in *Nicholson* refused to characterize a contract for deed as a mortgage.²²¹

3. Application to Third-Party Lenders

The Montana purchase money mortgage statute does not, on its face, extend beyond the two-party lender-seller context to include the third-party lending institution. In *Pulse v. North American Title Co.*,²²² however, the Montana Supreme Court defined the purchase money mortgage as “a mortgage on land executed to secure the purchase money by a purchaser of the land contemporaneously with the acquisition of the legal title thereto or afterward, but as part of the same transaction.”²²³ Although not central to the decision, the court held that a deed of trust given to a bank in consideration for an enabling loan by the bank was a purchase money mortgage.²²⁴ *Pulse*, therefore, has arguably expanded the anti-deficiency protection under the definition of the purchase money mortgage from the two party vendor-vendee context to the third-party lender context.

4. Purchase Money Mortgage Statute Reforms

The *Pulse* decision sufficiently confuses the meaning of the purchase money mortgage statute to require legislative amendment. Other states' legislatures have expanded the purchase money mortgage definition to the third-party context.²²⁵ California prohibits a deficiency judgment under a purchase money mortgage “as to all vendors who take back real estate security and to those third-party lenders who take a mortgage or a deed of trust to secure all or part of the purchase price of purchaser occupied dwell-

219. *Id.* at ____, 747 P.2d at 1361.

220. The contract for deed provision requiring an escrowed warranty deed as security, however, fits the definition of a mortgage as a contract where property is “hypothecated” for “an act,” namely, payments. MONT. CODE ANN. § 71-1-101 (1987).

221. The stated reason for the *Nicholson* court's refusal to characterize a contract for deed as a purchase money mortgage was statutory. *Nicholson*, __ Mont. at ____, 747 P.2d at 1360. Underlying policy reasons may also include the fact that contracts for deed are the most common form of noninstitutional seller financing in Montana. Preventing the seller from obtaining a deficiency judgment could eliminate the ability of many buyers to obtain seller financing when conventional financing is unavailable because of falling land values.

222. __ Mont. ____, 707 P.2d 1105 (1985).

223. *Id.* at ____, 707 P.2d at 1107.

224. *Id.* at ____, 707 P.2d at 1108.

225. CAL. CIV. PROC. CODE § 580(b) (West 1988); ARIZ. REV. STAT. ANN. § 33-729(4) (1987); OR. REV. STAT. § 88.075 (1987).

ings less than five families."²²⁶ In Oregon, the anti-deficiency rule has been expanded by statute to the third-party financier context, but only on homes financed up to \$50,000.00, provided the same is used by the purchaser as his primary or secondary single-family residence.²²⁷

Any such amendment in Montana clearly should declare whether the statute applies in the third-party context. If so, it should also classify the deficiency protection according to the kind of security device, be it a contract for deed, residential or commercial deed of trust, or solely a mortgage transaction.²²⁸ Amendments should also clarify whether the deficiency protection depends on the use of the real estate, whether commercial, residential, or agricultural.²²⁹ The reason for this distinction centers on the differing degree of the financial risk associated with residential as opposed to commercial property ownership.²³⁰ The statute should also address whether the residential owner must occupy the property, whether purchase money protection should be extended to only the borrower's principal residence, and whether residential property put to commercial use should be excluded (such as multi-family residential rental units).

C. *Are Guarantors Protected Under Montana's Anti-Deficiency Statute?*

1. *Guarantors and the One Action and the No Further Action Rules*

Montana's judicial foreclosure scheme does not address whether a party to a continuing guaranty with the foreclosing creditor can seek refuge in substantive protection of the *Chunkapura* decision, the purchase money mortgage statute, or the one action rule.²³¹ No Montana law or statutory language directly prohibits a

226. CAL. CIV. PROC. CODE § 580(b) (West 1988).

227. OR. REV. STAT. § 88.075 (1987).

228. Statutory definition of whether the statute applies to contracts for deed or the judicial deed of trust foreclosures could eliminate unnecessary litigation.

229. Whether the legislature desires to promote seller financing on certain uses of property governs whether the statute should apply to all kinds of security devices. "To deny such vendor-mortgagees deficiency judgment in the event of a foreclosure may deter the use of socially useful financing." NELSON & WHITMAN, *supra* note 2, § 8.3, at 605.

230. "Most homeowners are not highly knowledgeable and are generally unable to appreciate, to the same degree as a commercial investor, the financial risk associated with property ownership." Platt, *Deficiency Judgments in Oregon Loans Secured by Land: Growing Disparity Among Functional Equivalents*, 23 WILLAMETTE L. REV. 37, 55 (1987).

231. MONT. CODE ANN. §§ 71-1-222, -232 (1987); *Chunkapura*, ___ Mont. ___, 734 P.2d 1203.

direct action against a guarantor for a deficiency judgment after the judicial foreclosure of a mortgage. Cases in other jurisdictions addressing the issue turn on the specific language of the particular anti-deficiency statute involved.²³² However, "there is clear[ly] . . . a judicial predisposition to deny guarantors the protections of anti-deficiency legislation."²³³ The rationale of one jurisdiction having a one action rule illustrates why deficiency protection can be denied to the guarantor if the creditor gives adequate notice of the sale:

The measure of the guarantor's liability is determined by his own contract of guaranty. If the primary debt is secured, we discern no impediment to a guaranty providing for liability only to the extent that a deficiency judgment would be obtainable against the primary debtor. The most obvious protection for the guarantor would be to attend the foreclosure sale of the security and bid up the price to its fair market value: by that means he would insure that his liability under the contract of guarantee would be precisely coextensive with the potential liability with the primary debtor under the anti-deficiency statute.²³⁴

Thus, in Nevada no direct prohibition against taking a deficiency judgment against a guarantor exists if two conditions are met. First, an independent contract of guarantee must exist between the lender and guarantor, which is not dependent on the promissory note between the mortgagor and the mortgagee.²³⁵ Second, the guarantor must obtain adequate notice of the foreclosure sale so as to "bid up" the price to its fair value.²³⁶ Montana's one action rule should be amended to contain these requirements to clearly define a guarantor's post-sale liability.

Montana's purchase money mortgage statute does not prohibit a deficiency judgment against the guarantor of the mortgagor's obligation.²³⁷ However, if the mortgagor is actually the guarantor and the creditor has attempted to obviate the restrictions of the purchase money mortgage statute by using a "dummy mortgagor," then case law applying anti-deficiency protections similar to Mon-

232. Annotation, *Mortgages: Effect Upon Obligation of Guarantor or Surety of Statute Forbidding or Restricting Deficiency Judgments*, 49 A.L.R.3d 554 (1973). See also NELSON & WHITMAN, *supra* note 2, § 8.3, at 606.

233. NELSON & WHITMAN, *supra* note 2, § 8.3, at 606.

234. *Thomas v. Valley Bank*, 97 Nev. 320, 323, 629 P.2d 1205, 1207 (1981).

235. If the guarantor is actually a cosigner of the note, the effect of the foreclosure judgment merges the note into the judgment and exonerates the note, thus reclosing the co-maker. *Lepper v. Jackson*, 102 Mont. 259, 57 P.2d 768 (1936). However, a guarantor's obligation is not exonerated by the discharge of the principal obligor without the intervention or omission by the creditor. MONT. CODE ANN. § 28-11-214 (1987).

236. *Thomas*, 97 Nev. at 323, 629 P.2d at 1207.

237. MONT. CODE ANN. § 71-1-232 (1987).

tana's purchase money mortgage statute would prohibit a deficiency judgment.²³⁸

A guarantor's liability after a judicial foreclosure of a residential deed of trust, however, remains unclear after *Chunkapura*.²³⁹ *Chunkapura* expanded the no further action statute to immunize the debtor from deficiency exposure.²⁴⁰ Arguably, then, the other protections of the statute also apply to the judicial foreclosure of a residential deed of trust. The no further action statute specifically prohibits any action against the borrower's surety or guarantor.²⁴¹ While the no further action statute clearly prohibits any judgment against the guarantor after a non-judicial foreclosure,²⁴² its effect on a judicial foreclosure of an occupied, residential deed of trust or a commercial deed of trust remains uncertain.²⁴³ One solution sanctioned by other jurisdictions with anti-deficiency legislation involves including a waiver in the contract between the guarantor and creditor as executed by the guarantor, eliminating any anti-deficiency rights between the guarantor and the creditor.²⁴⁴ Montana's no further action statute should be amended to reflect whether such a waiver would effectively permit a creditor to obtain judgment against the guarantor.

After a non-judicial foreclosure, the no further action statute prohibits any deficiency against the guarantor "on the note, bond, or other obligation secured by the trust indenture or against any other person obligated on such note, bond, or other obligation."²⁴⁵ It is not clear whether the statute prohibits a direct action against the guarantor if an independent contract of guarantee exists between the creditor and the guarantor. The statute should be amended to clarify whether a creditor can pursue the guarantor after the nonjudicial sale.

VII. REGULATION OF PRICE ADEQUACY

Apart from these procedural and the substantive anti-defi-

238. *In re Wilkin Maxfield Mgmt. Co.*, 117 F.2d 913 (9th Cir. 1941); *Riddle v. Lushing*, 203 Cal. App. 2d 831, 21 Cal. Rptr. 902 (1962).

239. *Chunkapura* applied the non-judicial no further action rule to a judicial foreclosure of a deed of trust.

240. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1206.

241. See MONT. CODE ANN. § 71-1-317 (1987).

242. See MONT. CODE ANN. § 71-1-317 (1987).

243. Arguably, the *Chunkapura* court based its decision on only the anti-deficiency protections of section 71-1-317 of the Montana Code Annotated rather than the other broad language of that statute.

244. *Valley Bank v. Larson*, 104 Idaho 772, 774, 663 P.2d 653, 655 (1983).

245. MONT. CODE ANN. § 71-1-317 (1987).

ciency protections, Montana law also attempts to limit the debtor's deficiency exposure by regulating bid price adequacy at public sales of mortgaged properties. Historically, this regulation developed in response to the "strict foreclosure" problem. The mortgagee would obtain possession of the land in exchange for the defaulted loan, thus causing a forfeiture of any equity the debtor then had in the property, assuming the value of the land exceeded the amount of the debt.²⁴⁶ In areas of appreciating land value, increasing the means for competitive bidding and payment to the debtor of any surplus amounts received on the creditor's profitable resale of the property to the debtor after the sale have been proposed to protect the debtor's equity in a property.²⁴⁷ Montana's current problem, however, is that the state has experienced a "depression of sorts" since 1981, depressing land values.²⁴⁸ Consequently, the need for price adequacy at the public sale is even more critical to protect the debtor from loss of the property and exposure to a deficiency judgment.

VIII. MONTANA'S LEGISLATIVE AND JUDICIAL RESPONSE TO PRICE INADEQUACY

The court in *Chunkapura* observed that other states have fair market value statutes protecting the debtor against falling land values, noting that Montana has no such legislation.²⁴⁹ Any examination of the need for fair market value legislation in Montana requires an initial analysis of existing judicial and statutory protections against sale price inadequacy.

A. Inadequate Sale Price

The Montana Supreme Court, as numerous other jurisdictions, has recognized its inherent equitable power to overturn a grossly inadequate public sale price:

Mere inadequacy of price, not attended by circumstances of fraud, misconduct, accident, mistake, or surprise tending to influence the result, is not sufficient to invalidate such a sale. Otherwise, the mere lack of competitive bids, or the intervening of any like circumstance whereby the price realized should be deemed inadequate, would be sufficient to render questionable the title obtained by sale under execution [citing cases]. This rule obtains

246. See *supra* notes 10-12 and accompanying text.

247. See Wechsler, *supra* note 3, at 889.

248. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1208.

249. *Id.*

generally with reference to judicial sales, as well as to sales under execution, and is applied more rigorously in those states in which the right of redemption exists. A gross inadequacy of price is competent, so far as it goes, to establish fraud; but it is not in itself, in the absence of other circumstances tending to show fraudulent behavior on the part of the sheriff or the plaintiff in the writ, enough to warrant the presumption that the sale was fraudulent.²⁵⁰

The court's unwillingness to set aside the sale for "mere inadequacy" of sale price was based on policy grounds. If a slight price inadequacy justified voiding the sale, the same would discourage the number of bidders, thus hampering competitive bidding.²⁵¹ The judicial "mere inadequacy" rule has been extensively criticized as providing no predictable standard of protection for the debtor; each case depends on its individual facts.²⁵² The rule also provides no stated objective standard of protection in the event of a disparity between price and value.²⁵³ Furthermore, the dearth of modern case law in Montana makes it impossible to predict the circumstances under which the court might apply the gross inadequacy rule.²⁵⁴ Other criticism centers on the highly subjective nature of the "shock the conscience" standard necessary to trigger a court ordered resale²⁵⁵ and the unstructured nature of evidence admissible to establish the true value of the property.²⁵⁶

B. Montana's Redemption Statutes

Montana's statutory right of redemption provides a more indirect source of regulating price adequacy.²⁵⁷ More than half of the states authorize a statutory right of redemption providing additional time for the mortgagor, its successor in interest, or, in many instances junior lienholders, to pay a certain sum of money, usually the foreclosure sale price, to redeem the title to the property.²⁵⁸ Montana's one year right of redemption is applicable to any property sold under the traditional mortgage, or presumably, upon ju-

250. *Burton v. Kipp*, 30 Mont. 275, 286, 76 P. 563, 565 (1904).

251. Washburn, *The Judicial and Legislative Response to Price Inadequacy in Mortgage Foreclosure Sales*, 53 So. CAL. L. REV. 843, 860 (1980).

252. *Id.* at 861.

253. *Id.*

254. Platt, *supra* note 230, at 45. Platt makes the same argument regarding the rule in Oregon.

255. Washburn, *supra* note 251, at 866.

256. *Id.* at 867.

257. MONT. CODE ANN. §§ 25-13-801 through -825 (1987). See also *infra* notes 281-87 and accompanying text.

258. NELSON & WHITMAN, *supra* note 2, § 8.4, at 616.

dicial foreclosure of a commercial deed of trust.²⁵⁹ In *Chunkapura*, the Montana Supreme Court eliminated any redemption right after the judicial foreclosure of an occupied, single-family residential deed of trust.²⁶⁰ The statutory right of redemption differs from the equity of redemption.²⁶¹ The mortgagor loses the latter after the mortgagee elects to accelerate the entire amount of the mortgage upon default by the mortgagor and obtains a decree of foreclosure.²⁶² The statutory right of redemption continues for one year after the sheriff's sale and applies in Montana to the traditional mortgage, a mortgage sold under the power of sale, and a commercial deed of trust foreclosed judicially.

In the non-judicial context, the grantor-mortgagor cannot redeem the property after a trustee sale of the deed of trust property.²⁶³ This forms a part of the *quid pro quo* between the creditor and the borrower: the creditor gives up the right to pursue the deficiency judgment and the borrower sacrifices the right of redemption.²⁶⁴ The debtor's virtually unlimited equity of redemption before the trustee's sale supplies another rationale for the elimination of the debtor's right of redemption in the non-judicial context: the debtor can escape acceleration of the debt by payment of ar-rears up to the trustee's sale.²⁶⁵

In the judicial context, the debtor who personally occupies the property has the right to remain in possession during the redemption period.²⁶⁶ Additionally, temporary Montana moratorium law creates a right of first refusal in the event of a sale or lease of the foreclosed property for the immediately preceding owner.²⁶⁷

Redemption is available to the judgment debtor, his spouse or his successor in interest, or if the debtor is a corporation, to the corporation or a stockholder.²⁶⁸ Redemption is also available to any creditor having a lien by judgment, mortgage, or attachment subse-

259. MONT. CODE ANN. §§ 25-13-801 through -825 (1987); *Chunkapura*, ____ Mont. at ____, 734 P.2d at 1205.

260. *Chunkapura*, ____ Mont. at ____, 734 P.2d at 1210-11.

261. See *supra* notes 5-7 and accompanying text.

262. NELSON & WHITMAN, *supra* note 2, § 7.6, at 489; *Dipple v. Neville*, 82 Mont. 280, 286, 267 P. 214, 218 (1928).

263. The purchaser at the trustee's sale obtains the title of the trustee free of any redemption right. MONT. CODE ANN. § 71-1-318 (1987). The purchaser can obtain possession within ten days after the sale. MONT. CODE ANN. § 71-1-319 (1987).

264. *Chunkapura*, ____ Mont. at ____, 734 P.2d at 1210.

265. MONT. CODE ANN. § 71-1-312 (1987).

266. MONT. CODE ANN. § 25-13-821 (1987).

267. MONT. CODE ANN. § 25-13-902 (1987). This moratorium law terminates June 30, 1996.

268. MONT. CODE ANN. § 25-13-801(1)(a) (1987).

quent to the encumbrance foreclosed.²⁶⁹ At any time within one year after the sale, the redemptioner can reacquire the property by tendering the equivalent of the purchase price plus six percent per annum interest on the purchase price, and assessments and taxes paid by the purchaser, plus interest thereon.²⁷⁰ Montana does not permit the creditor to include other advances such as management fees incurred during the redemption period in the redemption amount.²⁷¹ Montana law prohibits waiver of this statutory right of redemption prior to the foreclosure sale.²⁷² This prohibition also applies in the federal context to a Small Business Administration or Farmers Home Administration loan mortgage.²⁷³ The effect of redemption by the judgment debtor restores the debtor "to his [previous] estate," thus reviving any liens on the property junior to the lien foreclosed²⁷⁴ and causing a deficiency judgment obtained against the debtor to attach to the foreclosed property upon the debtor's redemption.²⁷⁵

Most notably, statutory redemption gives the debtor a second chance to repurchase the property for the amount bid at the sale.²⁷⁶ Theoretically, the redemption period allows the debtor time to rehabilitate his financial affairs and obtain financing for the repurchase of his home at the sale price. In practice, however, this "second chance" aspect of the redemption statute is rarely exercised due to the borrower's inability to obtain new financing.²⁷⁷ Data gathered from other states shows that mortgagors rarely redeem from a foreclosure sale.²⁷⁸ Studies in two counties in Iowa between 1881 and 1980 showed decennial incidences of redemption ranging from 3.9 percent to 25 percent.²⁷⁹ Studies in the Oregon counties of Clackamas, Marion, and Multnomah between 1970 and 1980 showed a decennial incidence of redemption of 9.8 percent.²⁸⁰

269. MONT. CODE ANN. § 25-13-801(1)(b) (1987).

270. MONT. CODE ANN. § 25-13-802 (1987).

271. *Lester v. J. & S. Investment Co.*, 171 Mont. 149, 153, 557 P.2d 299, 301 (1976).

272. MONT. CODE ANN. § 71-1-229 (1987).

273. *United States v. Ellis*, 714 F.2d 953, 957 (9th Cir. 1983); *United States v. Pastos*, 781 F.2d 747, 750 (9th Cir. 1986).

274. *Dipple v. Neville*, 82 Mont. 280, 287, 267 P. 214, 219 (1928).

275. *McQueeney v. Toomey*, 36 Mont. 282, 296, 92 P. 561, 565 (1907).

276. *Platt*, *supra* note 230, at 48.

277. *Id.* See also *Washburn*, *supra* note 251, at 931.

278. See *Washburn*, *supra* note 251, at 930-31 ("If the property is worth more than the sale price, it is theoretically possible for the mortgagor to secure financing to redeem the property.").

279. *Bauer, Statutory Redemption Reconsidered; The Operation of Iowa's Redemption Statute in Two Counties Between 1881 and 1980*, 70 IOWA L. REV. 343, 386-89 (1985).

280. Comment, *Oregon Statutory Right of Redemption—Any Redeeming Qualities?*, 16 WILLAMETTE L.J. 891, 915 (1980).

Further, the incidence of redemption from foreclosure sales in Washington between 1956 and 1960 was 1.1 percent.²⁸¹

More importantly, statutory redemption deters deliberate underbidding by the sale purchaser because a redemptioner need only pay the sale price, plus taxes, assessments, and 6 percent per annum interest.²⁸² The purchaser-creditor has therefore no incentive to bid the property below the amount of the debt owed. Otherwise, the creditor risks losing its lien to the redeeming debtor, or a redemptioner who has purchased the debtor's redemption rights,²⁸³ or a junior lien creditor entitled to redeem the property.²⁸⁴ In such event, the original purchaser-creditor becomes an unsecured creditor as to the amount of its bid not paid by the redemptioner who acquired its right through the debtor.²⁸⁵

The folklore of redemption theory only emphasizes the fact that a deficiency judgment will immediately attach to the debtor's property if the debtor redeems.²⁸⁶ However, studies show that the debtor rarely redeems anyway and that lenders rarely pursue deficiency judgments.²⁸⁷ Because the debtor's redemption right is a saleable commodity, the central thrust of the redemption statute in the commercial context insures that the purchaser-creditor bids no less than the amount owed. If the creditor bids any less, a second lienholder may obtain the property through the debtor at a windfall and render the purchaser-creditor unsecured as to the balance of the debt owed.

Although the redemption statute forces the creditor-purchaser to bid no less than the debt owed, the redemption right renders the title acquired by the sale purchaser defeasible and discourages

281. Shattack, *Security Transactions*, 36 WASH. L. REV. 303, 311 n.3 (1961).

282. MONT. CODE ANN. § 25-13-802 (1987); Washburn, *supra* note 251, at 931.

283. See *Brown v. Timmins*, 79 Mont. 246, 256 P. 176 (1927); *Baker v. Pennsylvania Fire Ins. Co.*, 81 Mont. 271, 263 P. 93 (1928).

284. MONT. CODE ANN. § 25-13-801 (1987).

285. The redemptioner acquiring its right through the debtor need only pay the purchaser-creditor the amount of the bid price, plus 6 percent statutory interest and limited costs and assessments. MONT. CODE ANN. § 25-13-802 (1987); *Hamilton v. Hamilton*, 51 Mont. 509, 154 P. 717 (1916). The balance of the debt owed to the creditor, if the debtor or his assigns redeems, is not secured by any lien. If the redemptioner does not acquire its right through the debtor, it must pay the senior lien holder's lien amount plus interest, etc.. MONT. CODE ANN. § 25-13-803 (1987).

286. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1205.

287. Wechsler, *supra* note 3, at 878. In the New York data gathered by Wechsler only one of ninety-four foreclosure sales resulted in a deficiency, and in that case the judgment was unsatisfied. Wechsler also notes that lenders rarely pursue deficiency judgments in the residential context because the debtor is *in extremis* already. *Id.* at 895-96. The rationale, however, does not apply in the commercial context.

competitive bidding at the sale, thus depressing the sale price.²⁸⁸ Redemption schemes also increase the cost of credit by increasing interest rates charged and reducing loan value ratios (thus increasing down payments).²⁸⁹ In an exhaustive study of the costs of judicial foreclosure and statutory redemption in Iowa, the author candidly states, "admittedly, the empirical evidence that presently is available falls far short of demonstrating judicial foreclosure and statutory redemption produce such a profusion of benefits that those states in which they presently do not exist should embrace them."²⁹⁰ The author also demonstrates that a radical difference exists in the average cost of uncontested non-judicial foreclosures and the average cost of uncontested judicial foreclosures,²⁹¹ reflected in terms of increased interest rates and down payments to the prospective borrower.²⁹²

Applied to Montana, the credit costs of judicial foreclosure and redemption are substantial enough to warrant legislative inquiry as to whether these costs outweigh the redemption statute's effect on deterring deliberate underbidding in commercial and residential contexts. Eliminating the right of redemption for the judicial foreclosure of the residential deed of trust (as in *Chunkapura*) may reduce credit costs. However, the countervailing increase in credit costs caused by *Chunkapura*'s elimination of the deficiency judgment renders the net effect of the decision uncertain.

IX. FAIR MARKET VALUE—IS IT NECESSARY IN LIGHT OF MONTANA'S REDEMPTION STATUTE?

A. Fair Market Value

The court in *Chunkapura* urged the Montana Legislature to consider the enactment of fair market value legislation, sending copies of the decision to the speaker of the house of the 1987 Montana Legislature.²⁹³ The need for such legislation must be assessed in light of Montana's redemption statute and other substantive Montana anti-deficiency law.

288. Washburn, *supra* note 251, at 854 n.57 and accompanying text.

289. Bauer, *supra* note 279, at 376-81; Comment, *Cost and Time Factors in Foreclosure of Mortgages*, 3 REAL PROP., PROB. & TR. J. 413 (1968).

290. Bauer, *supra* note 279, at 375.

291. *Id.* at 378-79.

292. *Id.* at 351 n.35, where Bauer concludes that in the final analysis "[t]he actual effects of judicial foreclosure and statutory redemption . . . are some reduction in the size of mortgage loans, some increase in mortgage loans interest rates, or a combination of the two."

293. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1209.

Legislatures enact fair market value legislation primarily in response to falling land values when forced sales bring only nominal sale prices, resulting in increased deficiency exposure to the debtor.²⁹⁴ Instead of focusing on measures aimed at insuring an adequate sale price, the fair market value statutes abandon the foreclosure sale price obtained as the test for the deficiency.²⁹⁵ Fair market value statutes limit the deficiency to an established value rather than by a percentage of value as under "upset" appraisal statutes.²⁹⁶ Courts determine valuation through testimony, often witnesses for the parties, although some statutes authorize court appointed appraisers.²⁹⁷ "Seventeen states have [fair market] value legislation providing that the amount of the deficiency judgment must be based on the greater of statutorily determined fair market value or sale price."²⁹⁸ Procedurally, in most states "the evidentiary hearing occurs upon the creditor's deficiency complaint, which sets forth the creditor's allegation of the fair value."²⁹⁹ The debtor must then introduce evidence of fair value. The Idaho Code provides an example of such a statute placing the burden on the creditor:

No court in the State of Idaho shall have jurisdiction to enter a deficiency judgment in any case involving a foreclosure of a mortgage on real property in any amount greater than the difference between the mortgage indebtedness, as determined by the decree, plus costs of foreclosure and sale, and the reasonable value of the mortgaged property, to be determined by the court in the decree upon the taking of evidence of such value.³⁰⁰

Idaho also applies the fair market value statute to a judicial foreclosure of a deed of trust.³⁰¹ Nevada's statute provides a more formal procedure.³⁰²

The Idaho and Nevada statutes fail to protect the mortgagee

294. NELSON & WHITMAN, *supra* note 2, § 8.3, at 601-02.

295. *Id.*

296. Washburn, *supra* note 251, at 907-08.

297. *Id.* at 908.

298. *Id.*

299. *Id.* at 909.

300. IDAHO CODE § 6-108 (1987).

301. IDAHO CODE § 45-1512 (1987).

302. NEV. REV. STAT. § 40.455 (1987) applies to both judicial and non-judicial sales. Under the Nevada statute, within three months after the sale, upon fifteen days' notice, the party requesting the deficiency must request a fair market value hearing. Either party can present evidence. Ten days prior to the hearing the court or either party can request a court appointed appraiser to impartially appraise the property, and this appraisal is admissible evidence of value of the property. The amount of the deficiency is the lesser of the debt minus the fair market value or sale price.

when a third-party purchaser purchases the property at the sale. The mortgagee must credit the higher fair market value rather than the presumptively lower sale price against the debt. Thus, if not the purchaser, the mortgagee does not receive the economic equivalent of the difference between the fair market value and the sale price. Commentators frequently criticize this aspect of fair market value statutes.³⁰³ South Dakota addresses the problem by limiting application of the fair market value statute to sales in which the mortgagee is the successful bidder.³⁰⁴

If the fair market value is less than the judgment amount, under the South Dakota statute the mortgagee has the burden of proving that its bid equals the fair market value.³⁰⁵ The court then credits either the fair market value or sale price, whichever is greater, against the debt for the purpose of determining the deficiency. Other statutes place this burden on the debtor to prove that the fair market value exceeds the bid amount.³⁰⁶

For obvious reasons, a fair market value statute based on existing market values achieves its objective only when fair market valuation occurs at or near the time of the judicial sale. Accordingly, most such statutes require that the valuation occur within a short time following the sale, typically no more than ninety days.³⁰⁷ Yet by their use of intrinsic or future valuation, certain fair market value statutes in depressed periods yield values higher than the market price because judicial sales during an economic depression reflect prices equal to actual market values.³⁰⁸ Courts thus entertain a policy-based fiction that a value credit is the best possible solution to price inadequacy when values are generally depressed.³⁰⁹

303. NELSON & WHITMAN, *supra* note 2, § 8.3, at 602; Washburn, *supra* note 251, at 911.

304. S.D. CODIFIED LAWS ANN. §§ 21-47-15 through -16; 21-48-13 through -14 (1988).

305. Washburn, *supra* note 251, at 912.

306. *See, e.g.*, MICH. COMP. LAWS ANN. § 600.3280 (West 1968); Washburn, *supra* note 251, at 912.

307. Washburn, *supra* note 251, at 913.

308. Washburn, *supra* note 251, at 913-14, noting:

If the property brings a low foreclosure sale price as a result of a general or local economic depression, a market value determination will yield a correspondingly depressed amount. The statutory fair market value in depressed periods may be somewhat higher than the sale price, since judicial sales do not yield prices equal to current market values. A valuation in the same market environment, however, will often simply confirm the depressed sales price and will not yield an amount equal to the intrinsic or future value of the property.

Id.

309. *Id.* at 914. *See also* Skilton, *Assessing the Mortgage Debtor's Personal Liability*, 90 U. PA. L. REV. 440, 451-52 (1942).

Montana does not need fair market value protections. After foreclosure of a two-party purchase money mortgage or a judicial foreclosure of an occupied, single-family residential deed of trust, the debtor has no deficiency exposure under either such foreclosure.³¹⁰ *Chunkapura's* invitation to the Montana Legislature to enact fair market value legislation therefore seems enigmatic. However, a Montana residential and commercial non-purchase money mortgage debtor still faces deficiency exposure, as does a borrower under a commercial deed of trust.³¹¹ If the legislature enacts fair market value legislation to limit deficiency exposure under the commercial deed of trust or mortgage, this may unwisely increase the cost of credit by increasing interest rates and reducing loan to value ratios.³¹² When the value of real property collateral is, or may be, insufficient to cover the loan, the lender often relies on the commercial developer's individual net worth and the possibility of recourse to additional personal property or collateral security. Limiting the creditor's recourse to the difference between the higher of the sale price bid or the fair market value on the remaining amount of debt ignores Montana's redemption scheme which already protects the Montana commercial deed of trust or mortgage debtor to the extent that the real value of the property exceeds the amount bid at the sheriff's sale. Thus, Montana's redemption statute already adequately protects the commercial borrower. As a policy matter, full deficiency exposure does not unfairly disadvantage the commercial borrower since commercial borrowers typically understand the risk involved with real property ownership in times of fluctuating property values.³¹³

X. MEANS OF IMPROVING PRICES PAID AT DISTRESS SALES

A. *Judicial and Non-Judicial Sales of Distressed Property*

1. *Overview of the Notice of Sale Procedures for Sheriff's and Trustee Sales in Montana*

Montana's judicial foreclosure scheme requires compliance

310. MONT. CODE ANN. § 71-1-232 (1987); *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1210.

311. *Id.*; MONT. CODE ANN. § 71-1-232 (1987).

312. Commercial deeds of trust would not be as salable on the secondary mortgage market with fair market legislation governing their foreclosure since that may delay the lender from acquiring free title. See generally *Congressional Findings for the Proposed Federal Mortgage Foreclosure Act H.R. 10688 and S. 2507*, 93d Cong., 1st Sess. (1973); Comment, *Cost and Time Factors in Foreclosure of Mortgages*, 3 REAL PROP., PROB. & TRUST J. 413 (1968).

313. Platt, *supra* note 230, at 55.

with the general provisions of Montana's execution of judgment statutes.³¹⁴ After the court has entered the foreclosure decree, the creditor must post a notice, as prescribed by statute, for twenty days in three public places of the township or city where the property is situated and where the property is sold.³¹⁵ The creditor must also publish the notice once a week for twenty days in "some newspaper published in the county, if there be one"³¹⁶

Montana's non-judicial foreclosure scheme contains substantially stricter notice requirements than Montana's judicial scheme. The debtor and all persons having a lien or interest of record subsequent to the interest of the debtor and all other persons must be given 120 days' notice by certified mail.³¹⁷ Additionally, the creditor must publish the notice of sale at least forty-one days prior to the sale in a newspaper of general circulation where the property is located,³¹⁸ or must post the property with the recorded notice of sale at least twenty days before the sale date.³¹⁹

2. Constitutional Notice Requirements

If the creditor fails to comply with any of these notice requirements, he has arguably violated "notice" protections under the due process clause of the fourteenth amendment.³²⁰ Additionally, if the debtor never receives notice of his right to contest the existence of a default at any time in the non-judicial foreclosure proceeding, the creditor risks violating the requirement under the due process clause of the fourteenth amendment that the debtor be given the opportunity for a hearing before being deprived of a significant property interest.³²¹

314. MONT. CODE ANN. §§ 25-13-701 through -714 (1987).

315. MONT. CODE ANN. § 25-13-701(1)(c) (1987).

316. MONT. CODE ANN. § 25-13-701(1)(c) (1987).

317. MONT. CODE ANN. § 71-1-315(1)(a) (1987).

318. MONT. CODE ANN. § 71-1-315(1)(c) (1987). The statute requires the last publication to be made at least twenty days before the date fixed for the trustee's sale. The publication must occur once a week for three consecutive weeks. First publication is, therefore, forty-one days prior to sale.

319. MONT. CODE ANN. § 71-1-315(1)(b) (1987).

320. See, NELSON & WHITMAN, *supra* note 2, § 7.24 at 562-64, and *Mennonite Bd. of Missions v. Adams*, 462 U.S. 791, 795 (1983) (where the Court emphasized that constructive notice alone does not satisfy the requirement that the type of notice used must be reasonably calculated to apprise interested parties) (citing *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 314 (1950)).

321. NELSON & WHITMAN, *supra* note 2, § 7.25, at 566-69 (citing *Sniadach v. Family Fin. Corp.*, 395 U.S. 339 (1969); *Fuentes v. Shevin*, 407 U.S. 67 (1972), *reh'g denied*, 409 U.S. 902 (1972)).

In Montana, the creditor usually gives the debtor written notice of his right to contest the existence of a default in the initial notice of default that precedes the commencement of

3. Debtor's Right to Direct the Sale

At the sale, the judgment debtor can direct the order in which the real or personal property is to be sold and can require separate sales of known lots or parcels if this generates a higher sale price.³²² The Montana Supreme Court has interpreted this statute to allow a debtor to compel the creditor to sell commercial property before residential property.³²³ If the foreclosure decree specifies that the property must be sold *en masse* and the debtor fails on the record to establish the prejudicial effect of such a sale method, there is no error in permitting the property to be sold *en masse* as described in the mortgage.³²⁴ If the foreclosure decree does not specify the manner of the sale of the property, the statutory provisions giving the debtor the right to direct the sale would control the transaction.³²⁵ Because there is no decree otherwise directing the sale of the property in the non-judicial context, the trustee determines how to sell the property; however, upon reasonable notice to the trustee, the debtor can direct the order of the sale.³²⁶

Both the judicial and non-judicial statutory schemes require that the property be sold to the highest bidder.³²⁷ However, only the non-judicial scheme explicitly requires "cash."³²⁸ The judicial scheme contains no cash requirement, but Montana does require sheriff's sales of personal property to be done in cash.³²⁹

XI. CRITICISMS OF MONTANA'S NOTICE AND SALE REQUIREMENT

A. Criticism of the "Cash Only" Requirement

The creditor at the judicial and non-judicial sale has a distinct advantage over other bidders because he can receive a credit

the non-judicial foreclosure by thirty days. Even if this notice is not given, some courts hold that the debtor's right to enjoin the foreclosure process by suit comports with the "opportunity for a hearing" requirements. NELSON & WHITMAN, *supra* note 2, § 7.25, at 569 (citing Laughlin v. Walters, 718 F.2d 513 (1st Cir. 1983); Fitzgerald v. Cleland, 650 F.2d 360 (1st Cir. 1987); Young v. Ridley, 309 F. Supp. 1308 (D.D.C. 1970). *But see* Turner v. Blackburn, 389 F. Supp. 1250 (W.D.N.C. 1975); Northrip v. Federal Nat'l Mortgage Ass'n, 372 F. Supp. 594 (E.D. Mich. 1974), *rev'd on other grounds*, 527 F.2d 23 (6th Cir. 1975)).

322. MONT. CODE ANN. § 25-13-704 (1987).

323. First Nat'l Bank v. Powell, ___ Mont. ___, ___, 689 P.2d 255, 257 (1984).

324. Elston v. Hix, 67 Mont. 294, 298-300, 215 P. 657, 659 (1923); Thomas v. Thomas, 44 Mont. 102, 119 P. 283 (1911).

325. MONT. CODE ANN. § 25-13-704 (1987).

326. Powell, ___ Mont. at ___, 689 P.2d at 255.

327. MONT. CODE ANN. §§ 71-1-315(4), 25-13-704 (1987).

328. MONT. CODE ANN. § 71-1-315(4) (1987).

329. Proto v. Missoula County, ___ Mont. ___, ___ P.2d ___, 45 St. Rptr. 265 (1988).

against the judgment amount for his bid (an "exchange of credits") instead of a cash payment.³³⁰ This advantage, it is argued, discourages competitive bidding by third-party bidders at the sale and suppresses actual sale prices.³³¹

B. Criticisms of the Advertising Requirements

Judicial and non-judicial foreclosures usually result in advertising in the legal column of local newspapers, posting of notice on the property and posting of notice at the courthouse. These kinds of notice devices have been criticized as not conveying notice of the sale to the general real estate market.³³² As a result of failing to apprise the public of the impending foreclosure sale, only a limited group of speculators or investors who are interested in buying the property at low prices attend the sale.³³³ Because similar notice and sale provisions in other jurisdictions constitute a major cause of price inadequacy in foreclosure sales, these defects in both Montana's judicial and non-judicial foreclosure notice requirements present a serious problem.³³⁴

In Montana, under both the judicial and non-judicial foreclosure scheme, the creditor engages a local newspaper to print the sale notice in the paper's legal section. However, as shown above, printed legal advertisements buried in the newspaper do not attract the general public. Additionally, the absence of necessary descriptive information fails to inspire further inquiry by the general public.

XII. PROPOSED REFORMS

A. Commercial Advertising and Plain Language

The Uniform Land Transactions Act³³⁵ provides a starting

330. Washburn, *supra* note 251, at 849 (citing *inter alia* Barnard v. First Nat'l Bank, 176 Okla. 326, 328, 55 P.2d 972, 974 (1936)).

331. Washburn, *supra* note 251, at 849.

332. See, NELSON, *Deficiency Judgments After Real Estate Foreclosures in Missouri: Some Modest Proposals*, 47 Mo. L. REV. 151, 152 (1982); Tefft, *The Myth of Strict Foreclosure*, 4 U. CHI. L. REV. 575 (1937).

333. Washburn, *supra* note 251, at 848 (citing, *inter alia*, Fairchild, *Foreclosure Methods and Costs: A Reevaluation*, 7 BROOKLYN L. REV. 1, 4 (1937); Durfee & Doddridge, *Redemption from Foreclosure Sale—the Uniform Mortgage Act*, 23 MICH. L. REV. 825 (1925)).

334. See, Washburn, *supra* note 251, at 896. See also, Durfee and Doddridge, *supra* note 333, at 832; Tefft, *supra* note 333, at 589-90.

335. Although not adopted by any state due to its monumental objective of unifying state foreclosure law, the Uniform Land Transactions Act (ULTA) (1975 original text) provides helpful proposals because its overall assumption is that both the creditor's and debtor's interests are best served when the property commands the best price on disposi-

point for revisions to Montana's judicial notice and sale provisions.³³⁶ The Act requires the creditor to use the method that is "reasonable under the circumstances" and contemplates the use of a real estate agent or real estate advertisement to reach the broadest possible class of potential third-party bidders.³³⁷ Mere advertisement in a legal publication does not meet that section's requirements of "commercial reasonableness."³³⁸ The breadth of the standard forces the mortgagee to make an affirmative effort to offer the type of property sold to known markets in the real estate community involved, resulting in increased exposure and salability. Increased advertisement also broadens the group of potential bidders who may become aware of the sale. Data showing that advertisement in the legal section of the newspaper does not attract the general public makes this aspect of the Act compelling.³³⁹

In addition to the method of advertising, the content of the foreclosure notice should be clarified. Elimination of esoteric legal descriptions and legalese in favor of "normal, commercial descriptive, and pictorial advertising" could better attract the public.³⁴⁰ Additional information should include a description of the use of the real estate, the street address, the zoning designation, and available financing terms, if any. Such information would permit a potential bidder to inspect the property, possibly triggering increased bidding at the sale.

B. *Increasing Time for Financing*

Increasing the time between the first public notice and the sale date of the foreclosed property could facilitate financing for potential third-party bidders.³⁴¹ The time given to the public to obtain financing under Montana's judicial scheme can be as short as twenty days,³⁴² while under the non-judicial scheme the initial publication can occur as close as forty-one days to the date of sale.³⁴³ These first notice dates should be extended back to enable

tion. ULTA § 3-505, comment 1 (1975).

336. ULTA § 3-508(a) (1975).

337. ULTA § 3-508(a) (1975).

338. ULTA § 3-508(a) (1975).

339. Nelson, *supra* note 332, at 163. Washburn, *supra* note 251, at 896; Wechsler, *supra* note 3, at 891.

340. Nelson, *supra* note 332, at 163.

341. Financing approval can take as long as two months at certain lending institutions. Increasing the first notice period to comply with the realities of time in commercial loan approval time frames could result in increased competitive bidding.

342. MONT. CODE ANN. § 25-13-701 (1987).

343. MONT. CODE ANN. § 71-1-315(1)(c) (1987).

an interested third-party bidder adequate time to obtain financing.

C. *Down Payment at the Sale*

The requirement that the third-party bidder pay cash at the sale chills competitive bidding, especially in light of the mortgagee's ability to exchange credits and avoid cash outlay at the sale.³⁴⁴ To compensate for this disadvantage, the Uniform Land Transactions Act permits the third-party bidder to pay with a "bank obligation" or to deposit 10 percent of the bid price in cash and pay the remaining balance within five weeks.³⁴⁵ If the bidder fails to make the deposit or complete the sale, the seller may resell the property or bring an action for specific performance.³⁴⁶ Montana allows the sheriff to recover only the amount occasioned by the loss on resale to the second bidder,³⁴⁷ but does not afford any flexibility in financing or specific performance remedies. The flexible ULTA provision promotes competitive bidding; Montana's judicial and non-judicial sales statutes should be amended accordingly.

D. *Court Confirmation*

Montana does not require court confirmation of the judicial and non-judicial sale price.³⁴⁸ The ULTA requires post-sale court confirmation insuring that creditors comply with the Act's notice and sale provisions.³⁴⁹ The person conducting the sale must report to the court, which confirms the sale if "justice has been done."³⁵⁰ The ULTA does not contain any fair market value standard for confirmation, but leaves the decision to the court's discretion on a case-by-case basis.³⁵¹

Although Montana does not require judicial confirmation, the court in *Chunkapura* urged the Montana Legislature to enact fair market value legislation that is in effect a type of confirmation.³⁵² Assuming that some kind of confirmation legislation is necessary,³⁵³ the ULTA court confirmation standard is more realistic be-

344. Washburn, *supra* note 251, at 849.

345. ULTA § 3-508(b) (1975).

346. ULTA § 3-508(b) (1975).

347. MONT. CODE ANN. § 25-13-705 (1987).

348. Interior Sec. Co. v. Campbell, 55 Mont. 459, 466, 178 P. 582, 584 (1919).

349. ULTA § 3-509 (1975).

350. ULTA § 3-509 (1975).

351. ULTA § 3-509 (1975).

352. *Chunkapura*, ___ Mont. at ___, 734 P.2d at 1209 (1982).

353. Arguably, Montana's redemption scheme for commercial properties and anti-deficiency rules already protect the debtor from deliberate underbidding by the creditor. See

cause, unlike the inherent or intrinsic fair market value statutes,³⁵⁴ the court need not make a value credit for properties that are otherwise incapable of valuation on the market. Rather, such a credit would constitute only one of many factors the court can use to confirm the sale. Additionally, the ULTA confirmation standard permits sufficient flexibility to prevent, at the court's discretion, a "battle of the appraisers" at the confirmation hearing.

XIII. CONCLUSION

Ambiguity permeates Montana's judicial and non-judicial mortgage foreclosure statutes. *First State Bank v. Chunkapura* raises numerous questions regarding the judicial foreclosure of a Montana deed of trust. *Pulse v. North American Title Co.* creates numerous questions relating to Montana's purchase money mortgage statute. The call for fair market value legislation in light of Montana's redemption scheme raises serious questions about the need for fair market value legislation. The ambiguities governing Montana's one action rule regarding a single obligation secured by personal and real property serve neither the creditor or debtor. Such ambiguity only creates the opportunity for litigation to "represent one's client" and "clarify the law" at the expense of either the debtor or the creditor. Additionally, Montana's sheriff's sale and trustee's sale statutes do not promote active and competitive bidding or realistically apprise buyers of the nature of the property subject to sale.

Any state's judicial and non-judicial mortgage foreclosure scheme cannot reverse adverse economic trends. However, as the historical development of mortgage foreclosure law reveals, the broad policy of mortgage foreclosure law is to minimize deficiency exposure to the buyer, while affording the creditor access to its collateral in partial or total satisfaction of the unpaid debt. If modernized and streamlined, Montana's mortgage foreclosure statutes could more effectively accomplish those policies.

supra notes 293-313 and accompanying text. In any event, confirmation should be required only if the lender seeks a deficiency judgment.

354. See *supra* notes 294-303 and accompanying text.

