

Foreclosures-
Supreme Court
Cases

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*Sure for Thursday's
H/B meeting* *March 1, 1988*

February 26, 1988

The Honorable Jan Faiks
President Alaska State Senate
P.O. Box V
Juneau, Alaska 99801

Re: Foreclosures

Dear Senator Faiks:

As if the debtor were not under enough pressure, the Alaska Supreme Court has just made it more difficult. I have enclosed the February 26, 1988, cases decided by our supreme court. These decisions allow the lender to place the consumer under serious financial pressure far beyond that which the Legislature intended when the statutes were enacted.

The first case is Moening v. Alaska Mutual Bank, decided February 26, 1988. The case holds that the lender may elect to pursue an action on the note and obtain a judgment against the debtor for all sums due on the promissory note (deed of trust note). In the event the lender cannot collect all sums due on the note, they can then recover the balance of their money through foreclosure, either nonjudicial or judicial.

In Conrad v. Counselor Investment Co., decided February 26, 1988, the court held that the lender may pursue the debtor despite specific language in the deed of trust. This is so, says the court, because the inclusion of the language was not an election of that remedy. In short, says the court, the inclusion of specific language was not an exclusion of other remedies. How a consumer would know the difference is beyond me. To illustrate the point, all of the other defendants in Conrad were attorneys.

I'm sure that a review of these cases will cause you concern for the vast majority of AHFC borrowers who were told that if there was a default the mortgage insurance would pay the mortgage. No one was even told that they were at risk for a separate law suit. Certainly, the banks and other closing agents always tied a default to foreclosure and mortgage insurance. I believe that such specific representations created substantial confusion at the time of closing these loans in light of the rights the lenders held. Certainly, the representations as to the applicability of the mortgage insurance coverage appears to have been erroneous and thus fits the definition of either innocent or negligent misrepresentation.

The Honorable Jan Faiks
February 29, 1988
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I believe legislation to curb the lenders' powers must be introduced immediately. I suggest that the lender, upon default, must be compelled to foreclose and, as part of the foreclosure process, be compelled to bid a fair market value (not a distressed market value). Once the fair market value is bid, the mortgage insurance should be applied to the difference and then the lender could receive a judgment for any remaining deficiency.

If I can be of any assistance, please contact me.

Sincerely,

LAW OFFICES OF WILLIAM L. McNALL

By: William L. McNall
William L. McNall

WLM/sel

Enclosures - as stated.

cc: The Honorable Rick Halford
The Honorable Kay Brown

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THE SUPREME COURT OF THE STATE OF ALASKA

HAROLD J. MOENING and
COLLEEN M. MOENING,

Appellants,

v.

ALASKA MUTUAL BANK,

Appellee.

File No. S-1980

O P I N I O N

[No. 3274 - February 26, 1988]

Appeal from the Superior Court of the State
of Alaska, Third Judicial District, Anchorage,
Milton M. Souter, Judge.

Appearances: Francis J. Nosek, Jr. and Kelly
Fisher, Anchorage, for Appellants. Gordon F.
Schadt and Milford H. Knutson, Anchorage, for
Appellee.

Before: Matthews, Chief Justice, Rabinowitz,
Compton, and Moore, Justices. [Burke,
Justice, not participating.]

COMPTON, Justice.

This appeal presents three questions. The first question is whether a secured creditor initially may ignore the security and sue for a personal judgment on the underlying debt, absent an agreement to the contrary. The second is whether the creditor agreed to limit its remedy to foreclosure of the security. The third is whether the suit on the debt extinguishes the security as a matter of law.

I. FACTUAL AND PROCEDURAL BACKGROUND

Harold Moening and Ronald Rivard became business associates in 1983. Prior to their association, Rivard was the sole shareholder of Quest Enterprises, Inc. (Quest). Moening agreed to guarantee Quest's debts to Alaska Mutual Bank (AMB) in exchange for a 40% interest in the business.¹

To effectuate the guarantee, Moening executed a \$700,000 deed of trust note in favor of AMB.² The note was secured by a deed of trust on Moening's home, and on the property which originally secured the Quest obligations extinguished by the consolidation. Moening defaulted. Later Moening executed a secured promissory note for \$33,000 to guarantee the debt for

1. Colleen Moening is a named defendant because she co-signed many of the obligations with her husband Harold Moening.

2. The principal was payable on demand in a single installment. Absent a demand, the note was due on May 7, 1985.

property purchased by Quest in Peters Creek.³ Moening defaulted on this note as well.

AMB filed a complaint against Moening seeking a personal judgment on the notes. It did not foreclose the deeds of trust nor attempt to exercise the power of sale. The superior court entered summary judgment for AMB, concluding that AMB had the right initially to ignore its security and sue on the note. The court entered a money judgment for \$733,000 in principal due on the notes, plus accrued interest, costs, and attorney's fees. In addition, the court ordered that the notes should be filed with the court, marked "Conditionally Cancelled" and, "if subsequent execution on the judgment does not satisfy it, the amount by which it is not satisfied may form the basis of judicial or non-judicial foreclosure of the collateral securing the promissory notes."

Moening appeals on the grounds that (1) as a matter of law, AMB must exhaust the security first; (2) AMB agreed to exhaust the security first; and (3) AMB waived its security by suing on the notes.⁴ For the reasons hereinafter set forth, we affirm the judgment of the superior court.

3. The note was secured by a deed of trust identical to that securing the \$700,000 note. The trust deed is not part of the record.

4. Moening also argues that AMB failed to join indispensable parties (Rivard and Quest). Alaska R. Civ. P. 19(b). This is an action to collect a debt. Neither Rivard nor

(Footnote Continued)

II. THE RIGHTS OF A SECURED CREDITOR

Moening argues that a secured creditor may not ignore the security and sue on the underlying obligation; it must first exhaust the security. AMB contends that a secured creditor has the option to foreclose or sue on the note, and that it may pursue these remedies concurrently or consecutively.

Statutes provide a secured creditor with a variety of remedies when the debtor defaults. For example, the creditor may bring an action for judicial foreclosure. AS 09.45.170.⁵ The creditor is then entitled to a deficiency judgment against the debtor. Id.; Smith v. Shortall, 732 P.2d 548, 549 (Alaska 1987); Suber v. Alaska State Bond Comm., 414 P.2d 546, 555-56 (Alaska

(Footnote Continued)

Quest was a party to the note and neither has an interest in this lawsuit. Civil Rule 19(a)(2). Moreover, their absence does not preclude granting complete relief between Moening and AMB. Civil Rule 19(a)(1). The fact that Moening may have claims against Rivard arising from other agreements, or that Rivard and Quest may have interests of record in the security, does not render them indispensable to AMB's suit on the note.

5. AS 09.45.170 provides:

A person having a lien upon real property, other than that of a judgment, whether created by mortgage or otherwise, to secure a debt or other obligation may bring an action to foreclose the lien. In the action, the court may direct the sale of the encumbered property or a portion of it and the application of the proceeds of the sale to the payment of costs, expenses of sale, and the amount due the plaintiff. The judgment shall also determine the personal liability of a defendant for the payment of the debt secured by the lien and be entered accordingly.

1966). The debtor has a statutory right of redemption for twelve months after the sale is confirmed. AS 09.45.190, 09.35.250.

The creditor may elect to conduct a nonjudicial foreclosure sale if the deed of trust provides for this remedy. Suber, 414 P.2d at 555-56; AS 34.20.070(a).⁶ The creditor is not entitled to a deficiency judgment following a nonjudicial foreclosure. Smith, 732 P.2d at 549; AS 34.20.100.⁷ The debtor is not entitled to redeem the property, unless the deed of trust provides otherwise. AS 34.20.090(a).

6. AS 34.20.070(a) provides in part:

If a deed of trust is executed conveying real property located in the state to a trustee as security for the payment of an indebtedness and the deed provides that in case of default or noncompliance with the terms of the trust, the trustee may sell the property for condition broken, the trustee, in addition to the right of foreclosure and sale, may execute the trust by sale of the property, upon the conditions and in the manner set forth in the deed of trust, without first securing a decree of foreclosure and order of sale from the court
.....

(Emphasis added).

7. AS 34.20.100 provides:

When a sale is made by a trustee under a deed of trust, as authorized by AS 34.20.070 -- 34.20.130, no other or further action or proceeding may be taken nor judgment entered against the maker or the surety or guarantor of the maker, on the obligation secured by the deed of trust for a deficiency.

Statutes also refer to an action on the underlying obligation. Alaska Statute 09.45.200 provides:

During or after the pendency of an action for the recovery of a debt secured by a lien mentioned in AS 09.45.170, an action cannot be maintained for the foreclosure of the lien unless judgment is given in that action that the plaintiff recover the debt or a part of it, and an execution issued in the action against the property of the defendant is returned unsatisfied in whole or in part.

WAM

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The clear implication of this section is that the creditor may sue directly on the note without first foreclosing the property. Moreover, if the creditor prevails in the legal action and cannot satisfy the judgment against the debtor's personal property, it may then maintain an action for judicial foreclosure of the security.

The superior court order also permits AMB to foreclose nonjudicially if the judgment on the note is returned unsatisfied. Moening argues that, even if AMB initially may ignore the security, it may not foreclose nonjudicially after obtaining a judgment on the note.

The anti-deficiency statute prohibits a deficiency judgment following exercise of a power of sale; however, it does not preclude the exercise of a power of sale following a judgment on the note. AS 34.20.100, supra note 7. Under the common law, a prior suit on the note does not preclude subsequent judicial or nonjudicial foreclosure of the security. Foothills Holding Corp. v. Tulsa Rig, Reel & Mfg., 393 P.2d 749, 751 (Colo. 1964); Berg

v. Liberty Fed. Savings & Loan, 428 A.2d 347, 348-49 (Del. 1981); Klondike, Inc. v. Blair, 211 So. 2d 41, 42-43 (Fla. App. 1968).

The doctrine of election of remedies does not apply, because foreclosure and a suit on the note are not inconsistent remedies. Klondike, 211 So. 2d at 42; Norwood Realty v. First Fed. Savings & Loan, 109 S.E. 2d 844 (Ga. App. 1954); Skach v. Lydon, 306 N.E. 2d 482, 485 (Ill. App. 1973). See also 55 Am. Jur. 2d Mortgages § 543, at 523 (1971).

We conclude that the statutes permit a secured creditor initially to ignore the security and sue on the note. Once the creditor obtains a personal judgment which is returned unsatisfied in whole or in part, the creditor may judicially or nonjudicially foreclose the security.⁸

8. In Smith v. Shortall, 732 P.2d at 549, we held that a spouse who nonjudicially foreclosed a deed of trust securing her former husband's property division obligation was not entitled to a deficiency judgment under AS 34.20.100. In dicta we stated:

The obligation was evidenced by a promissory note and secured by a deed of trust. When [Debtor] defaulted on the obligation, [Creditor] had several options. She could have waived the security of the deed of trust and sued on the note. Or, she could have brought an action to judicially foreclose the deed of trust, retaining the right to recover a deficiency judgment. AS 09.45.170; Suber v. Alaska State Bond Committee, 414 P.2d 546, 555 (Alaska 1966). Instead, [Creditor] elected the remedy of non-judicial foreclosure. By electing this remedy, [Creditor] lost her right to recover a deficiency judgment against [Debtor].

(Footnote Continued)

III. THE PARTIES' AGREEMENT

When a note is executed and secured by a deed of trust, the documents are read and construed together as one contract to ascertain the parties' intent. In re Sutton Inv., 266 S.E.2d 686, 689 (N.C. App. 1980), rev. denied, 301 N.C. 90 (1980); Herrington v. Murphy, 446 P.2d 595, 597 (Okla. 1968). The contract is interpreted to give effect to the reasonable expectations of the parties, looking to the language of the contract, the circumstances surrounding its adoption, and case law interpreting similar agreements. Craig Taylor Equip. v. Pettibone Corp., 659 P.2d 594, 597 (Alaska 1983). Ambiguities are construed in favor of the debtor. Patton v. First Fed. Sav. & Loan Ass'n, 578 P.2d 152, 156 (Ariz. 1978).

Any agreement between the parties that the creditor will not seek a deficiency judgment and will look only to the security is enforceable. Stern v. Itkin Bros., 385 N.Y.S.2d 753, 754 (N.Y. Sup. 1975).⁹ Such an agreement is enforced even when the security is destroyed by foreclosure of a superior lien. The

(Footnote Continued)

Id. We disapprove of this dicta insofar as it suggests that a suit on the note constitutes a legal waiver of the security.

9. A rider to the Stern mortgage provided in part:

On default hereunder, no deficiency judgment shall be sought, rendered or entered against the mortgagor and mortgagees will look only to the mortgaged premises.

385 N.Y.S.2d at 754.

formerly secured inferior creditor is not entitled to sue on the note. Laclede Inv. Corp. v. Kaiser, 596 S.W.2d 36, 39 (Mo. App. 1980).¹⁰

The \$700,000 obligation was evidenced by a "deed of trust note." By its terms, Moening expressly promised to pay principal and interest. The note also stated:

[E]very party signing . . . this note hereby . . . binds himself thereon as a principal, . . . and promises, if this note is not timely paid and is placed in the hands of an attorney for collection, or suit is brought hereon, to pay all costs of collection, including reasonable attorney's fees.

(Emphasis added). The note constitutes a personal obligation of Moening. It does not preclude AMB from suing directly on the note.

The \$33,000 debt is evidenced by a "single payment promissory note" in which Moening expressly promised to pay principal and interest. In case of default, Moening agreed to pay AMB's collection costs and attorney's fees. It does not limit AMB's ability to sue Moening.

10. The Kaiser note contained the following provision:

No personal liability shall be asserted or be enforceable against the maker, it being intended that the sole remedy of the holder hereof be by the foreclosure of the Deed of Trust and Security Agreement

596 S.W.2d at 39 n.1.

The deeds of trust securing the loans contain a power of sale provision permitting nonjudicial foreclosure. The trust deeds also expressly allow judicial foreclosure.¹¹ They do not limit the creditor's right to ignore the security and sue on the note.

IV. CANCELLING THE NOTES AND TRUST DEEDS

When AMB submitted a proposed judgment on the notes, Moening objected because the judgment did not include an order cancelling the notes and deeds of trust under Civil Rule 78(d).¹² AMB submitted the original notes to the court, but did not submit the trust deeds. AMB requested that the notes not be cancelled in case the personal judgment was returned unsatisfied. The superior court ordered that the notes be marked "Conditionally

11. The trust deed states in part:

In the event that this Deed of Trust is foreclosed as a mortgage and said property sold as a foreclosure sale [the purchasers may make necessary repairs or alterations] .
. . .

12. Alaska R. Civ. P. 78(d) provides:

In all cases in which a judgment upon a written instrument is entered, such instrument shall be filed with the court, and unless the court otherwise orders, it shall be cancelled by marks and writing upon its face. The clerk shall retain the same in the files unless otherwise directed by the court.

Cancelled." Moening argues that the superior court erred by failing to unconditionally cancel the notes and trust deeds, entering the order without adequate briefing, and entering the order after the notice of appeal was filed.

When judgment is entered on a written instrument, the instrument shall be filed with the court and cancelled on its face, unless the court orders otherwise. Civil Rule 78(d). We perceive no reason why a secured note should not be subject to this general rule. The note merges with the judgment, and any further proceedings will be to enforce the judgment rather than the note.

In contrast, the deeds of trust should neither be filed with the court nor cancelled:

[A] judgment recovered upon a debt secured by a mortgage does not merge the mortgage nor operate as a discharge, abandonment, or release of the mortgage security.

. . . The mortgage continues to secure such debt and is not released, discharged, or satisfied by a judgment on the debt, note, or bond. Such judgment stands subordinate to the mortgage lien.

Silver v. Williams, 175 A.2d 673, 676 (N.J. Super. Ct. Ch. Div. 1961) (emphasis in original), rev'd on other grounds, 178 A.2d 649 (N.J. Super. Ct. App. Div. 1962). In essence, the creditor ends up with a secured judgment.

Although the superior court could have simply cancelled the notes, it had discretion under the rule to order otherwise.

The conditional cancellation order does not constitute an abuse of that discretion.¹³

AFFIRMED.

13. The record does not support Moening's assertion that the conditional cancellation order was entered after Moening filed a notice of appeal. The order was entered on January 7. The notice of appeal contains an initial filing stamp of December 19; however, that stamp was cancelled and the notice shows a second stamped filing date of January 7.

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THE SUPREME COURT OF THE STATE OF ALASKA

MARSHALL LEE CONRAD and)
COLLEEN M. CONRAD,)

Appellants/Respondents,)

v.)

File No. S-1996/2102

COUNSELLORS INVESTMENT CO.,)
a partnership; BRIAN J.)
BRUNDIN; BILL LAWRENCE;)
MARCUS R. CLAPP; JERRY E.)
MELCHER; and JAMES M. POWELL,)

O P I N I O N

Appellees/Petitioners.)

[No. 3275 - February 26, 1988]

Appeal in File No. S-1996 from the Superior Court of the State of Alaska, Fourth Judicial District, Fairbanks, Gerald J. Van Hoomissen, Judge. Petition for Review in File No. S-2102 from the Superior Court of the State of Alaska, Fourth Judicial District, Fairbanks, Jay Hodges, Judge.

Appearances: Barry Donnellan, Fairbanks, for Appellants/Respondents. Timothy R. Byrnes, James M. Gorski, Hughes, Thorsness, Gantz, Powell, and Brundin, Anchorage, for Appellees/Petitioners.

Before: Matthews, Chief Justice, Rabinowitz, Compton, and Moore, Justices. [Burke, Justice, not participating.]

COMPTON, Justice.

This appeal presents two questions. The first question is whether secured creditors agreed to limit their remedy to nonjudicial foreclosure of their security. The second is whether the creditors' subsequent claim for judicial foreclosure of that security is precluded by the judgment in a prior suit on the note.

I. FACTUAL AND PROCEDURAL BACKGROUND

Counsellors Investment Co. (Counsellors)¹ purchased commercial property in Fairbanks from Marshall Lee Conrad and Colleen M. Conrad. In partial payment for the property, Counsellors gave the Conrads a note secured by a second deed of trust.

Counsellors eventually stopped making payments on the note and offered to reconvey the property to the Conrads in satisfaction of the debt. The Conrads declined the offer and sued Counsellors and its partners for a personal judgment on the note (Conrad I).

The superior court entered summary judgment for Counsellors on the ground that the Conrads' "remedy under their note and deed of trust is that provided in Paragraph B6 of the deed of trust and in AS 34.20.070-.135, and that [the Conrads] may not

1. Counsellors is a general partnership. The partners are Brian Brundin, Bill Lawrence, Marcus Clapp, Jerry Melcher and James Powell.

maintain a suit on the promissory note alone;" in other words, the Conrads' remedy was limited to nonjudicial foreclosure of the security. Since the judgment form submitted by Counsellors was not consistent with some of the court's oral conclusions, the Conrads moved to amend the judgment to clarify whether they had the right to foreclose judicially. The court denied the motion and entered an order prohibiting the Conrads from exercising "any remedy inconsistent with the deed of trust." However, the court struck language in the proposed order which expressly precluded an action for judicial foreclosure.

The Conrads appealed the judgment in Conrad I and filed a complaint for judicial foreclosure and a deficiency judgment (Conrad II). Counsellors moved to dismiss the complaint, arguing that the Conrads' claim for judicial foreclosure was barred by the judgment in Conrad I. The superior court denied the motion to dismiss because "the question of judicial foreclosure was not before the court in the [prior] action" and "the right of the Conrads to maintain this action for judicial foreclosure of a deed of trust is granted by AS 09.45.170." Counsellors petitioned for review. We granted review and consolidated the cases for appeal.

II. CONRAD I: DID THE CREDITORS AGREE TO LIMIT THEIR REMEDY TO NONJUDICIAL FORECLOSURE OF THE SECURITY?

The Conrads argue that they have the right initially to ignore their security and sue on the note, or to file a complaint

for judicial foreclosure. Counsellors does not dispute that a secured creditor generally has that option; however, it contends that the deed of trust expressly limits the Conrads' remedy to nonjudicial foreclosure.

In Moening v. Alaska Mutual Bank, __ P.2d __, Op. No. 3274 at 6 (Alaska, February 26, 1988), we held that absent an agreement to the contrary, a secured creditor has the option whether to sue on the note or foreclose the security. If the creditor sues on the note and obtains a personal judgment which is returned unsatisfied, the creditor may then foreclose the security. Id.; AS 09.45.200.² In determining whether the parties agreed to limit the creditor's remedies, the note and trust deed are construed together and interpreted to carry out the reasonable expectations of the parties. __ P.2d at __, Op. No. 3274 at 7.

The deed of trust note here in issue states that Counsellors "promise(s) to pay" the Conrads the loan amount. In the event of default, the Conrads may at once declare the entire debt due and payable. The note does not indicate that

2. AS 09.45.200 provides:

During or after the pendency of an action for the recovery of a debt secured by a lien mentioned in AS 09.45.170, an action cannot be maintained for the foreclosure of the lien unless judgment is given in that action that the plaintiff recover the debt or a part of it, and an execution issued in the action against the property of the defendant is returned unsatisfied in whole or in part.

Counsellors is not liable for payment; therefore, the Conrads are entitled to sue on the note or foreclose judicially unless the deed of trust provides otherwise.

Counsellors argue that Paragraph B6 of the deed of trust limits the Conrads' remedy to nonjudicial foreclosure:

Upon default by Trustor in payment of any indebtedness secured hereby or in performance of any agreement hereunder, all sums secured hereby shall immediately become due and payable at the option of the Beneficiary. In the event of default Beneficiary shall execute or cause the Trustee to execute a written notice of such default and of his election to cause to be sold the herein described property to satisfy the obligation hereof, and shall cause such notice to be recorded in the office of the recorder of each recording precinct wherein said real property of [sic] some part thereof is situated.

(Emphasis added). Counsellors reasons that the language "Beneficiary shall execute" must be construed as a limitation on the Conrads' right to do anything else.³ However, we believe that the only logical interpretation of this language requires the Conrads to execute the notice only after they have "elected" the remedy of nonjudicial foreclosure. The Conrads are entitled to exercise any other remedies permitted by law.

We conclude that the deed of trust does not limit the Conrads to the remedy of nonjudicial foreclosure. The trust deed

3. See Fowler v. City of Anchorage, 583 P.2d 817, 820 (Alaska 1978) ("Unless the context otherwise indicates, the use of the word 'shall' denotes a mandatory intent.")

does not expressly preclude a suit on the note. The fact that a creditor may foreclose nonjudicially does not imply that it may not foreclose judicially.⁴ Because the Conrads' remedies were not expressly waived in the note or deed of trust, they had the right to sue on the note or foreclose the security. Therefore, the superior court erred as a matter of law when it entered summary judgment against the Conrads on their right to sue on the note.⁵

4. AS 34.20.070(a) provides in part:

If a deed of trust is executed conveying real property located in the state to a trustee as security for the payment of an indebtedness and the deed provides that in case of default or noncompliance with the terms of the trust, the trustee may sell the property for condition broken, the trustee, in addition to the right of foreclosure and sale, may execute the trust by sale of the property, upon the conditions and in the manner set forth in the deed of trust, without first securing a decree of foreclosure and order of sale from the court,

...

(Emphasis added).

5. The superior court appeared concerned that the Conrads filed suit on the note without providing Counsellors any notice of default. Paragraph B6 of the deed of trust requires the Conrads to record a notice of default as one of the steps leading to nonjudicial foreclosure. However, no notice is required if the Conrads pursue one of the other remedies available to them as secured creditors. See Smith v. Certified Realty, 585 P.2d 293, 294 (Colo. App. 1978), aff'd, 575 P.2d 1043 (Colo. 1979) (debtor has no equitable right to cure default in an action brought solely on a promissory note).

III. CONRAD II: IS THE CREDITORS' CLAIM FOR JUDICIAL FORECLOSURE PRECLUDED BY THE PRIOR SUIT ON THE NOTE?

Counsellors argues that the Conrads' claim for judicial foreclosure is precluded by the judgment on the note. The Conrads contend that judicial foreclosure was not addressed in Conrad I.

We described the claim preclusive effect of a prior judgment in State v. Smith, 720 P.2d 40, 41 (Alaska 1986), as follows:

Under the doctrine of res judicata (claim preclusion), a judgment on the merits of a controversy bars subsequent suits between the same parties asserting the same claim for relief when the matter raised was or could have been decided in the first suit. Pankratz v. State, Department of Highways, 652 P.2d 68, 74 (Alaska 1982); Calhoun v. Greening, 636 P.2d 69, 71-72 (Alaska 1981). The Restatement (Second) of Judgments § 24(a) (1982) states that the claim extinguished by the first judgment:

includes all rights of the plaintiff to remedies against the defendant with respect to all or any part of the transaction, or series of connected transactions, out of which the action arose.

A mere change in the legal theory asserted will not avoid the preclusive effect of the first judgment. Pankratz, 652 P.2d at 74.

Arguably, Conrad II is barred under this reasoning. Conrad I involved the same parties and resulted in a judgment on the merits. The Conrads could have joined a claim for judicial

foreclosure with their claim for judgment on the note. Thus, it is irrelevant whether the Conrad I court ruled on this issue.⁶

On the other hand, the common law permits a creditor to judicially foreclose a security following an action on the note. E.g., Foothills Holding Corp. v. Tulsa Rig, Reel & Mfg., 393 P.2d 749, 751 (Colo. 1964); Berg v. Liberty Fed. Sav. & Loan Ass'n, 428 A.2d 347, 348-49 (Del. 1981); Klondike, Inc. v. Blair, 211 So. 2d 41, 42-43 (Fla. App. 1968). Moreover, AS 09.45.200 permits an action for judicial foreclosure "after the pendency of an action for the recovery of a [secured] debt," provided that the creditor prevails in the prior action and its judgment remains unsatisfied in whole or in part.⁷

We believe that this situation is best viewed as an express statutory exception to general principles of res judicata. A creditor need not join its claim for judicial foreclosure in the suit for recovery on the note at the risk of losing its security. In one sense, the subsequent foreclosure may be considered a special form of execution on the prior

6. To the extent that Counsellors argues that this issue is precluded by Conrad I, it is relevant whether the first court ruled on the judicial foreclosure question. We agree with the Conrads that the superior court did not rule that the Conrads are limited to nonjudicial foreclosure; despite Counsellors' best efforts to obtain a decision on this question, the court left it unresolved.

7. See AS 09.45.200, supra note 2.

judgment for the creditor. Under AS 09.45.200, the creditor may bring these claims consecutively.⁸

The decision of the superior court in File No. S-1996 is REVERSED; the decision in File No. S-2102 is AFFIRMED. The cases are REMANDED to the superior court for further proceedings. The Conrads may elect whether to proceed with the suit on the note or the foreclosure.

8. However, when the creditor resorts first to judicial foreclosure, failure to join its claim for a deficiency judgment may result in claim preclusion. See AS 09.45.170; see also Darnell v. Denton, 669 P.2d 981, 983 (Ariz. App. 1983); but see Perpetual Bldg. & Loan Ass'n v. Braun, 242 S.E.2d 407 (S.C. 1978).

STATE OF ALASKA THE LEGISLATURE

LEGISLATIVE AFFAIRS AGENCY

POUCH Y - STATE CAPITOL
JUNEAU, ALASKA 99811
907 465 3800

MEMORANDUM

February 22, 1988

SUBJECT: Judicial and nonjudicial foreclosures

TO: Representative Steve Rieger, Co-Chairman
Representative Kay Brown, Co-Chairman
Subcommittee on Housing and Banking
Joint Committee on Economic Recovery

FROM: Richard A. Bradley
Legislative Counsel 

You have requested that we explain the distinction between a "judicial foreclosure" and a "nonjudicial foreclosure."

In real property law, the document that establishes the procedure to be used to foreclose the interests of the purchaser of the property in the property is usually either a mortgage or a deed of trust.

While the terms are not always used precisely in the actual documents, the general understanding is that a mortgage will require a judicial foreclosure because it does not contain provisions for its foreclosure. A mortgage is the older procedure used for centuries in Anglo-American real property law.

In more recent years, legislatures have established the deed of trust. The provisions of the laws establishing the procedure permit the foreclosure of the purchaser's interests without judicial intervention. It is assumed that it is more expeditious and simpler to use.

While both procedures are to some extent statutory now, I believe that historically the judicial foreclosure may have been entirely judicial. Because it was judicial, the equity of redemption (or more recently, simply a right of redemption) was the judicial invention to avoid what the courts considered the harsh remedy of cancelling the purchaser's equity because the last of many payments wasn't timely. It

Representative Steve Rieger
Representative Kay Brown
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gave the purchaser a period after the execution to redeem; these period if they exist, are now statutory.

The statutory provisions describing judicial foreclosure provisions appear at AS 09.35; the premise of AS 09.35 is that the mortgage has already been foreclosed judicially and "executions" are necessary to turn a judgment into assets. Note that the purchaser is given a right of redemption for a year (AS 09.35.250) and that deficiency judgments (a further judgment for the difference between the underlying debt owed and the amounts recovered at executions) are permitted (AS 09.35.100).

The statutory provisions describing nonjudicial foreclosures appear at AS 34.20.070 - 34.20.135. Generally there is no right of redemption (AS 34.20.090(a)) and deficiency judgments are prohibited (AS 34.20.100).

If I may be of further assistance, please advise.

RAB:gc
WKG1:108

By Staff
H/B Committee

February 23, 1988

JUDICIAL V. NONJUDICIAL FORECLOSURE PROVISIONS:

Judicial Foreclosure - foreclosure conducted via the court system. Courts may issue a deficiency judgement against the borrower, and the borrower in turn has the "right of redemption", unless the property is sold "BFP" (to a bonafide purchaser) and not subject to the right of redemption.

Nonjudicial Foreclosure - foreclosure conducted outside the court system. No deficiency judgement or right of redemption period allowed.

Mortgage - Foreclosure proceedings can only be conducted judicially with a mortgage, because there is nothing in place in the mortgage document for default remedies. (Mortgages are rarely used in the State of Alaska.) In a judicial foreclosure, the court may give the lender a deficiency judgement for the difference of what they can sell the property for and what is actually owed on the property. This deficiency judgement is a personal obligation on the part of the borrower. The borrower has the "right of redemption" to pay what is owed and regain possession to the property in judicial foreclosures only. (See "Right of Redemption" below)

Deed of Trust - Foreclosure proceedings can be accomplished by judicial or nonjudicial means. The deed of trust document has prescribed foreclosure provisions, thereby allowing the lender to foreclose outside of court, i.e. nonjudicial foreclosure proceedings. Deficiency judgements are prohibited in a nonjudicial foreclosure however, and the lender must take what they can get. The lender does have the option to a judicial foreclosure if they feel that it is worth going after the holder of the deed of trust personally via a deficiency judgement issued by the courts. (In many cases, it is not worth the time and effort to the lender to foreclose via the court system.)

Right of Redemption - that period of time, (one year), as set by statute for the defaulting borrower to "redeem" himself and pay up on the mortgage, thereby regaining "custody" of his property. Generally, there is no right of redemption in a nonjudicial foreclosure.

WILLIAM L. MCNALL
ANN WALLER RESCH
DAVID RANKINE

LAW OFFICES OF
WILLIAM L. MCNALL
310 "K" STREET
SUITE 312
ANCHORAGE, ALASKA 99501

AREA CODE 907
TELEPHONE 276-2535

February 17, 1988

Representative Brown
Alaska State Legislature
P.O. Box V
Juneau, Alaska 99811

*I hope this helps
Wm*

Re: Condominium Foreclosures and the moratorium
proposed by H.B. 432

Dear Representative Brown *Kay*

In response to your panels request, I thought I would write to make several suggestions regarding the current economic problems of the condominium industry in particular and real estate industry in general. This may help clarify my testimony of last Saturday. There is no combination of policies that can completely solve our present problem. Rather, effort should be directed toward ending factors that contribute to the downturn so that the innate resilience of our economy can take effect. What is needed is greater institutional flexibility by the players in the real estate area. I also have some suggestions regarding legislation you have under consideration.

The following factors are contributing to the continued decline in this area. First, there is the "foreclosure cycle". When a borrower gets into trouble, the lender has to make a decision whether to work with the borrower or to foreclose. When foreclosure occurs the property is then dumped on the market and the incremental increase in supply has the effect of further pushing down prices. The price decline shatters the confidence and pocket books of other owner/borrowers who then consider abandoning their property which leads to additional foreclosures and or bankruptcy.

Let me give you several examples from clients who have consulted this firm for advice. We have numerous such clients who own rental housing. They have been able to withstand the early stages of the downturn but now have to compete for tenants with foreclosed properties managed either by governmental entities who have unlimited ability to subsidize rents, or from the individuals who have purchased foreclosed properties at a great discount. Many of these individuals can afford to keep properties going but are, with increasing frequency choosing not to do so. This office recently completed handling a Chapter 7 bankruptcy on behalf of an engineer who decided he would rather pocket his \$80,000 a year salary rather than continue to use it to keep his rental units afloat.

His creditors did not receive anything as a result of the bankruptcy except the return of the property.

Most condo owners can live with payments and negative equity, but are increasingly deciding not to do so. One reason is that the foreclosure cycle has caused them to lose confidence in ever being able to sell their condominium unit. Other policies also contribute to owners deciding to walk away from condominiums and their mortgages. These policies include owner occupancy restrictions of AHFC that prevent rental, AHFC decertification of condo project for reasons unrelated to the credit worthiness of its occupants, and financial difficulties born by owners associations in collecting dues. This latter factor has led to a combination of deferred maintenance and dues increases which prompts remaining owners to consider walking away from their loans. A lack of standards related to condo management firms is also a problem. The condo trade group, CAI, has proposed that managers be licensed by occupational licensing. This is a good idea.

AHFC will not provide financing to owners in projects that do not meet its owner occupancy percentage of 70% although it will finance the sale of units it has acquired as a result of a foreclosure in such projects. In calculating this percentage it counts its own units as not being owner occupied as well as units occupied by family members of the owner but not the owner himself. Numerous condos have lost their certification for AHFC financing on this basis. A client of this firm contemplated selling her condo and had a loan balance low enough to do so. When AHFC decertified her project on owner occupancy grounds, she simply stopped paying them. The condo is now in a nonjudicial foreclosure and will be contributing to the downward cycle. Restricting rentals of condos puts condo associations in conflict with their members who would like to rent and reduces the options for owners who must for some reason move.

Each time AHFC decertifies a condominium association a new collection of owners give up hope because of the inability to finance any sale. The effect of project decertification is to deprive owners of marketable title. Despite this fact the decision to decertify projects is unaccompanied by any hearing or due process. I've heard stories of condo projects threatened with decertification because of disputes as trivial as condominium accounting practice and the dislike of the associations decision on how to manage their projects or when to repair and repaint. AHFC will also decertify a condo when too many of the members are delinquent in paying dues.

I support several bills that you have before you which seek to help to break this cycle. These include HB 432, 433, and Senator Faiks bill which gives a condo lien rights to rents on condominium units when dues are not being paid. I first want to discuss the efficacy of some of the policies that have been used already.

AHFC bashing has become a popular sport these days. I do not subscribe to the notions that AHFC is to blame for our problem. I find it to be as responsive to the public as any governmental entity. When the public wanted financing AHFC provided it. I believe AHFC can provide a major contribution to ending the existing problem.

In general AHFC's response has been a combination of carrot and stick. The stick has been a policy of judicial foreclosures. The carrot is the HOAP program. The theory of doing judicial foreclosures on a large scale has been to up the ante for an owner who decides to abandon his property. In general, I do not think the policy has met great success. Judicial foreclosures have the disadvantage of costing more in attorney's fees and have not brought in much money in return, although individual cases have been successful. It is possible for an individual to shelter from creditors just less than \$40,000 in a bankruptcy by maximizing use of exemptions. This figure exceeds most peoples net worth and eliminates, in most cases the economic threat judicial foreclosures have on a homeowner. The policy of using judicial foreclosures has been a disaster for condominiums because it lengthens the period between the time the owner stops paying dues and the condo is taken over by AHFC. Also, if judicial foreclosure results in a bankruptcy, liability for condominium dues is discharged.

The HOAP program has met with success, but on a smaller scale than is needed. This program is intended to assist financially distressed owners to work out their financial problems by payment plans and adjustment to their loan payments. The program is administered by mortgage insurers. This was a smart move. In the past AHFC has been badly served by its sellers/servicers in dealing with borrowers with problems. The servicers often swept problem loans under the rug by foreclosing instead of having the patience to work with borrowers.

I was told by someone at MGIC that nationwide only 20% of mortgage loans that at some point become delinquent result in a foreclosure. In Alaska the figure is 65%. The principal drawback of the program is that it helps only people who are slightly distressed financially but not people who have suffered a steep reduction in income. It also does not address the problem of homeowners who simply can't afford their home any longer or need to get out of it for non-economic reasons.

HB 433 will go a long way towards breaking the foreclosure cycle by giving debtors the option of preventing a foreclosure conditional upon the tender of the rental value of the property. I suggest some amendment to the proposed bill. A nonjudicial foreclosure can be conducted in three months. The superior court's calendar is sufficiently crowded that a petitioner for relief under the act might not be able to get his case to hearing before the property is lost. The court could prevent this from happening by issuing a preliminary injunction against sale. A prerequisite of an injunction is that the movant has to post a bond to protect the opposing party from any loss if the injunction is improvidently issued. Alaska Public Utilities Commission the Greater Anchorage Borough, 534 P.2d 549 (Alaska 1975). I fear that if you do not include a provision setting the amount of a bond the relief you intend could be frustrated by overly large bonds being required. There are several statutes where the legislature has set restrictions on injunction bonds. For example, AS 45.55.200 permits the State to enjoin a securities offering without posting a bond. I also note that in Carol v. Eldorado Estates Division No. 2 Association, 680 P.2d 1158 (Alaska 1984) the court held that a statute providing for injunctive relief would obviate the necessity of the party seeking an injunction to show irreparable injury. This is another requirement of an injunction. I suggest as an addition to the proposed act a provision requiring the court to restrain a foreclosure based upon the debtor depositing an estimated rental with the court clerk. This would tide things over until a final hearing could be heard and the actual rental value could be determined.

As mentioned, condominiums suffer when dues are not paid. I would change paragraph (b) of sections two and three of HB 433 to include a statement that provides that condominium dues must be paid as a condition of the relief requested.

The bill as presently proposed does not address the problem of properties incumbered with multiple deeds of trust.

For example, if the rental value does not cover payments on a first deed of trust is the second deed of trust holder, or other encumberancer to go unpaid for a year or two? An equitable solution to this problem would be to apportion the rental proceeds amongst lien holders based on the ratio of the principal balance of the obligations.

The proposed statute applies to all real property. You might want to consider whether you want its coverage to extend to raw land or only to real property whose principal value is derived from improvements. Here the consideration is the fact that undeveloped land has an insignificant rental value.

Opponents of the bill may argue that a wealthy person could use the courts in all cases to reduce for one or two years their payments to rental value. I do not believe this is what would happen. In addition to the remedy of foreclosure, mortgage creditors have the option of waiving their security and sueing for the amounts owing on the note. Smith v. Shortall, 732 P.2d 538 (Alaska 1987). If a wealthy person sought to enjoin a foreclosure under the bill as written, the lender could sue the individual for the principal owing on the note and collect from the debtor's other assets. This option would be less desirable for poor debtors since the security might be their principle asset. In this way the bill, as drafted, is self regulating on this issue.

The legislative findings portion of the bill points out that one of its purposes is to hold off foreclosures during a time when there is little market for the properties and to prevent double recoveries to mortgagees. I recommend as an additional or alternative step an amendment to AS 9.45.170. This part of the judicial foreclosure statute provides that the court should set the manner of a judicial foreclosure sale and the application of proceeds of the sale. The problem here is that the lender in a judicial foreclosure can bid a very low price for the property and after the redemption period has run sell the property at a profit. The debtor receives no credit for the resale price but must satisfy the judgement by paying the difference between the amount bid by the creditor at the execution sale and the mortgage balance, even if this works a double recovery. I have argued, with mixed results, that under this statute the court can set a minimum price for the property. I fear that it may be a long time before the supreme court has an opportunity to decide this issue.

Other states have included in their statutes language that expressly provides that court can set a minimum bid in order to protect debtors from being victims of such a double recovery situation. I recommend you consider an amendment of the

statute that expressly requires courts to set a minimum bid in such situations. I enclose the Wisconsin cases of Suring State Bank v. Geese, 246 N.W. 556 (Wis. 1933) and First Wisconsin National Bank of Oshkosh v. K.S.W. Investments, 238 N.W. 2d 123 (Wis. 1985) these cases discuss how a fair market price for a judicial foreclosure execution sale can be determined in order to prevent victimizing debtors by this kind of recovery.

I strongly support House Bill No. 432 which permits trades on AHFC financed properties. This bill would provide great assistance in breaking the "foreclosure cycle" when non-economic reasons are the cause of the owner abandoning the property. Examples are individuals whose families outgrow their condo or who must move to other parts of the state.

A criticism I have heard of the program is that if everyone wanted to trade up, only poorer quality housing would remain in AHFC's inventory. Even if this were true, such a result would be a good social policy in that it would improve living standards. However, this argument overlooks the fact many people would like to trade down. Examples are where a divorce makes keeping a house impossible, one can envision numerous other situations where owners can no longer afford their houses. In those situations trading down may be a alternative to foreclosure and may permit AHFC to reduce its inventory of condos.

A trading program would work best if all parties shared the benefits and burdens. Such a program might work in this manner; suppose an individual owns a condo with a \$80,000 loan balance and value of \$60,000 desires to trade into a house worth \$100,000. AHFC would take back the condo and "sell" the house for \$110,000 including \$10,000 down. Such a condo would have mortgage insurance in the approximate amount of \$20,000. The \$10,000 down payment would go to the mortgage insurer to compensate it for the loss on any resale of the condo. The insurer has an incentive to take this loss because it would eliminate expenses it would be incurring as a result of the house having been foreclosed. As a further incentive for insurers to participate in such a program, the "buyer" might be required to execute what is known as a "without recourse" deed of trust in favor of the insurer or AHFC. This type of instrument is a lien on the property which by its terms can be satisfied from the sale of the property rather than from the individual who signs it. The deed of trust would provide for repayment of the \$10,000 lost as a result of the transfer only from a future sale of the property. To encourage individuals to take good care of their house so that it did appreciate, the

deed of trust could have a provision that provided for a split of any appreciation with the owner in a 50/50 basis with half going to the owner and half to AHFC up to the \$10,000 amount. Acceptance of the return of collateral does not necessarily violate the typical mortgages insurance policy. As can be seen from the enclosed policy of Republic, paragraph 10 provides for "acceptance by the insured at any time of a voluntary conveyance from the borrower of his interest in the mortgaged real estate...shall not preclude the insured from recovery for loss under this policy."

These pieces of legislation would be of some assistance to condos but are not, with the exception of Senator Faiks bill providing a lien on rentals, tailored to the particular problems of community associations. These problems are in urgent need of being addressed. First, the owner occupancy policy is pernicious and should be abandoned. No legislation is required to accomplish this. In 1972 when the legislature created AHFC its finding section of the act stated one of the reasons for the corporations existence was to provide for the "sale and rental of dwelling units for persons of lower and moderate income..." AS 18.56.010. One can read the AHFC act from cover to cover without finding a provision empowering it to restrict owners/occupancy. Instead one finds AS 18.56.088 (i) which permits AHFC to make restrictions only for mobile homes "not in accordance with the provisions of this chapter, including conditions and terms related to owner/occupancy." From this I conclude that AHFC's owner occupancy restrictions are unlawful at present.

There was no owner occupancy requirement prior to 1981. In that year AHFC switched from exclusively selling its own bonds to a policy of generally issuing bonds through entities such as F.N.M.A. These agencies have the owner occupancy and other restrictions as a way of rationing the uses for their funds. However, whenever AHFC wants to it still issues its own bonds when it sees a need to have a program that does not fit within the F.N.M.A. or Freddie Mac guidelines. The HOAP program is a result of just such a bond issue.

In 1986 AHFC bonded a program for homeowners who desired to refinance and rent their homes. AHFC could not find a mortgage insurer for the issue but pursuant to AS 18.56.095 issued its own mortgage insurance policies for which it collects premiums. I enclose a copy of such a policy. Thus all AHFC has to do to end the owner occupancy restriction problem is to float a bond issue and use the mortgage insurance fund to back the bond. These bonds would only have to cover

Re: H.B. 432
Page 8 of 8

financing need for those projects that do not meet the F.N.M.A. or Freddie Mac standards.

Other condo problems could be alleviated by AHFC being more attentive to the needs of associations. No legislation is needed for AHFC to provide associations with due process before it decertifies them. That is required by the constitution.

In 1985 you passed a new condominium law. One provision of that act, AS 34.08.470, provided for something colloquially known as the super lien. This enables associations to amend their charters to require foreclosing mortgagees to make good on unpaid assessments going back six months prior to the action to collect. This can be of great assistance in alleviating the financial disaster associations experience when an owner stops paying dues. To enact the provision the associations must achieve an affirmative vote of 70% of their owners. A number of associations have enacted the lien, but due to foreclosures few of the remaining associations can muster the votes. AHFC has supported the super lien, but refuses to cast a vote either for or against the lien in elections to enact it. A change of this policy would be of some assistance to distressed projects.

In general, the best response to the problems of the housing industry is to innovate in ways to break the foreclosure cycle. Although all of the problems will not be solved by a proposal made in this letter, they will provide a means to end the psychological, practical and financial factors which continue to damage the market. By eliminating these factors the decline is likely to stop sooner and at a higher level than it will otherwise.

Sincerely,

LAW OFFICES OF WILLIAM L. McNALL

By: William L. McNall
William L. McNall

WLM/cq
Enclosures



MASTER POLICY

No. _____

Republic Mortgage Insurance Company
Winston-Salem, N.C. 27102

-- (A Stock Insurance Company Herein Called the Company)

AGREES TO PAY TO

(Hereinafter Called the Insured)

in consideration of the premiums to be paid by the Insured as specified in the Certificate, and in reliance upon the statements made in the Application submitted by the Insured, any loss sustained by reason of the default in payments by a Borrower as hereinafter set forth subject to the following conditions:

CONDITIONS

1. APPLICATION AND COMMITMENT

The Borrower and the Insured shall furnish the Company with an Application in connection with each mortgage loan for which coverage under this policy is desired, on forms furnished by and prepared in compliance with requirements prescribed by the Company. Approval of the Application shall be at the discretion of the Company and shall be in the form of a Commitment prescribing the terms of the coverage.

2. NOTICE AND CERTIFICATE

Within seven (7) days after consummation of the mortgage loan transaction, the Insured shall forward notice thereof to the Company, together with the premium, and the Company shall immediately issue and forward a Certificate to the Insured or the Certificate previously issued to the Insured shall then become effective, binding the Company according to the terms and conditions of the Commitment and of this policy. The effective date of the Certificate shall become the date on which the mortgage loan transaction was consummated, which date shall precede the Commitment expiration date or an extension thereof approved in writing by the Company.

3. PAYMENT OF PREMIUMS

In the event that coverage includes renewal privileges, the renewal premiums shall be paid within 45 days following the anniversary of the effective date of the Certificate. Failure to pay any premium, initial or renewal, when due will terminate the liability of the Company with respect to the mortgage loan insured pursuant to the Certificate.

4. TERMINATION BY COMPANY

The Company shall remain liable under this policy with respect to such Commitments or Certificates issued to the Insured, as long as the terms and conditions herein contained are fully complied with. However, the Company reserves the right to terminate this policy, upon 30 days notice subject to its remaining liable on such Commitments and Certificates already issued.

5. CANCELLATION BY INSURED

The Insured shall have the privilege of canceling the coverage pursuant to any Certificate by returning such Certificate to the Company. On receipt thereof, the Company shall refund to the Insured such sum as may be determined to be due in accordance with the cancellation schedule set forth herein; providing however, that no refund shall be paid in the event that a claim for loss has been filed.

6. RESTORATION OF DAMAGE

As a prerequisite for the payment of such loss as may be determined to be due herein, should there be physical loss or damage to the property from any cause, whether through accidental means or otherwise, the Insured shall cause the said property to be restored to its condition at the time of the issuance of the Certificate, reasonable wear and tear excepted.

7. OPEN-END PROVISION

The Insured may increase the mortgage loan balance by making an additional loan to the Borrower, provided that an Application is made therefor subject to approval by the Company. In the event of such approval, the prevailing premium therefor shall be paid to the Company, for the additional amount loaned to the Borrower, and the Company shall issue a Certificate insuring the additional amount.

8. COMPLETED CONSTRUCTION

In the event that the mortgaged premises consists of improvements in the process of construction, the Company shall not be liable until such construction is completed.

9. NOTICE OF DEFAULT

Within 10 days after the Borrower is four (4) months in default, notice thereof shall be given to the Company by the Insured. Monthly reports indicating the default status of the Borrower's account shall be given to the Company thereafter until such time as appropriate proceedings are commenced, title has been vested in the Insured, or the Borrower is less than four (4) months in default.

10. PROCEDURE ON DEFAULT

When the Borrower's account is four (4) months in default, the Company may direct that the Insured commence appropriate proceedings as herein defined, which shall be commenced, in any event, when the Borrower's account is nine (9) months in default. Such proceedings, when instituted, shall be diligently pursued, and should applicable laws permit the appointment of a receiver, application therefor shall be made by the Insured, with the recommendation that an agent of the Company be appointed to so act. The Company shall be furnished, within a reasonable time, copies of all notices and pleadings required in such proceedings, and with any pertinent information requested by the Company. The Insured shall also furnish to the Company, at least fifteen days prior to the foreclosure sale, a statement indicating the amount anticipated to be due, at the time of the sale, to the Insured under the terms of this policy and shall be required to bid, at the sale, the amount due to the Insured under the terms of this policy. Acceptance by the Insured at any time of a voluntary conveyance from the Borrower of his interest in the mortgaged real estate or commencement by the Insured of appropriate proceedings on default of the Borrower, even though his account is less than four (4) months in default, shall not preclude the Insured from recovery for loss under this policy.

11. COMPUTATION OF LOSS

The amount of loss payable to the Insured shall be limited to the principal balance due pursuant to the mortgage agreement, accumulated interest computed through the date of the tender of conveyance, as hereinafter set forth (penalty interest excluded), real estate taxes and hazard insurance premiums necessarily advanced by the Insured, any expenses necessarily incurred by the Insured in the preservation of the mortgaged real estate, and all other necessary expenses of the appropriate proceedings, including court costs, and reasonable attorney's fees not exceeding three per cent (3%) of the principal and interest due as herein set forth.

12. WHEN LOSS PAYABLE

Any loss due to the Insured shall be payable within 60 days after filing of a claim for such loss on a form to be furnished by the Company. The claim for loss must be accompanied by a tender to the Company of conveyance of title to the mortgaged real estate together with satisfactory evidence that

such title is good and merchantable in the Insured, free and clear of all liens and encumbrances. Failure to file a claim for loss within 60 days after completion of appropriate proceedings shall be deemed an election by the Insured to waive any right to claim payment under the terms of this policy.

13. OPTION OF PAYMENT

In lieu of conveyance of title to the mortgaged premises and payment in accordance with Condition 11, the Company shall have the option of paying a percentage of such amount due to the Insured and thereafter shall have no claims to said real estate, such payment to be a full and final discharge of the Company's liability. The percentage of the amount due under condition 11 to be payable under this option will be designated in the Certificate of Insurance issued by the Company under the caption Optional Guaranty Payment.

14. WHERE NOTICE IS GIVEN

All notices, pleadings, claims, tenders, reports and other data required to be given by the Insured to the Company shall be mailed postpaid to the home office of the Company.

15. NO RIGHT OF SUBROGATION AGAINST BORROWER

The Borrower shall not be liable to the Company for any loss paid to the Insured pursuant to this policy; provided, however, that the real estate shall consist of a single family dwelling occupied by the Borrower; otherwise, the Company reserves the right to make claim against the Borrower for any loss paid or deficiency suffered by the Company.

16. TO WHOM PROVISIONS APPLICABLE

The provisions of this policy shall inure to the benefit of and be binding upon the Company and the Insured, and their successors and assigns.

17. SUIT

No suit or action on this policy for recovery of any claim shall be sustained in any court of law or equity unless all the conditions of this policy have been complied with, unless specifically waived by the Company in writing, and unless commenced within two (2) years after the loss can be determined.

18. CONFLICT WITH LAWS

Any provision of this policy which is in conflict with the laws of the jurisdiction in which this policy is effective is hereby amended to conform with the minimum requirements of such laws.

19. DEFINITIONS

Four (4) months of default is defined as the failure to pay the total aggregate amount of four (4) monthly payments due under the terms of the mortgage agreement. Similarly, nine (9) months of default is defined as the failure to pay the total aggregate amount of nine (9) monthly payments due under the terms of the mortgage agreement.

Mortgage agreement is defined to include a note, mortgage, bond, deed of trust, or other instrument used in connection with the Borrower's loan.

Appropriate proceedings are defined as any legal remedy permissible, under the laws of the jurisdiction in which the real estate is located, to vest title in the Insured, including, but not limited to, foreclosure by public or private sale.

The term Borrower, or Insured, when used herein, shall mean the singular or plural, male or female, individual, partnership, or corporation, as the case may be.

IN WITNESS WHEREOF, The Company has caused its Corporate Seal to be hereto affixed and these presents to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding on the Company by virtue of countersignature by its duly authorized agent.

REPUBLIC MORTGAGE INSURANCE COMPANY

William A. Simpson
President

Date



Frank Brown
Secretary
Robert H. [Signature]
Authorized Representative



ALASKA HOUSING FINANCE CORPORATION

Rental Program Mortgage Insurance

MASTER POLICY

Alaska Housing Finance Corporation, a public corporation and government instrumentality of the State of Alaska (herein called the "AIF" when in its capacity as administrator of amounts available within certain insurance accounts referred to in this Policy), agrees to pay, from amounts available in the Rental Program Account of the Housing Insurance Fund, to Alaska Housing Finance Corporation (hereinafter called the "Insured") in consideration of the premiums to be paid by the Insured, benefits as herein set forth upon the default by a Borrower in the payment of a loan insured hereunder, subject to the following conditions:

CONDITIONS

1. Definitions -- as used in this Policy, the term --

- A. Borrower shall mean the person or persons, firm or corporation designated as such on the face of the Certificate.
- B. Property shall mean the real property identified on the face of the Certificate, and shall include all appurtenances, rights of access, ingress and egress and improvements thereon.
- C. Loan shall mean the indebtedness of the Borrower to the Insured in the amount and for the term specified on the face of the Certificate, which is evidenced by a written obligation and secured by a Mortgage.
- D. Mortgage shall mean any Mortgage, deed of trust or other instrument creating a first lien upon the Property as security for repayment of the Loan in accordance with applicable law.
- E. Two (2) Months in Default shall mean the failure of the Borrower to have made monthly Loan payments when due so that sums equal to the aggregate of two (2) such monthly payments are delinquent.
- F. Appropriate Proceedings shall mean any practical legal remedy required or permitted after default under applicable local laws to vest in the Insured title in and to the Property, including, but not limited to, foreclosure by public or private sale or voluntary conveyance from the Borrower.

- G. Merchantable Title shall mean ownership of the Property free and clear of all liens, encumbrances and rights of parties in possession excepting only: (i) the lien of current general real estate taxes not yet due and payable; (ii) easements for public utilities, recorded building restrictions and the effect of building laws or regulations with which the improvements on the premises comply and which do not impair the use of the premises and the improvements thereon for their intended purposes; and (iii) such minor imperfections of title as would not prevent the Property from being readily saleable and freely transferable.
- H. Satisfactory Evidence of Merchantable Title shall mean a title insurance company's commitment to insure that Merchantable Title is vested in the Insured or that institution from which the Loan was acquired; or opinion or certificate of any attorney approved by the AIF, directed to the AIF, affirming that the Insured is vested with Merchantable Title to the Property based upon an abstract of title or comparable title evidence generally acceptable by a purchaser of real estate in the area.
- I. Certificate shall mean any Acknowledgement of Mortgage Loan Insurance issued by the AIF to the Insured in accordance with the terms of this Policy to extend insurance coverage to the Loan therein described.
- J. Amount of Insurance shall mean the amount of the Original Loan Amount identified on the face of the Certificate.
- K. Loss Computation Date shall mean: (a) the date of the written claim for loss submitted to the AIF, or (b) the date sixty (60) days following the completion of Appropriate Proceedings, whichever is the earlier date.

2. Application and Commitment

Execution by the AIF of a Certificate shall constitute approval of the application for insurance and represent the form of a Commitment describing the terms of the coverage.

3. Effective Date; Policy Period

The Certificate shall become effective on the date on which the Loan is purchased by the Insured for the term of the Loan subject to payment of required premiums. The Policy may be terminated with respect to a Loan upon mutual consent by the AIF and the Insured.

4. Cancellation

The AIF may cancel a Certificate upon failure of the Insured to pay any of the premiums (including renewal premiums) within ninety (90) days after the date the same becomes due and payable, but the AIF shall not otherwise have the right to cancel a Certificate except upon consent of the Insured. The AIF's liability under individual Certificates issued pursuant to this Policy shall terminate automatically as of the due date for the payment of renewal premium, without any further act of the AIF, upon the failure of the Insured to pay any renewal premium within ninety

(90) days after the due date thereof. The Insured may, at any time, cancel a Certificate for which no claim for loss has been made by returning same to the AIF, in which event a portion of the premium paid will be refunded in accordance with the applicable cancellation schedule. The AIF reserves the right to terminate this Policy at any time, but termination shall not affect liability of the AIF with respect to Certificates outstanding at the date of said termination.

5. Loan Modifications; Open End Provisions; Assumptions

- A. The Insured shall not make any change in the amount, interest rate, term or amortization schedule of an insured Loan other than as permitted under the original Loan documents (note and deed of trust), or release or discharge the Borrower from liability on an insured Loan, waive or modify any of its rights under an insured Loan, or authorize a change in the character or use of the Property without the prior written approval of the AIF.
- B. The Insured may increase the balance of an insured Loan by making an additional loan to the Borrower, provided that an application is made therefor and approved by the AIF. In the event of such approval, the Insured shall pay the AIF a premium with respect to the additional amount loaned to the Borrower, at the then prevailing premium rate, and the AIF shall issue a rider or endorsement insuring such additional amount.
- C. It being understood that the Loans insured under this Policy are being originated pursuant to a program of Alaska Housing Finance Corporation which generally prohibits the assumption of the mortgage Loan, coverage of an insured Loan shall terminate automatically if and as of the date the obligation to make payments under such insured Loan is assumed by a person other than the original or subsequently approved Borrower, unless: (i) the original or subsequently approved Borrower remains personally liable on the insured Loan, or (ii) the AIF approves of the assumption in writing, upon such information and other documentation requested by the AIF and furnished by the Insured.

6. Completion of Construction

If improvements on the Property are proposed or in the process of construction, no loss shall be paid hereunder until such construction is completed according to plans and specifications consistent with documentation submitted to the AIF. Any expenses incurred or sums advanced by the Insured incident to completing such construction other than as disbursements of the proceeds of the Loan shall not be included in any claim for loss.

7. Restoration of Damage

If any physical loss or damage occurs to the Property from any cause, whether through accidental means or otherwise, the Insured shall cause the Property to be restored to its condition as of the date of the consummation of the Loan transaction, reasonable wear and tear excepted, and the expenses incurred in such restoration shall not be included in any claim for loss.

8. Condemnation

If the value of the Property is reduced through condemnation (or a sale in lieu of condemnation), the Amount of Insurance shall be reduced by the amount of the entire proceeds awarded in or resulting from such taking or sale.

9. Notice of Default

The Insured shall give written notice of default to the AIF within fifteen (15) days after the Borrower is Two (2) Months in Default. Said notice to the AIF shall include copies of notices, if any, sent to the Borrower. Thereafter, the Insured shall provide written monthly reports concerning the Loan status to the AIF until such time as the Loan is less than Two (2) Months in Default or the Insured has made a claim for loss to the AIF. Failure of the Insured to give notice of default as required by this Policy shall preclude or diminish any claim for loss if such failure shall prejudice the rights of the AIF under any provision, requirement or condition of the Policy and Certificate but only to the extent of such prejudice.

10. Procedure by the Insured on Default

After the Borrower shall be Two (2) Months in Default, the AIF may direct that the Insured commence Appropriate Proceedings. Such direction to commence Appropriate Proceedings shall be at the option of the AIF, but the Insured may, in the absence of such direction, institute such proceedings at any time after said default. When directed by the AIF, such proceedings shall be instituted promptly and diligently pursued, and shall include proceedings for the appointment of a receiver, collection of rent and/or the enforcement of any rights of the Insured with respect to other security or collateral to the extent that the same are feasible for the purpose of limiting loss and permitted by applicable law. The Insured shall furnish to the AIF copies of all notices and pleadings required in any such proceedings and any additional information reasonably requested by the AIF. In any proceeding in which the Insured is required to bid at a public sale to obtain title to the Property, unless otherwise directed by the AIF, the Insured may bid any amount, in its sole discretion, provided, however, that failure to obtain title shall preclude the right to make a claim for loss, and that the amount of loss which may be claimed shall be computed in accordance with Condition 11 irrespective of the amount bid or the amount recovered by the Insured out of the proceeds of sale.

11. Computation of Loss

The amount of loss sustained by the Insured for each insured Loan shall be limited to: (a) the unpaid principal balance, not in excess of the Amount of Insurance, reduced by the amount of any rents or other recovery received or collected by the Insured; (b) accumulated unpaid interest computed at the contractual rate but not in excess of the contractual rate in effect on the date when the Borrower is Two (2) Months in Default (exclusive of late charges and penalties) through the Loss Computation Date; (c) sums advanced for payment of real estate taxes and hazard insurance premiums, prorated through the Loss Computation Date; (d) sums advanced for preservation of the Property, but expense incurred for preservation of the Property shall be limited to one thousand five hundred dollars (\$1,500.00) unless the AIF shall waive such limitation in writing; and (e) all other reasonable and necessary expenses incurred in Appropriate Proceedings including court costs and attorney's fees, but expense incurred for attorney's fees shall be limited to three percent (3%) of the principal and interest due as herein set forth.

12. Payment of Claim

- A. Notice of Claim -- Any claim for loss insured against this Policy shall be submitted in writing by the Insured to the AIF and must be accompanied by a tender of Merchantable Title together with Satisfactory Evidence of Merchantable Title. Failure to submit a claim for loss within sixty (60) days after the Insured has obtained Merchantable Title shall be deemed an election by the Insured to waive any right to such claim payment under the terms of this Policy.
- B. Settlement Options -- The AIF in its discretion and at its option may alternatively elect to pay the Insured either: (i) the entire amount of the loss computed in accordance with Condition 11, and upon such payment the Insured shall convey Merchantable Title to the AIF; or (ii) a percentage of such loss, as specified on the face of the Certificate in accordance with the premium plan under which the Loan is insured and, in the event of payment under this option, Merchantable Title shall be retained by the Insured. The AIF shall elect its settlement option within sixty (60) days after receipt of notice of a claim.
- C. Payment Procedure -- Any claim payment due the Insured shall be payable within sixty (60) days after receipt of notice of a claim and all supporting documents which may reasonably be required by the AIF. The payment of a claim by the AIF, under either of its options as provided hereinabove, shall be a full and final discharge of its liability hereunder.

13. Option to Acquire Loan

At any time that the Borrower shall be Two (2) Months in Default and before receipt by the AIF of a claim for loss, the AIF shall have the option to acquire the Loan and all of the right, title or interest of the Insured in and to the Property or any Appropriate Proceedings and other security or collateral. The Insured shall furnish to the AIF, within thirty (30) days after written notice of the exercise of this option by

the AIF, a written notice of the acquisition cost which shall be computed through the date of the exercise of this option by the AIF in the same manner as the computation of loss under Condition 11 to the extent that principal, interest and other sums and expenses are actually unpaid or incurred. Payment of the acquisition cost so computed shall be made by the AIF to the Insured within thirty (30) days after receipt of the statement of the Insured together with all supporting documents which may be reasonably required by the AIF. Upon request, the Insured shall execute and deliver to the AIF such instruments or documents which the AIF may require in order to effect or confirm the assignment, transfer or conveyance of the Loan and any right, title or interest of the Insured acquired by the AIF hereunder.

14. Duty of Cooperation

At any time, upon request of the AIF, whether or not notice of default has been given to the AIF, the Insured shall cooperate with the AIF and furnish all reasonable information and assistance in connection with any effort by the AIF to cure or avoid default or limit loss with respect to any insured Loan.

15. Subrogation

The AIF shall be subrogated to all of the rights of the Insured against the Borrower and/or all other parties liable for the payment of the Loan arising out of or connected with the Loan to the extent of the payment of benefits by the AIF under the Policy (i) in all cases where the Real Estate does not consist of a single family dwelling occupied by the Borrower, and (ii) when the Insured agrees that the AIF shall have subrogation rights. Except as herein provided, the AIF shall have no subrogation rights against the Borrower.

16. Limitation of Actions

No suit or action arising from this Policy on account of any loss shall be commenced in any court of law or equity unless the Insured has complied with all the conditions of this Policy and the Certificate, excepting conditions specifically waived or altered in writing by the AIF, and unless commenced within two (2) years after such loss was payable to the Insured.

17. Notices

All notices, reports or other documents required or permitted to be given by either party to the other shall be in writing and shall be forwarded by pre-paid postage to the recipient at the address shown on the face of the Certificate or at such other address as the respective parties may hereafter in writing specify.

18. Changes in the Agreement

This Policy together with the Certificate shall constitute the entire agreement between the Insured and the AIF. No provision, requirement or condition of the Policy and Certificate shall be deemed to have been waived, altered, amended or otherwise changed unless stated in writing and duly executed by the AIF. Each of the provisions of this Policy and Certificate are severable, and a waiver, alteration, amendment or change of one provision whether by the AIF, as aforesaid, or by operation of law, shall not be construed as a waiver, alteration, amendment or change of any other condition.

19. Beneficiaries under Policy

The provisions of this Policy and Certificate shall inure to the benefit of and be binding upon the AIF and the Insured and their respective successors and assigns. In the event that the Insured assigns an insured Loan, this Policy and the Certificate shall continue in force and effect in favor of such assignee subject to the terms thereof.

IN WITNESS WHEREOF, The AIF has caused the Corporate Seal of Alaska Housing Finance Corporation to be hereto affixed and these presents to be signed by a duly authorized officer.

ALASKA HOUSING FINANCE CORPORATION,
in its capacity as administrator
of amounts available within certain
insurance accounts referred to in
this Policy.

Ronald D. Lehr
Ronald D. Lehr
Executive Director

dence indicates that when Phillips worked, he worked unusually long hours. He also took an unusually large number of vacations. We note that the Board's computation under subsection (1) must fairly account for Phillips' irregular work schedule.

REVERSED AND REMANDED.



Steven Roy SMITH, Appellant,

v.

Helen P. SHORTALL, Appellee.

No. S-1343.

Supreme Court of Alaska.

Feb. 13, 1987.

Former husband appealed from order of the Superior Court, Third Judicial District, Anchorage, William H. Fuld, J., which divided proceeds of former husbands' lawsuit and awarded former wife deficiency judgment on note secured by apartment complex on which former wife had foreclosed. The Supreme Court, Moore, J., held that: (1) antideficiency judgment statute precluded former wife from recovering deficiency judgment after electing remedy of nonjudicial foreclosure, and (2) tax liability of former husband and wife which had resulted in levy on proceeds of former husband lawsuit should have been offset against settlement proceeds before dividing them in accordance with divorce decree.

Reversed.

1. Mortgages ⇨373

By electing remedy of nonjudicial foreclosure, secured creditor under deed of trust lost her right to recover deficiency judgment. AS 34.20.100.

2. Mortgages ⇨378

Secured creditor's motion to compel payment and reduce to judgment was the type of "further action or proceeding" following nonjudicial foreclosure precluded by antideficiency judgment statute. AS 34.20.100.

See publication Words and Phrases for other judicial constructions and definitions.

3. Costs ⇨172

Paralegal services, if recoverable at all, are recoverable as costs rather than as attorney fees. Rules Civ.Proc., Rule 79(b).

4. Divorce ⇨254(1)

In determining net proceeds from former husband's lawsuit, which were to be divided between former husband and wife according to divorce decree, court did not err in declining to deduct costs of paralegal services in addition to attorney fees.

5. Divorce ⇨254(1)

In dividing proceeds of former husband's lawsuit in accordance with terms of divorce decree, court properly deducted amount which had been collected in trust for coplaintiff in lawsuit.

6. Internal Revenue ⇨4855

When Internal Revenue Service levied on proceeds of former husband's lawsuit which, according to divorce decree, was to be divided between former husband and wife, court should have offset tax liability from settlement proceeds rather than giving former wife 50% of net proceeds prior to levy, where levy was based on joint tax liability of former husband and wife.

Millard F. Ingraham, Anchorage, for appellant.

Laurel J. Peterson, Anchorage, for appellee.

Before RABINOWITZ, C.J., and
BURKE, MATTHEWS, COMPTON and
MOORE, JJ.

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OPINION

MOORE, Justice.

Steven Smith and Helen Shortall were divorced on April 28, 1983. The divorce decree required Smith to execute a promissory note for \$125,000 in Shortall's favor. The note was secured by a deed of trust on a warehouse apartment complex Smith owned. The note called for an initial payment of \$10,000 followed by annual installments of \$20,000, and contained an acceleration clause. In addition, the divorce decree required Smith to pay Shortall 50% of the net proceeds of an admiralty lawsuit then pending in the U.S. District Court, *Smith v. The ARCTURIS*.

Smith paid the initial \$10,000 due under the promissory note but defaulted on the first \$20,000 installment. Shortall accelerated the note. Pursuant to AS 34.20.070, the trustee elected to sell the warehouse apartment complex to satisfy her claim. At the trustee's sale, Shortall bid \$139,986.11, the total amount Smith owed her under the promissory note. After acquiring title to the property, she learned that its appraised value, less encumbrances and the cost of repairs, was approximately \$12,000.

Meanwhile, the *ARCTURIS* case settled. Smith received \$43,000, which he deposited into a trust account established by his attorney for the purpose of receiving and disbursing the proceeds of the settlement. Before any disbursements were made, the Internal Revenue Service levied on the account for a tax liability of \$22,884.42 owed jointly by Smith and Shortall. Smith's attorney paid the IRS claim from the trust account. The attorney also paid approximately \$7,000 in attorney's fee for the *ARCTURIS* lawsuit, and \$4,300 for a related claim that had been assigned to Smith by an *ARCTURIS* co-plaintiff for collection. The attorney divided the balance of the settlement proceeds equally between Smith and Shortall. Shortall received \$4,379.80.

Shortall moved for an order reducing to judgment the balance owed under the promissory note and compelling payment

thereof. In addition, she moved for an order to show cause why Smith should not be held in contempt for his handling of the *ARCTURIS* settlement proceeds. The superior court granted both motions, and subsequently entered final judgment awarding Shortall \$115,000 as principal due under the promissory note; \$13,706.71 for *ARCTURIS* proceeds; and interest, costs, and attorney's fees incurred in reducing to judgment the amount due under the promissory note. We reverse.

A. *The Promissory Note*

[1] The divorce decree obligated Smith to pay Shortall \$125,000. The obligation was evidenced by a promissory note and secured by a deed of trust. When Smith defaulted on the obligation, Shortall had several options. She could have waived the security of the deed of trust and sued on the note. Or, she could have brought an action to judicially foreclose the deed of trust, retaining the right to recover a deficiency judgment. AS 09.45.170; *Suber v. Alaska State Bond Committee*, 414 P.2d 546, 555 (Alaska 1966). Instead, Shortall elected the remedy of non-judicial foreclosure. By electing this remedy, Shortall lost her right to recover a deficiency judgment against Smith.

[2] Alaska's anti-deficiency judgment statute, AS 34.20.100, provides that

[w]hen a sale is made by a trustee under a deed of trust, as authorized by AS 34.20.070-34.20.130, no other or further action or proceeding may be taken nor judgment entered against the maker or the surety or guarantor of the maker, on the obligation secured by the deed of trust for a deficiency.

Shortall's motion to compel payment and reduce to judgment is precisely the type of "further action or proceeding" precluded by AS 34.20.100. *Hull v. Alaska Federal Sav. & Loan Ass'n*, 658 P.2d 122, 125 (Alaska 1983).

The effect of the trustee's sale was to discharge all of Smith's obligations under the note. Therefore, the superior court

erred in granting judgment for Shortall. We reverse the judgment and vacate the award of interest, attorney's fees, and costs incurred in reducing the note to judgment.

B. *The ARCTURIS Proceeds*

[3, 4] The divorce decree entitled Shortall to "50 percent of the net proceeds, that is, less costs and attorney's fees, if any," derived from the ARCTURIS lawsuit. The superior court calculated Shortall's share as 50 percent of the principal settlement (\$43,000) less attorney's fees (\$6,824.98). Smith argues that, before dividing the settlement proceeds, the court should have offset the claim assigned to Smith for collection (\$4,300) and IRS levy (\$22,884.42).¹ We agree.

[5] The \$4,300 represented proceeds Smith collected in trust for an ARCTURIS co-plaintiff. The money belonged to neither Smith nor Shortall, and was not part of the net proceeds of the suit.

[6] Spouses who file a joint income tax return are jointly and severally liable for the full tax liability. *United States v. Tietje*, 231 F.Supp. 738, 740 (E.D.Ill.1964). By declining to offset the tax liability from the settlement proceeds, the superior court placed the full burden of the liability on Smith alone. Absent evidence of equitable reasons for such a result, this was error.

REVERSED.



1. Smith also argues that the attorney's fees offset should have included the value of paralegal services. Paralegal services, if recoverable at all, are recoverable as costs under Alaska R.Civ.P. 79(b). *Atlantic Richfield Co. v. State*,

STATE of Alaska, Petitioner,

v.

James A. RIDGELY, Jr., Respondent.

No. S-1197.

Supreme Court of Alaska.

Feb. 13, 1987.

Defendant was convicted in the Superior Court, Third Judicial District, Anchorage, Victor D. Carlson and Ralph E. Moody, JJ., of murder and he appealed. The Court of Appeals, 705 P.2d 924, reversed. The Supreme Court, Moore, J., held that evidence sustained trial courts determination that defendant's confession was voluntary.

Reversed and remanded.

1. Criminal Law ⇐532

In determining voluntariness of confession, trial court must find the external, phenomenological facts surrounding the confession, must then infer an internal, psychological fact from those external facts, and must then assess the legal significance of that inferred mental state.

2. Criminal Law ⇐1158(4)

Trial court's determining historical facts surrounding confession is fact-finding task and reviewing court must defer to trial judge's findings unless they are clearly erroneous, but reviewing court has duty to examine entire record and make its own independent determination as to mental state of accused and its legal significance based on facts found by trial court.

3. Criminal Law ⇐531(1, 3)

State bears burden of proving voluntariness of *Miranda* waiver and of confession by preponderance of evidence.

723 P.2d 1249, 1253 (Alaska 1986). Whether paralegal services will be recognized as costs in a specific case is left to the discretion of the trial judge. There is no evidence here that the judge abused this discretion.

mit the plaintiff's truck to pass in safety. Were there no testimony tending to show that the plaintiff's truck, in turning around the "sand hole," was proceeding in the ordinary way and along the usual line of travel taken by loaded trucks, we should have a different situation. We think, however, under all of the circumstances of this case, that the jury was reasonably warranted in inferring that plaintiff's driver was not negligent. This being our conclusion, we think the court erred in changing the answers of the jury and in ordering judgment for defendant.

Judgment reversed, with directions to restate the verdict as rendered by the jury and to enter judgment in favor of the plaintiff for the amount of the damages found.

SURING STATE BANK v. GIESE et al.

Supreme Court of Wisconsin.

Feb. 6, 1933.

1. Evidence — 18.

Court judicially notices fact that present economic depression has affected realty values and caused almost complete absence of market for realty.

2. Mortgages — 526(2).

Without statute, equity court may decline to confirm foreclosure sale where bid is inadequate and economic conditions prevent competitive bidding.

3. Mortgages — 526(1).

Court in ordering foreclosure sale or resale may in its discretion take notice of economic emergency and fix minimum or upset price at which premises must be bid in if sale is confirmed.

Court may after proper hearing fix minimum or upset price at which premises must be bid in if sale is to be confirmed; this being a power that courts of equity ordinarily exercise in cases of foreclosure of corporate property which is of such size and character as to preclude establishment of fair price by competitive or cash bidding.

4. Mortgages — 526(6).

On application to confirm foreclosure sale, court may establish property's value and require that it be credited on judgment, giving mortgagee option to accept or not.

If court has not previously fixed an upset price, and, on application to confirm sale, adopts procedure of conducting hearing and establishing value of property and, as condition to confirma-

tion, requiring that fair value of property be credited on foreclosure judgment, mortgagee should be given option to accept or reject it, and, in event of its rejection, resale of property should be ordered.

Appeal from an order of the Circuit Court for Oconto County: Arold F. Murphy, Circuit Judge.

Action by the Suring State Bank against Ernestine Giese and others. From an order confirming a mortgage foreclosure sale on the condition that a deficiency judgment be denied, plaintiff appeals.—[By Editorial Staff.]

Reversed and remanded.

The order, which was entered on the 30th of June, 1932, confirmed the sale in an action for the foreclosure of a real estate mortgage "on the express condition that plaintiff's motion for a deficiency judgment against the defendants Giese be denied and such sale is thus confirmed and such deficiency judgment is expressly denied." The complaint in the action included a prayer for a deficiency judgment, and the judgment was in the usual form, and contained, among other things, an order for a deficiency judgment in the event that the proceeds of the sale be insufficient to pay the amounts due under the mortgage. The sheriff's report of sale contained the report of a deficiency upon the sale of \$1,379.18. Plaintiff's motion for an order confirming the sale and for a deficiency judgment followed.

The defendants, in opposition to the motion to confirm the sale, produced affidavits to the effect that the premises were worth from \$2,000 to \$3,000, while the affidavits in support of confirmation place the value of the premises at from \$1,000 to \$1,500. At the sheriff's sale plaintiff had bid in the property for \$600, charged against the defendants \$100.03 court costs and sheriff's fees, credited defendants with \$400.12, and asked for a deficiency judgment of \$1,379.18 upon an original loan of \$2,000.

Harold W. Kraeger, of Oconto, for appellant.

Lehner & Lehner and Adolph P. Lehner, all of Oconto Falls, and V. J. O'Kelliher, of Oconto, for respondents.

WICKIHEIM, J.

It is the contention of the plaintiff that it is entitled to a deficiency judgment as a matter of course; the court having in the original judgment ordered a judgment for deficiency, which order was appealable and has never been appealed from. This may well be conceded without at all affecting the

merits of this case. The order appealed from confirms the sale upon the express condition that plaintiff be not entitled to a deficiency judgment. The court finds in its order that the premises were reasonably worth a sum in excess of \$2,000, and it is evident from a reading of the order, that the trial court's theory is that plaintiff, having secured the premises at the grossly inadequate valuation of \$600, should be required to credit defendants with the reasonable value of the premises.

[1] The question presented is one of great importance, and one to which earnest consideration has been given. The court takes judicial notice of the fact that the present economic depression has not merely resulted in a serious dislocation of the value of real estate, but also in the almost complete absence of a market for real estate. As a consequence there is no cash bidding at sales upon foreclosure. In normal times competitive bidding is the circumstance that furnishes reasonable protection to the mortgagor, and avoids the sacrifice of the property at a grossly inadequate sale price. In the present situation the device of a judicial sale largely fails of its intended purpose because of the lack of competitive bidding, and the question arises whether a court of equity is wholly impotent to rise to the needs of justice and see that the parties are fairly and properly protected. This is not a situation in which ordinary logic with respect to values has much vitality. In theory, a thing that cannot be sold has no value, and so with a parcel of real estate that is offered for sale at foreclosure. It may be argued that it is worth what purchasers will pay for it, and no more, and that if the only price offered constitutes but a negligible part of its theretofore assumed value, it nevertheless represents the value of the real estate at that time. Such a conclusion is shocking to the conscience of the court, or, as the old equity courts said, to the conscience of the chancellor, and to all notions of justice as applied to this situation. Certainly the land has value so long as it or the buildings upon it may be used, and certainly in the case of farm lands, which constitute the homes of farmers, the premises have value in the sense of usefulness, however difficult it may be to translate this value into terms of dollars. Furthermore, this real estate, which is suffering from the consequences of a period of readjustment through which we are passing, has potential or future value which may legitimately be taken into account. Its value in terms of dollars has been affected by a general condition. No one piece of land has depreciated in value; it has all depreciated. It has all suffered from the lack of demand on the part of buyers. Under these circumstances it is within the power of a court of equity, without the aid of statute, to take

one or all of three steps for the protection of the parties and the promotion of a fair solution of the difficulties. What is said here is said in the light of the present emergency, and because of the present inadequacy of a judicial sale to establish a fair value for the security.

[2] 1. The court may decline to confirm the sale where the bid is substantially inadequate. While it has been said that mere inadequacy of consideration is not a ground for setting aside a foreclosure sale, this rule has been rather carefully circumscribed by the court. In *Griswold v. Earden*, 146 Wis. 35, 130 N. W. 952, 953, this court, speaking through Mr. Chief Justice Winslow, said: "It has been said by this court that it is the settled practice of courts of equity to refuse a resale for mere inadequacy of consideration, and that this court will not depart from that rule where no other cause exists. *Meehan v. Blodgett*, 56 Wis. 511, 37 N. W. 291. This is doubtless a correct statement of the rule, but it seems from the argument in the present case that it may be easily misunderstood. It must be strictly confined to cases where there is absolutely no fact appearing, except that the price is inadequate. Whenever other facts appear, such as mistake, misapprehension, or inadvertence on the part of the interested parties or of intending bidders, as a result of which it seems to the court the failure to obtain a fair and adequate price for the property was due in whole or in part to such mistake, misapprehension, or inadvertence, the court will readily refuse to approve the sale. No fraud is necessary to justify the court in so withholding its approval. The question simply is, Is the sale under all the circumstances one of which the court in justice to all parties should approve?"

This doctrine is also stated in *Kramer v. Thwaites*, 105 Wis. 534, 81 N. W. 654, and *Johnson v. Gault*, 106 Wis. 247, 82 N. W. 130. What was said in the *Griswold Case* is applicable here, when the fact of an inadequate price is coupled with an emergency which operates to prevent competitive bidding. A court of equity is justified in refusing to confirm the sale and ordering a resale.

[3] 2. The court, in ordering a sale or a resale, may, in its discretion, take notice of the present emergency, and, after a proper hearing, fix a minimum or upset price at which the premises must be bid in if the sale is to be confirmed. This is a power that courts of equity ordinarily exercise in cases of foreclosure of corporate property which is of such size and character as to preclude the establishment of a fair price by competitive or cash bidding. *Northern Pacific Railway Co. v. Boyd*, 225 U. S. 482, 33 S. Ct. 354, 57 L. Ed. 931. We see no reason why the same power should not be exercised in cases

where economic conditions are such as to preclude the element of competitive bidding, and to make ineffective the ordinary and usual manner of fixing the market value of the property.

[4] 3. The court may, upon application for the confirmation of a sale, if it has not theretofore fixed an upset price, conduct a hearing, establish the value of the property, and, as a condition to confirmation, require that the fair value of the property be credited upon the foreclosure judgment. If an upset price has been established, the plaintiff may be required to credit this amount upon the judgment as a condition to confirmation. If the fair value as found by the court, when applied to the mortgage debt, discharges it, there will be no occasion for the entering of a deficiency judgment. In case this procedure is adopted by the court, the option should be given to the plaintiff to accept or reject it. In the event of its rejection, the resale of the property should be ordered.

In the instant case the court evidently took the third of the three methods of dealing with this problem. While in terms it denied the deficiency judgment, in effect it valued the property, found this value to be equal to the debt, and required that it be credited against the debt as a condition to the confirmation of the sale. This was not error, for the reasons heretofore stated. However, it is our conclusion that plaintiff should have been given the option to accept or reject the condition. In the event that the condition is rejected, the court may set aside the sale and order a resale in accordance with the principles set out in this opinion. It follows that the order must be reversed.

Order reversed, and cause remanded for further proceedings in accordance with this opinion.

IN RE GRANGER'S ESTATE.

CONTINENTAL ILLINOIS BANK & TRUST
CO. v. WISCONSIN TAX COM-
MISSION et al.

Supreme Court of Wisconsin.
Feb. 6, 1933.

Taxation — 200(3).

Refusal to permit executor's appeal over 60 days after order fixing inheritance tax voluntarily paid by executor held not abuse of discretion (St. 1931, §§ 72.09(2), 72.101, 72.105).

It appeared that executor, for reasons which it deemed sufficient, notably the unlikelihood of a successful contest of con-

sideration of tax statute and the unwisdom of risking further funds of estate in prosecuting such a contest, deliberately decided not to appeal, paid the tax, and closed the matter about two and one-half months before a decision of United States Supreme Court in another case relative to state's power to impose inheritance tax under similar circumstances.

Appeal from an order of the County Court of Dane County; George Kroncke, County Judge.

Proceeding by the Continental Illinois Bank & Trust Company, as executor of the estate of Sarah L. Granger, deceased, wherein the executor filed a petition, opposed by the Wisconsin Tax Commission and others, seeking permission to appeal to the Supreme Court from an order determining the amount of an inheritance tax. From an order denying the petition, the executor appeals.—[By Editorial Staff.]

Affirmed.

The order appealed from was entered on June 18, 1932, and denied the appellant herein permission to appeal to the Supreme Court from the order determining the amount of the inheritance tax in the estate of Sarah L. Granger, deceased. Application for leave to appeal was filed within one year from the date of the said order, but more than sixty days thereafter.

Sarah L. Granger was a resident of Chicago at the time of her death on July 1, 1927, and had never been a resident of Wisconsin. At the time of her death, she owned 450 shares of the capital stock of the Oconto Company, a Wisconsin corporation. Aside from this she had no estate or property in Wisconsin. The executor petitioned the county court of Dane county, Wis., for special administration for the purpose of determining the inheritance tax due to the state of Wisconsin upon the transfer of this stock. On October 3, 1931, the county court of Dane county made an order determining the inheritance tax at \$1,300.48, plus interest of \$606.17. This amount was paid to the county treasurer of Dane county on October 16, 1931. On January 4, 1932, the United States Supreme Court, in *First National Bank of Boston v. State of Maine*, 251 U. S. 312, 52 S. Ct. 174, 70 L. Ed. 313, held that a state cannot, consistently with due process of law, impose a tax upon a transfer of shares of stock in a corporation of the state, and that the situs, for succession tax purposes, of shares of stock, is at the domicile of the owner rather than at the home of the corporation.

Thereafter, in February, 1932, the executor petitioned the county court for an order per-

71 Wis.2d 359

**FIRST WISCONSIN NATIONAL BANK
OF OSHKOSH, Respondent,**

v.

**KSW INVESTMENTS, INC., a Wisconsin
Corporation, Appellant, Gerald Kramer,
a/k/a Jerry Kramer, et al., Defendants.**

No. 628 (1974).

Supreme Court of Wisconsin.

Submitted Dec. 2, 1975.

Decided Feb. 10, 1976.

Mortgagee moved for order confirming foreclosure sale of mortgagor's property to mortgagee and for a deficiency judgment. The Circuit Court, Winnebago County, William E. Crane, J., confirmed price bid by mortgagee at foreclosure sale and ordered deficiency judgment against mortgagor, and mortgagor appealed. The Supreme Court, Day, J., held trial court's order confirming sale would be reversed where trial court erred as matter of law in criteria used to establish fair value of property; that statute providing for application for confirmation of sale and for deficiency judgment mandates that no sale shall be confirmed until court is satisfied that fair value of premises has been credited toward mortgage debt; that trial court should, when confronted with such motion, make specific finding of fair value of premises and make specific finding that such value has been credited towards debt; and that in determining "fair value," price which person willing and able to buy property would reasonably pay for it, not for purposes of speculation, but for that use to which it has been or reasonably may be put, should be considered.

Reversed and remanded.

1. Mortgages — 526(1, 2)

Decision to confirm judicial sale following foreclosure is vested in broad discretion of trial court, but such confirmation may be

refused if there is apparent inadequacy in price which was caused by mistake, misapprehension, or inadvertence on part of interested parties or possible bidders. W.S.A. 816.165(2).

2. Mortgages — 526(2)

Confirmation of judicial sale following foreclosure of mortgage may be denied in discretion of trial court if bid price was so inadequate so as to shock conscience of court. W.S.A. 816.165(2).

**3. Appeal and Error — 945, 946
Courts — 26**

Trial court, when acting on matters resting within its discretion, must exercise legal discretion; if that discretion is abused or if court proceeds upon mistaken view of law, reviewing court will reverse.

4. Mortgages — 579

Trial court's order confirming judicial sale following mortgage foreclosure would be reversed where trial court erred as matter of law in criteria used to establish fair value of property. W.S.A. 816.165(2).

5. Mortgages — 526(1)

In determining "fair value" of premises for purpose of statute requiring that no sale of mortgaged property shall be confirmed or judgment for deficiency rendered until court is satisfied that "fair value" of premises sold had been credited on mortgage debt, price which person willing and able to buy property would reasonably pay for it, not for purposes of speculation, but for use to which it has been or reasonably may be put, should be considered by court. W.S.A. 816.165(2).

See publication Words and Phrases for other judicial constructions and definitions.

6. Mortgages — 526(6)

Mortgagee's expert's appraisal of value of property, in mortgagee's action for con-

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firmation of judicial sale of property following foreclosure and for deficiency judgment, which was based on his opinion of fair value of building valued as vacant, empty shell, even though both he and mortgagee's vice president regarded highest and best use of property was as bar-restaurant facility, was erroneously accepted by trial court in determining validity of sale. W.S.A. 816.165(2).

7. Mortgages — 526(6)

Language of statute governing confirmation of judicial sale of property following foreclosure mandates that no sale shall be confirmed until court is satisfied that fair value of premises has been credited toward mortgage debt, interest and costs; language to contrary in *Citizens Bank of Sheboygan v. Rose* (1973), 59 Wis.2d 385, 208 N.W.2d 110, withdrawn.

8. Mortgages — 526(6)

Trial court should, when confronted with mortgage to confirm sheriff's sale where mortgaged premises have been sold for less than amount due on mortgage, make specific finding of fair value of premises and make specific finding that such value has been credited toward mortgage debt, even though trial court's conscience is not shocked by bid; language to contrary in *Citizens Bank of Sheboygan v. Rose* (1973), 59 Wis.2d 385, 208 N.W.2d 110, withdrawn. W.S.A. 816.165(2).

Brief by: Berk, Pressentin & Hoida, Green Bay, for appellant.

Brief by: Timothy M. Dempsey and Dempsey, Magnusen, Williamson & Lampe, Oshkosh, for respondent.

DAY, Justice.

This is an appeal from an order confirming the price bid by the mortgagee, First Wisconsin National Bank of Oshkosh, at a foreclosure sale, and which also ordered a deficiency judgment against the appellant in the amount of \$124,458.06. The issue

raised is whether the price bid by the mortgagee was so inadequate as to result in an injustice to the owners of the property, if approved. *Home Bank v. Becker* (1970), 48 Wis.2d 1, 13, 179 N.W.2d 855. After reviewing the record, we reverse the order, not simply because the bid was very low, but more accurately because the trial court erred in finding the fair value of the property based on testimony establishing the fair market value of the building as an empty, vacant shell.

KSW Investments, Inc., purchased the property which is the subject of this appeal in 1969 for the sum of \$60,000. At the time of the purchase, the building, which was located in downtown Oshkosh directly across the street from a new bank building and one or two blocks from a new shopping center, was being used as a printing facility. On or about May 16, 1969, appellant KSW Investments, Inc., (hereafter KSW), executed and delivered to the respondent, First Wisconsin National Bank of Oshkosh (hereafter bank), its promissory note and mortgage for purchase money and improvement funds in the sum of \$100,000. At that same time, Gerald Kramer and Ben C. Stone, officers of KSW, delivered to the bank their guaranties each in the sum of \$130,000.

Approximately one year later, on May 5, 1970, KSW executed and delivered to the bank another promissory note and mortgage upon the premises in the sum of \$23,000. At this time, Kramer and Stone reissued their guaranties in the sum of \$153,000.

The property was purchased for investment purposes and was completely remodeled by KSW as a "Red Ram" restaurant, involving the expenditure of \$160,000 to \$170,000 for improvements, not including personal property, or the necessary equipment for operation as a restaurant. The property was leased to the management of the Red Ram restaurant.

Thereafter, the property underwent a number of management changes, and from

1970 to 1974, four different restaurant, bar or restaurant-bar businesses occupied the building. At the time of the foreclosure, the building was occupied by a bar known as the "Paddock Club."

KSW made no payments of principal or interest on the \$100,000 note after February 16, 1971, or on the \$23,000 note after January 16, 1971. In addition, real estate taxes and special assessments were left unpaid from 1969 throughout the foreclosure proceedings.

The foreclosure action was commenced and KSW did not answer. Judgment of foreclosure was entered and the property was ordered sold at a sheriff's sale. The bank was the only party present at the sale and made the only bid in the amount of \$23,000, subject to the delinquent real estate taxes, prorated real estate taxes, and interest due on the judgment—an additional amount of approximately \$23,000.

Thereafter the bank moved for an order confirming the sale and for a deficiency judgment. A hearing was held at which the bank presented testimony of its appraiser, Gordon Kargus, who testified he appraised the property at its fair market value as a vacant building—a shell. According to Kargus, the property had a fair market value of \$46,800.

KSW also presented the testimony of an appraiser who testified that in his opinion, the property had a market value of \$155,000, including personal property, and a fair market value of \$131,000 without the personal property.

Additionally, by stipulation documents were introduced in evidence indicating that the property had been assessed by the city of Oshkosh in 1969, the year of its purchase, at \$26,900; for 1970 through 1972 at \$62,600; and for 1973, the year of the foreclosure sale, at \$45,500. Testimony established that this type of property was assessed by the city assessor at 40% of its market value, which translates into market values of \$67,250 for 1969; \$156,500 for 1970 through 1972; and \$113,750 for 1973. It was not

stipulated that those were in fact correct market values for this property.

After hearing the testimony, the trial court rendered its decision, stating:

"The question before the court for determination is as to the fair value at a sheriff's sale, recognizing that a sheriff's sale is a distress sale and that the full fair market value is not necessarily received, and under Wisconsin decisions, it is not required.

"Recognizing that this is a distress sale, and recognizing further that the defendant KSW Investments and Mr. Stone had notice of this sale and chose not to attend and not to bid, all in all, the court finds that the bid price bid by the First Wisconsin National Bank of Oshkosh of \$23,000, assuming taxes which then amounted to \$23,500 or more, and they would be more at this time, was a fair value for the premises, and the court will therefore enter an order at this time and does order that the report of the sheriff be confirmed"

[1, 2] It is well settled that the decision to confirm a judicial sale following a foreclosure is vested in the broad discretion of the trial court, but such confirmation may be refused if there is an apparent inadequacy in the price which was caused by mistake, misapprehension or inadvertence on the part of the interested parties or possible bidders. See *Gumz v. Chickering* (1963), 19 Wis.2d 625, 121 N.W.2d 279. Additionally, such confirmation may be denied in the discretion of the trial court if the bid price was so inadequate so as to shock the conscience of the court. *Gumz v. Chickering*, Id.; *Citizens Bank of Sheboygan v. Rose* (1973), 59 Wis.2d 385, 388, 208 N.W.2d 110, and cases cited therein.

Sec. 816.165(2), Stats., (formerly sec. 278.105, Stats.), provides:

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"(2) In case the mortgaged premises sell for less than the amount due and to become due on the mortgage debt and costs of sale, there shall be no presumption that such premises sold for their fair value and no sale shall be confirmed and judgment for deficiency rendered, until the court is satisfied that the fair value of the premises sold has been credited on the mortgage debt, interest and costs."

There is no claim in the instant case that the alleged inadequate bid price was the result of mistake, misapprehension or inadvertence; rather, the argument is that the price of \$23,000 bid by the bank was so inadequate as to shock the conscience of the court.

[3] By finding the \$23,000 bid made by the bank to be the "fair value" of the property, the trial court implicitly found that the bid was not so inadequate as to shock its conscience. Such determination if made in the exercise of the trial court's discretion ordinarily will be affirmed by this court. However, we have held that the trial court, when acting on matters resting within its discretion, must exercise a legal discretion. If that discretion is abused or if the court proceeds upon a mistaken view of the law, this court will reverse. *Churchill v. Welsh* (1879), 47 Wis. 39, 54, 55, 1 N.W. 398. See also *Beberfall v. Beberfall* (1969), 44 Wis.2d 450, 171 N.W.2d 390.

This court has stated:

"This means that for this court to affirm what is contended to be a discretionary act there must be evidence that discretion was in fact exercised. If a judge bases the exercise of his discretion upon an error of law, his conduct is beyond the limits of discretion." *State v. Hutnik* (1968), 39 Wis.2d 754, 763, 159 N.W.2d 733, 737.

1. The appraisal by Kargus was made in May of 1973. In April of 1970, the bank had the property appraised at \$199,000 by Robin Jones. This gross disparity in appraisals remains unexplained in the record, except perhaps by the fact that the earlier appraisal was made when the Red Ram was occupy-

Also in *State ex rel. Schuller v. Roraff* (1968), 39 Wis.2d 342, 349, 350, 159 N.W.2d 25, 29, cert. den. 393 U.S. 1066, 89 S.Ct. 716, 21 L.Ed.2d 709, this court stated:

"... a discretionary order made by a trial court as a result of an erroneous view of the law may be reversed without establishing an abuse of discretion on the part of the trial judge..." (citations omitted)

[4] We conclude the order confirming the sale must be reversed because the trial court erred as a matter of law in the criteria it used to establish the fair value of the property.

In *Citizens Bank of Sheboygan v. Rose*, *supra*, this court noted "shocking the conscience of the court is another way of saying that the price is inadequate as a matter of law." *Id.* 59 Wis.2d at p. 389, 208 N.W.2d at p. 112. In the instant case, both sides presented testimony from their respective appraisers relating to the value of the property. The trial court accepted and adopted the appraisal made by Kargus for the bank. Kargus appraised the property at \$46,800. This appraisal was based on the property as a vacant, empty shell and from Kargus' own testimony, the figure given represented his opinion of the fair market value of the building as a vacant shell even though both he and the bank's vice-president recognized that the highest and best use of the property was as a bar-restaurant facility.¹

This fair market value of the building as a shell was followed by the trial court in determining the statutorily mandated "fair value" of the property. This court has previously stated with respect to the "fair value" of the foreclosed property as that term is used in the statutes th-

ing the building. Thus presumably the earlier appraisal was made on the basis of the property being used as a bar-restaurant, while the latter appraisal was made, although the building was occupied at the time by a bar, as if the building were a vacant shell.

Rafferty v. Roraff
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"'Fair value' obviously does not mean 'market value' as that term is generally understood, or that value which the property may probably have in the future under more favorable economic conditions or that value which it may have if the property be remodeled and put to other or more extensive uses which possibly may prove more profitable."

Northwestern Loan & Trust Company v. Bidinger (1937), 226 Wis. 239, 245, 246, 276 N.W. 645, 648.

The statute requires that the trial court be satisfied that the fair value of the premises sold has been credited on the mortgage debt, interest and costs prior to confirming the sale. In *Northwestern Loan & Trust Company v. Bidinger*, *supra*, at 247, 276 N.W. 645, this court recognized that the statute above quoted first enacted by Chapter 449, Laws of 1935, was a direct outgrowth from and almost an identical restatement of this court's opinion in *Suring State Bank v. Giese* (1933), 210 Wis. 489, 246 N.W. 556. In the *Suring State Bank* case, the foreclosed property had been bid in at a sheriff's sale for approximately one-third of its value and the mortgagee who was the purchaser at the sale was demanding a deficiency judgment for over \$1,600, so that, if the sale had been confirmed, the mortgagee would have had the property and still had a claim for more than four-fifths of the original loan. In *Suring State Bank*, this court recognizing the then existing economic depression and emergency, and acknowledging the inadequacy of a judicial sale to establish a fair value for the security, because of such emergency resulting in the absence of competitive bidders, stated that the trial court when presented with a motion to confirm a foreclosure sale, could do any one of the following things:

"(1) The court may decline to confirm the sale where the bid is substantially inadequate.

"(2) The court, in ordering a sale or a resale, may, in its discretion, take

notice of the present emergency and after a proper hearing, fix a minimum upset price at which the premises must be bid in if the sale is to be confirmed

"(3) The court may, upon application for the confirmation of a sale, if it has not theretofore fixed an upset price, conduct a hearing, establish the value of the property, and, as a condition to confirmation require that the fair value of the property be credited upon the foreclosure judgment." *Id.* at pp. 492-493, 246 N.W. at p. 557.

Sec. 278.105, Stats., merely codified the decision in the *Suring Bank* case with respect to the establishment of the fair value of the property and its application toward the mortgage debt. The term "fair value" and "real value" were used interchangeably in the *Suring Bank* case and following cases.

In *Kremer v. Rule* (1934), 216 Wis. 331, 257 N.W. 166, this court spoke to the question of the definition of market value and real value and stated:

"'Market value', as ordinarily defined, can have little if any, application to a mortgage foreclosure sale where obviously the defendant mortgagor is forced to sell and where the plaintiff mortgagee, in the absence of other bidders, is obliged to bid if the foreclosure sale is to be consummated. So when a court is determining 'real value of the premises' for the purpose of giving to the mortgagee the option to credit the amount thereof on the foreclosure judgment as a condition precedent to confirmation of a mortgage foreclosure sale which has already taken place upon a bid deemed by the court to be substantially inadequate, it should not consider 'market value' as that expression is ordinarily used and understood, much less the value that the premises may have had at some remote time or may have in the future if the price is obtainable for farm products prevalent during such past remote period shall again prevail.

"Real value of the premises' as used in the *Suring* case, should approximate that price which a person willing and able to buy the property would reasonably pay for it, not for purposes of speculation, but for that use to which it has been or reasonably may be put." *Id.* at pp. 338-339, 257 N.W. at p. 169. (emphasis supplied)

The language of the statute that "no sale shall be confirmed and judgment for deficiency rendered until the court is satisfied that the fair value of the premises sold has been credited on the mortgage debt, interest and cost" was subsequently interpreted by this court to mean nothing more than "such reasonable value as does not shock the conscience of the court." *Northwestern Loan & Trust Company v. Bidinger*, *supra*, 226 Wis. at p. 247, 276 N.W. at p. 649.

[5] In the instant case, the testimony upon which the court based this determination did not establish the fair value of the premises since Kargus, the appraiser, clearly applied the fair market value test to the building as if it were a vacant shell. This is not consistent with the definition of the fair value of the premises stated in *Kremer v. Rule*, *supra*. In determining the fair value of the premises, as that term is used in the statutes, the trial court should have considered the price which a person willing and able to buy the property would reasonably pay for it, not for purposes of speculation, but for that use to which it has been or reasonably may be put.

[6] Because the trial court relied on the appraisal of the fair market value of a vacant building in determining the bid represented the fair value of the property, the trial court erred as a matter of law.

[7,8] We note that certain language of this court in *Citizens Bank of Sheboygan v. Rose*, *supra*, appears to be inconsistent with the dictates of sec. 816.165(2), Stats., with respect to when a fair value must be found. In that case, this court said, 59 Wis.2d at pp. 388-389, 208 N.W.2d 112:

"The upset price or the fair value finding is utilized in the discretion of the court only after the court finds the price bid to be so inadequate as to shock its conscience. See *Kremer v. Rule* (1934), 216 Wis. 331, 257 N.W. 166; *Brinckley v. Sager* (1939), 232 Wis. 88, 286 N.W. 570; *Welfare Building & Loan Association v. Gearhard* (1940), 235 Wis. 229, 293 N.W. 813."

The statute itself does not speak in terms of the trial court being required to be shocked by an inadequate bid price before a fair value need be determined. Clearly, the parties and the trial court in this case did not interpret the statute that way since the trial court set the fair value of the premises at the price bid by the bank after the hearing on the motion to confirm. The language of the statute mandates that no sale shall be confirmed until the court is satisfied that the fair value of the premises has been credited toward the mortgage debt, interest and costs. For ease of administration and consistent with logical interpretation of the statute, the trial court should, when confronted with a motion to confirm a sheriff's sale where the mortgaged premises have been sold for less than the amount due on the mortgage, make a specific finding of the fair value of the premises and make a specific finding that such value has been credited toward the mortgage debt. These findings should be made even though the trial court's conscience is not shocked by the bid. The language to the contrary in *Citizens Bank of Sheboygan v. Rose*, *supra*, is withdrawn.

This interpretation more accurately reflects the language and meaning of this statute which has caused difficulty in interpretation for some time. For example, one commentator has stated that ever since the *Suring Bank* case, *supra*, this court "has been explaining just what was meant and correcting the methods of applying the statute by the lower court." Worthing, "Real Estate Foreclosures", 34 Wis. Bar Bul-

letin 63, at 72, (Dec., 1961). See also, 1939 Wis.L.Rev. 89, The Work of the Wisconsin Supreme Court, pp. 90-91.

In the instant case, we reverse the order confirming the sale since the trial court erroneously relied on the appraisal of the fair market value of the building as a vacant shell in determining the fair value of the property. We remand the case to the trial court with directions to hold a new hearing on the motion to confirm the sale. At this new hearing, each side should be given an opportunity to present testimony to establish the fair value of the property as that term has been defined herein.

The appellant also objected to various observations made by the trial judge during the hearing as to his personal knowledge of

the area. In view of the fact that this case is to be reheard, the matter of judicial notice will be subject to the new code of evidence. Sec. 902.01 covers judicial notice of adjudicative facts and provides that the parties may be heard as to the propriety of taking judicial notice and the tenor of the matter noticed.

The order is reversed and the cause remanded for further proceedings not inconsistent with this opinion.



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WILLIAM L. McNALL
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AREA CODE 907
TELEPHONE 278-8538

March 3, 1988

The Honorable Representative Kay Brown
Chairperson
House Judiciary Subcommittee
on Economic Recovery
P.O. Box V
Juneau, Alaska 99811

Re: Amendments to Foreclosure Statutes

Dear Honorable Representative Brown:

Enclosed are the proposed amendments and deletions of the foreclosure statutes. I wish to amplify the need for legislative action. In further discussion with bank counsel I am advised that lenders who now have the power as set forth in Moening and Conrad not only will use their ability to sue on the note as opposed to foreclosing, but probably have a duty to their shareholders to do so. Certainly lenders who are already aggressively pursuing collection efforts will add this "new" tool to their arsenal. It is quicker, less expensive, and has much greater impact on the borrower.

Sincerely yours,

LAW OFFICES OF WILLIAM L. McNALL

By: William L. McNall
William L. McNall

WLM:scl

Enclosure - as stated.

§ 09.45.170

ALASKA STATUTES

§ 09.45.

Article 3. Foreclosure of Liens.

Delete Sec. 09.45.170. Judgment on foreclosure of lien.

Add new to read as follows:

Sec. 09.45.170. Procedure on default of deed of trust or deed of trust notes for foreclosure of lien. (a) Upon default by a borrower, a secured creditor shall pursue a foreclosure either judicially or nonjudicially.

(b) After issuance of the notice of default, the amount of applicable mortgage insurance, if available, will be applied to the note balance thereby reducing the amount of the unpaid balance of the mortgage prior to further foreclosure action being taken.

(c) In a nonjudicial foreclosure, the beneficiary must at the foreclosure sale, bid the fair market value of the property as defined in Section 5 up to the mortgage balance, including costs of sale and attorney's fees.

(d) In a judicial foreclosure, the court, prior to sale, must establish the fair market value of the property.

(e) Fair market value of the property is defined as the real value of the property which should approximate the price a person acting without duress would be willing to sell the property for, and which a person willing and financially able to buy the property would reasonably pay therefore, not for purposes of speculation but for that use to which it has been or may be put. The Legislature finds such real values should be equivalent to the replacement costs as adjusted for wear and tear.

(f) Beneficiary may then apply to the court for confirmation of the sale and recover a deficiency judgment together with costs and reasonable attorney's fees on the remaining balance of the debt.

Add new Sec. to read as follows:

Sec. 09.45.171. Election of remedies. At the time the foreclosure action begins, lender must elect to proceed judicially or nonjudicially. Once the election is made lender cannot re-elect.

Delete Sec. 09.25.180. Sale of encumbered property.

§ 09.45.180

ALASKA STATUTES

§ 09.45.

Add new Sec. to read as follows:

Sec. 09.45.180. Inferior deed of trusts and deed of trust note. In the event a beneficiary of a deed of trust loses the security due to a foreclosure of a superior deed of trust, the beneficiary shall have the right to bring an action directly upon the unpaid balance of the promissory note secured by the deed of trust.

Delete Sec. 09.45.200.

Delete Sec. 09.45.210.