California Legislation Curbing Deficiency Judgments

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I

HISTORY, NATURE, AND SCOPE

A. History of California Legislation

The great depression of the early 1930's and its disastrous effect on land values prompted the California Legislature, like the legislative assemblies of other states, to enact measures aimed at relieving the plight of debtors whose obligations were secured by mortgages or other security interests in land. This type of legislation, known as moratoria, varied considerably in its details, but, generally speaking, consisted in postponement or stay of foreclosure sales, extension of redemption periods, grant of powers to cure defaults, abolition of, or limitations on, deficiency judgments, or a cumulation of all these measures.\(^1\) The provisions relating to postponements and stays of foreclosures were transitional in character and disappeared from the statute books in the middle 1940's.\(^2\) But the restrictions on deficiency judgments remained a permanent part of the law in a number of states.\(^2a\)

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\(^2\) In California all general moratoria were terminated by the clean-up legislation of 1945, Cal. Stat. 1945, ch. 294, p. 752, 755, § 10. For a survey of the prior legislation see Comment, *Moratoria and Stay Laws; Mortgage Moratoria Legislation in California*, 30 Calif. L. Rev. 172 (1942).

\(^{2a}\) See Note, *Mortgages—"Depression Jurisprudence"—Remaining Effects in Statutory*
In California the first two acts of this nature were passed in 1933 as chapters 642 and 793. In addition to making other changes, such as enacting provisions for the reinstatement of mortgages and deeds of trust having become due as the result of a failure to pay installments or to make other specified payments and for the foreclosure by action of deeds of trust as an alternative means of enforcement, chapter 642 introduced two important provisions relating to deficiency judgments, numbered as Code of Civil Procedure sections 580a and 580b. The first of these new sections limited the amount of a deficiency judgment following the exercise of a power of sale in a mortgage or deed of trust securing the obligation sought to be enforced to the difference between the amount of such obligation and the fair market value of the property sold, and, in addition, required that such action for a deficiency be brought within three months of the time of the sale. Code of Civil Procedure section 580b in its original form prohibited any deficiency judgment after any sale under a purchase-money mortgage or deed of trust. The other of these statutes of 1933, chapter 793, amended Code of Civil Procedure section 726 by limiting deficiency judgments, after foreclosure by action, to the difference between the amount of the indebtedness and the appraised fair market value of the real property sold at the time of the sale under the foreclosure decree.

In 1935 the legislature re-enacted the first of these two acts, except for one section not material here, in order to remove an ambiguity created by wording contained in the deleted section relative to the intended permanency of the provisions thus re-enacted. Subsequently, in the case of Stockton Sav. & Loan Bank v. Massanet, the supreme court accepted the construction of the original act in the sense in which the legislature had attempted to clarify its original intent.

At the same time, but by separate act, Code of Civil Procedure section 580b was amended so as to include in the occurrences barring defi-
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 deficiency judgments "any sale of real property for failure of the purchaser to complete his contract of sale."

In 1937 the legislature defined more clearly the procedure for obtaining limited deficiency judgments after a judicial foreclosure sale under Code of Civil Procedure section 726 and introduced a three months' limitation for the respective applications.11

In 1939 a further section, numbered as Code of Civil Procedure section 580c, was added.12 It barred deficiency judgments upon notes secured by land mortgages or deeds of trust after sales under the power contained in such mortgages or trust deeds. Since the section number allocated to the new provision conflicted with the numbering of an already existing section of different content and contained another mistake in draftsmanship (using the term "mortgagor" instead of "mortgagee") the legislature repealed the new statute in 1940 and re-enacted it with the proper correction, this time numbering it Code of Civil Procedure section 580d.13 As will be discussed in more detail subsequently, the enactment of this new provision curtailed greatly the area of applicability of Code of Civil Procedure section 580a.

The last substantial amendment came in 1949.14 It added a second paragraph to Code of Civil Procedure section 580b barring deficiency judgments in cases where chattel mortgages and land mortgages or trust deeds have been given to secure the combined purchase price of both real and personal property.

B. Constitutionality: Application to Pre-existing Mortgages or Trust Deeds

There was never any real doubt about the constitutionality of the prospective application of the anti-deficiency legislation.15 Problems arose, however, with regard to its applicability to mortgages or deeds of trust executed prior to enactment of some of these provisions. To be sure, there was no such question in relation to the new Code of Civil Procedure section 580d, since by its own terms it was applicable only to mortgages or deeds of trust executed after its effective date, i.e., September 19, 1939, and March 6, 1941, respectively (because of its repeal and re-enactment). However, the other new sections (Code of Civil Procedure sections 580a, 580b, 725a, and the clause added to 726) limiting the amount of deficiency judgments, did not contain similar provisions. In Bennett v. Superior Court16 the district court of appeal held that Code of Civil Procedure sec-

tion 580a, insofar as it limits the amount of deficiency judgments, could not be applied constitutionally to a pre-existing mortgage or deed of trust, and in *Central Bank of Oakland v. Proctor*17 the supreme court expressly endorsed this ruling. Other cases have reached the same result, though not necessarily on constitutional grounds.18

Conversely, in *Miller v. Hart*19 the supreme court declared that the limitation of Code of Civil Procedure section 726 as to the amount of deficiency judgments was applicable to deeds of trust executed prior to its effective date, *i.e.*, August 21, 1933, and that such construction did not violate the federal or state constitution, for the reason that prior to this time there was no statutory right to judicial foreclosure of deeds of trust and the legislature was free to grant the additional remedy subject to limitations. Of course, this reasoning and holding is inapposite to mortgages (whether with or without power of sale) executed prior to the effective date of the clause in question. Likewise, Code of Civil Procedure section 580b has been held inapplicable in its entirety to mortgages and deeds of trust executed prior to its effective date.20 However, the three-month limitation imposed upon actions for deficiencies within the maximum permitted for deficiency judgments, which was also a part of Code of Civil Procedure section 580a as originally enacted, has been held capable of, and meant to have, retrospective application.21

**C. Anti-Deficiency Legislation in Relation to Other Restrictions on the Remedies of Secured Creditors**

Legislation confining or barring deficiency judgments is not the sole restriction on the remedies of creditors taking or reserving security interests in land. It is only one of a congeries of limitations which a creditor so secured faces in California with regard to the enforcement of his rights. Others, based on statute or judicial policies, include in particular: (1) the requirement that he rely upon his security before enforcing the secured

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17 5 Cal. 2d 237, 54 P.2d 718 (1936).
deficit, flowing from the "one form of action" statute\textsuperscript{22} or equivalent judicial policies;\textsuperscript{23} and (2) the rules against piecemeal foreclosure of multiple (cumulative) security interests in land.\textsuperscript{24}

\textbf{D. Interrelation of the Several Provisions Barring or Limiting Deficiency Judgments}

As is evident from the history of the legislation in question, the various provisions curbing deficiency judgments cover different aspects of an important field of law and their interrelation is of considerable importance. Actually, there exists a veritable hierarchy of the governing rules:

(1) Code of Civil Procedure section 580b is the rule which cuts most deeply into the rights of the secured creditor because it bars completely all deficiency judgments in favor of creditors holding security for purchase money, regardless of the method of enforcement of such security.

(2) Next in stringency is Code of Civil Procedure section 580d because it completely bars deficiency judgments on notes secured by mortgages or deeds of trust, but only if the security interest was foreclosed by sale under a power contained in the governing instrument.

(3) The least reduction of the normal rights of secured creditors is produced by the limitations on the amount of deficiency judgments specified in Code of Civil Procedure sections 580a and 726. However, both these sections are inapplicable in cases of purchase-money security as they are controlled by Code of Civil Procedure section 580b. Moreover, the applicability of Code of Civil Procedure section 580a is further superseded by Code of Civil Procedure section 580d, \textit{i.e.}, in cases of mortgages and deeds of trust securing notes (not for purchase money) executed after September 19, 1939, where the security has been foreclosed under a power of sale.

\textbf{E. Anti-Deficiency Legislation and Judicial Interpretation}

As will be demonstrated in greater detail, the courts have exhibited a very hospitable attitude toward the legislative policy underlying the anti-deficiency legislation and have given it a broad and liberal construction that often goes beyond the narrow bounds of the statutory language. Moreover, the courts have been loath to accept any stratagem calculated to circumvent the social purposes attributed to the legislation by judicial

\textsuperscript{22} \textit{Cal. Code Civ. Proc.} § 726.
\textsuperscript{23} \textit{Bank of Italy Nat'l Trust \\& Sav. Ass'n v. Bentley}, 217 Cal. 644, 20 P.2d 940 (1933).
construction. A practitioner who relies upon the mere language of the sections, or who hopes to have found "a way out," may be sorely disappointed by the results of his course of action.

II

PURCHASE-MONEY SECURITY AS A BAR TO DEFICIENCY JUDGMENT

A. Scope and Structure of Code of Civil Procedure Section 580b in General

The first paragraph of section 580b provides:

No deficiency judgment shall lie in any event after any sale of real property for failure of the purchaser to complete his contract of sale, or under a deed of trust, or mortgage, given to secure payment of the balance of the purchase price of real property.

As the history and text of this paragraph indicate, the law contemplates two separate categories of cases in which deficiency judgments are barred: (1) after any sale of real property under a purchase-money deed of trust or mortgage; and (2) after any sale of real property for failure of the purchaser to complete his agreement. Although the common denominator of both these categories is the factor that each involves purchase-money security, it must be recognized that each has its own ramifications and requires separate treatment.

B. Purchase-Money Deeds of Trust and Mortgages as a Bar to Deficiency Judgments

1. Elements of the Bar of Section 580b in Cases of Purchase-Money Deeds of Trust and Mortgages: (a) "After Sale"

A careful reading of the language of section 580b reveals several mysteries. The pertinent portion of this section specifies that there can be no deficiency judgment after any sale under a purchase-money deed of trust or mortgage. Accordingly, on the one hand the statute literally does not require that the sale must have been under a purchase-money deed of trust or mortgage executed to, or for the benefit of, the creditor seeking the deficiency judgment. On the other hand, it seemingly demands that there must have been a sale, whether by virtue of a foreclosure decree or a power, under some purchase-money mortgage or trust deed. As a result, courts have been perplexed about the proper sphere of the bar in question.

The leading decision giving an authoritative exegesis to the purview of the section is Brown v. Jensen. The decision held that there could be no deficiency judgment after any sale under a purchase-money deed of trust or mortgage.

tion, and defendants, as part of the purchase price, executed in favor of the institution a note for $11,300, secured by a first deed of trust on the property; at the same time, as another part of the purchase price, defendants executed to plaintiffs another note for $7,200 secured by a second deed of trust on the property. After default the first deed of trust was foreclosed under the power of sale contained therein. Plaintiffs made no attempt to buy the property at the trustee's sale and brought an action on the note. The court held that section 580b constituted a bar to a recovery. In reaching this result, Justice Carter, speaking for the majority of the court, stated that "the clear import of the wording of section 580b" was that a creditor taking a purchase-money deed of trust or mortgage on the property sold may look only to the security. Rejecting the argument that use of the term "deficiency judgment" or of the words "after the sale" requires that there have been an actual foreclosure sale of the security interest, the court held that the bar applies to situations in which there was such a sale, as well as those in which a sale would be an idle act because the security is exhausted, as was the case in the controversy at hand. The contrary construction given the section in Hillen v. Soule was disapproved and reliance was placed upon Mortgage Guarantee Co. v. Sampsell, in which the court had stated that the security alone may be looked to for payment of a debt secured by a purchase-money mortgage or deed of trust.

Following the doctrine of Brown v. Jensen the courts have clung to the view that section 580b deprives the holder of a purchase-money deed of trust or mortgage of any remedy on the underlying debt against the principal debtor and, for instance, have reached the conclusion that wrongful interference with such security interest entitles the creditor vis-à-vis the wrongdoer to full recovery of the amount covered by the security.

2. Elements of the Bar of Section 580b in Cases of Deeds of Trust and Mortgages: (b) "Purchase-Money" Security

Code of Civil Procedure section 580b raises the bar against deficiency judgments only in cases of purchase-money security. Hence the question arises as to what constitutes a purchase-money mortgage or deed of trust within the meaning of section 580b. Candor requires the admission that the existing state of judicial authority, in view of seemingly conflicting results of some decisions and inconsistent or unguarded language in others, does not permit of a ready and assured answer.

In Brown v. Jensen Mr. Justice Carter stated that section 580b "deals with a special type of security transaction, a trust deed, given to secure

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to the vendor of property the purchase price agreed to be paid by the vendee. According to the vendor, mortgages or deeds of trust securing parties other than the vendor do not come within the purview of that section, regardless of their participation in the closing of the deal, and that, for instance, a mortgage or deed of trust given by the vendee of real estate on that property to a third party to secure repayment of a loan negotiated to procure the cash needed for the acquisition of the premises is not a purchase-money security within the meaning of section 580b. It must be noted, however, that for other purposes, especially in determining priorities between liens, the California courts have extended the notion of purchase-money mortgages so as to include mortgages executed to third parties to secure the repayment of loans obtained and used for the express purpose of acquiring certain property. The problem thus boils down to the issue whether the policies enshrined in section 580b are such that the phrase 'deed of trust or mortgage given to secure payment of the balance of the purchase price' as employed in that section requires an interpretation different from that accepted in connection with other situations, e.g., those envisaged by California Civil Code section 2898 (which confers special priority to purchase-money mortgages and deeds of trust). As indicated, the unsatisfactory state of the pertinent case law necessitates a careful canvassing of all available judicial opinion with due regard for chronological order.

Banta v. Rosasco was the first case in which the question 'what is a purchase-money mortgage within the meaning of Code of Civil Procedure Section 580b' had to be faced by an appellate court. The decision involved the liability of an assuming grantee for a deficiency where the original mortgage was not given as a part of the purchase price. The court held that Code of Civil Procedure section 580b was not a defense in such situation. It reached this result, however, for the reason that the mortgage in question was not "given" as purchase-money security and did not discuss the broader and different question whether a purchase-money mortgage within the meaning of section 580b could ever be executed to a person other than the vendor of the land.

Peterson v. Wilson contains the strongest expression supporting the
view that purchase-money mortgages and deeds of trust as envisaged by Code of Civil Procedure section 580b do not include security interests executed to third parties as part of their financing or refinancing the acquisition of the premises by the grantor. The case involved the status of a deed of trust of $186,000 executed to a bank in conjunction with the purchase of three apartment buildings. Before the purchase, the buildings stood in the name of a realty corporation and were encumbered by a "good-sized" deed of trust to the bank and a second mortgage to another party. Both encumbrances were released as a result of the refinancing. Subsequently the premises were transferred to the sister of the original purchaser and, in connection with that grant, she assumed the indebtedness secured by the deed of trust in issue. One of the litigants argued that this assumption did not constitute fair consideration because the trust deed in question was one securing purchase money and therefore left no indebtedness to be assumed and that, accordingly, the transfer was fraudulent as against, and voidable by, creditors of the transferor. The court rejected this contention on the ground that "the deed of trust here was not a purchase-money one." It relied upon, and quoted at length from, Ladd & Tilton Bank v. Mitchell, a case in Oregon involving a statute very similar to Code of Civil Procedure section 580b, in which the supreme court of that state had held that the legislation had the object of encouraging and protecting the purchase of real estate "which perchance is made for the purpose of obtaining a home," and that a construction which would include a third party, not the vendor, who supplies the funds used in the acquisition would only hamper prospective purchasers in obtaining loans and thus thwart the beneficial intent of the statute.

There are good reasons, however, for questioning whether Peterson v. Wilson continues to possess vitality as a precedent on the issue under discussion. Although the decision has never been explicitly overruled or disapproved in that respect, language and reasoning in other, especially more recent, cases seem to have shaken if not destroyed its authority. In Stockton Sav. & Loan Bank v. Massanet, which was decided prior to the Peterson case, the buyer of real property obtained a loan from a bank in order to discharge a pre-existing encumbrance as a part of the purchase arrangements and secured that loan by a deed of trust. Subsequently the buyer defaulted under the deed of trust and entered into an agreement whereby the property was conveyed to the bank and from the bank to a new purchaser. The latter executed a note to the bank for an amount equal to that

35 93 Ore. 668, 184 Pac. 282 (1919).
36 Peterson v. Wilson, supra note 34, was expressly disapproved on a different point in Freedland v. Greco, 45 Cal. 2d 462, 466, 289 P.2d 463, 465 (1955).
37 18 Cal. 2d 200, 114 P.2d 592 (1941).
owed by the original buyer, securing the same by a first deed of trust on the property, and another note for an additional amount to the original buyer, securing it by a second deed of trust on the property. Subsequently the bank sought a deficiency judgment on the new note. The court held that such relief was barred by section 580b. It rested this decision on the narrow ground that under the facts the bank had held record title and therefore was technically the vendor. Significantly, however, Justice Carter included in his opinion a discussion of the result which would follow if the original buyer and not the bank were to be considered the true vendor:

Even if it be accepted that [the original buyer] ... and not [the bank] ... was the vendor of the property, the fact remains that the trust deed and note were not merely a renewal or continuation of the note and trust deed owed by [the original buyer] ... because the latter was released and eliminated when [the original buyer] ... conveyed to [the bank] ... and [the bank] ... released [the original buyer] ... from liability thereunder ... The sum represented by the note and trust deed was a necessary part of the purchase price.  

Accordingly, the opinion considers it at least arguable that a mortgage or deed of trust executed to a third party as a necessary part of the purchase arrangements may be a purchase-money security within the meaning of section 580b. On the other hand, the opinion intimated that the mere assumption by the vendee of a pre-existing non-purchase-money encumbrance, even though made as part of the purchase price, would not convert the encumbrance into purchase-money security vis-à-vis the assuming vendee. Curiously, however, the opinion omitted any reference to Banta v. Rosasco.

Moreover, the language from Brown v. Jensen quoted above, which appears to sustain the thesis that a purchase-money mortgage or deed of trust within the meaning of section 580b is restricted to an encumbrance given to secure the vendor, must not receive undue emphasis by being read out of the context of other portions of the opinion. In that case the deed of trust in favor of the vendor was subject to a first deed of trust for the benefit of a savings and loan association securing a note executed as a part of the purchase price. In stating the facts Justice Carter summed them up with the observation: "Hence both trust deeds were purchase money trust deeds." 

The recent decision of Algeri v. Tonini lends further support to the view that the bar of section 580b includes a mortgage or trust deed executed by a vendee to a person other than the vendor as security for a loan of all

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88 Id. at 208, 114 P.2d at 597.
89 Supra text at note 29.
or a part of the purchase price, provided the lender intended such use of the money. In that case the plaintiff sought judicial foreclosure of a deed of trust and judgment for a possible deficiency. The property in question was acquired with the loan secured by the deed of trust sought to be foreclosed. The sole defense raised in the pleadings and at the trial was that the transaction was a joint venture rather than a loan. Only on appeal was the defense of section 580b interposed. The court of appeal affirmed the deficiency judgment on the ground that the evidence did not establish, as a matter of law, that the deed of trust was one for purchase-money:

The evidence does not compel a finding that the money was loaned ... for the express purpose of buying this specific property, and the cases do not hold that a transaction as described by respondent necessarily involves a purchase money deed of trust or mortgage.\(^{42}\)

For the sake of completeness it may be added that in *Lucky Investments, Inc. v. Adams*\(^{48}\) the court accepted a distinction between purchase-money and construction-money first deeds of trust with reference to security executed by the vendee for the benefit of an outside lender in connection with the acquisition, although the court recognized that the differentiation had no effect upon the applicability of section 580b to a subsequent purchase-money deed of trust taken by the vendor.

Accordingly, there seems to be mounting judicial support for the thesis that the prohibition of section 580b extends to mortgages and deeds of trust securing loans given by third party lenders for the express purpose of supplying all or a part of the purchase price. Certainly, the policy reason offered by *Peterson v. Wilson* for the opposite view is quite specious.\(^{44}\)

The courts have placed particular emphasis upon the rule that the question of whether a mortgage or deed of trust is one for purchase money within the meaning of section 580b must be determined as of the date of its execution.\(^{45}\) A subsequent renewal will not alter its character in that

\(^{42}\) Id. at 832, 324 P.2d at 727. (Emphasis added.)

\(^{43}\) 183 A.C.A. 463, 7 Cal. Rptr. 57 (1960).

\(^{44}\) Currie and Lieberman, in their recent article, "Purchase-Money Mortgages and State Lines: A Study in Conflict of Law Method," *supra* note 1, have endorsed the view that the statutes barring deficiency judgments for purchase-money mortgages and trust deeds operate only against vendor financing. But, after a painstaking though fruitless search for a cogent economic justification for this restriction, they arrive at their result on the tenuous ground that the legislatures in all likelihood did not have mental images of purchase-money mortgages that included the commercial financing of property acquisitions. Currie and Lieberman's careful study reveals that it is well-nigh impossible to ascertain a clearly defined statutory policy and that in the absence of clarification by the legislatures the courts must make the somewhat arbitrary choice of whether the vendee or the third-party financier should bear the risk of misjudgments, at the time of the real estate acquisition, as to present or future property values.

respect. Vice versa, a mortgage or deed of trust that is not purchase-money security in its origin will not be converted into such upon the mere assumption thereof as part of the purchase price by a subsequent buyer of the premises, at any rate not as between the holder of the security interest and the assuming grantee.

3. Elements of the Bar of Section 580b in Cases of Purchase-Money Deeds of Trust and Mortgages: (c) No Deficiency Judgment

The bar of section 580b applies only against deficiency judgments, i.e., judgments for the enforcement of the obligations flowing from the contract of sale. For example, a judgment dissolving a preliminary injunction against a private sale under a purchase-money deed of trust and decreeing that the sale proceed is not a deficiency judgment.

To be sure, there is language in several cases to the effect that “for a purchase-money mortgage or deed of trust the security alone can be looked to for recovery of the debt,” but it is now well settled that section 580b does not prohibit the vendor’s taking additional security for the purchase money on other property, whether owned by the vendee or third persons, and enforcing such security by judicial proceedings, as well as by sale under a power, whenever such action is called for. In Mortgage Guarantee Co. v. Sampsel the court enforced an assignment of rents which was agreed upon as additional security in a clause contained in a purchase-money deed of trust and which was to take effect upon any breach or default. It was held that the judgment appointing a receiver for the collection of rents and ordering the payment of the money collected to the beneficiary was not a “deficiency judgment in the sense in which it is used in section 580b.” The supreme court expressly endorsed and followed this holding in Freedland v. Greco. In that case a decree foreclosing a chattel mortgage and granting a judgment for the deficiency following foreclosure of a deed of trust securing the same indebtedness was affirmed as to the portion ordering the sale of the chattels and reversed as to the portion ordering the deficiency payment. While the decision actually construed and applied Code of Civil Procedure section 580d, the opinion made it abundantly clear that the same principles also governed under Code of Civil Procedure section 580b. Analogous rules had been laid down previously with respect to Code of

46 Lucky Investments, Inc. v. Adams, supra note 45.
51 A dictum to the contrary in Peterson v. Wilson, 88 Cal. App. 2d 617, 199 P.2d 757 (1948), was expressly disapproved, id. at 466, 289 P.2d at 465.
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Civil Procedure section 580a. Thus, in this respect, the three anti-deficiency sections have had a uniform construction.

Of course, where the chattel mortgage and the real estate mortgage or deed of trust secure different obligations no question arises as to the possibility of a deficiency judgment on the indebtedness secured by the chattel mortgage. The only pertinent restriction is limited to the special situation regulated by the second paragraph of section 580b, i.e., the case in which a real estate mortgage or deed of trust and a chattel mortgage secure payment of the combined purchase price of both real and personal property.

There remains the question whether the rule that the anti-deficiency legislation does not bar resort to additional security also applies to cases in which the additional security is not a security interest in specific property but consists of the personal obligation of another party as surety, endorser, or co-maker. Since the answer to that question may depend upon the possibility of a waiver of the benefits of section 580b, consideration of the problem will be deferred until the permissibility of a waiver has been discussed.

4. Permissibility of Waiver

Civil Code section 2953 vitiates any express agreement made or entered into by a borrower at the time of or in connection with the making of or renewing of any loan secured by a deed of trust, mortgage or other instrument creating a lien on real property, whereby the borrower agrees to waive the rights, or privileges conferred upon him by sections 2924, 2924b, 2924c of the Civil Code or by sections 580a or 726 of the Code of Civil Procedure . . . .

The pointed omission in this catalogue (which was adopted in 1937 and, after a radical change in 1939, was again cast in the present mold in 1941) of any reference to sections 580b and 580d has given room to speculation as to the effects of an attempted waiver of the benefits of these sections.

Theoretically, three different views are conceivable: (1) the omission of Code of Civil Procedure sections 580b and 580d from the catalogue of Civil Code section 2953 implies that a waiver is always effective, whether made in conjunction with the making or renewing of a loan, or subsequently; (2) the omission implies that such waiver is never effective, whether made in conjunction with the making or renewing of a loan, or subsequently; and (3) the omission has no implications and the principles of

Civil Code section 2953 apply also to waivers of Code of Civil Procedure sections 580b and 580d. Actually, the courts have indicated by strong dicta that a waiver of the benefits of section 580b cannot be made in advance at the time of execution of the mortgage or deed of trust. Accordingly, the only real question is whether the policies of Code of Civil Procedure sections 580b and 580d are so cogent that not even a subsequent waiver is permissible. Apparently no support for such an argument can be found in the case law. Conversely, much can be said in favor of the position that the general principles under which subsequent waivers of the other sections specified in Civil Code section 2953 are upheld also govern waivers of Code of Civil Procedure sections 580b and 580d. Needless to say, the waiver must be agreed upon by the mortgagor or trustor, and the mortgagee, trustee, or beneficiary cannot unilaterally waive his security in order to escape the bar of sections 580b or 580d.

5. Applicability of the Bar of Section 580b to Parties Severally Liable with the Vendee

As pointed out above (part II (B) 3), there remains the question whether the bar of Code of Civil Procedure section 580b inures to the benefit of parties severally liable with the vendee, such as co-makers of his purchase-money notes or sureties or endorsers. Since section 580b does not prevent the vendor from obtaining additional property security (see part II (b) 3 supra), it cannot be said that there is a clear-cut policy against additional personal security in the form of personal liability for the balance by parties other than the vendee; the matter requires further analysis.

On one hand, it was held in Stephenson v. Lawn that the endorser of a purchase-money note secured by a deed of trust may not plead the bar of section 580b as a defense. To appraise the force of this precedent correctly, however, attention must be given to the facts that in that case the endorsement was subsequent to and independent of the purchase transaction and that the endorser was the vendor himself. On the other hand, there is authority to the effect that the co-signer of purchase-money notes secured by a deed of trust on the property acquired does not suffer a detriment because section 580b shields him from liability on the notes. But in

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the cases applying this latter principle, the co-signer of the notes also took title to the property as joint tenant and co-signed the deed of trust and hence technically appeared as vendee vis-à-vis the vendor. Accordingly, this line of authority is not necessarily conclusive with respect to the general situation in which a person, not technically a vendee, adds his signature as co-maker, endorser, or surety to the purchase-money notes at the time of purchase.

In addition, there is a line of cases holding that the anti-deficiency legislation (in the particular instances, Code of Civil Procedure section 580a) does not protect a guarantor against liability for the full amount left unpaid after foreclosure.61 Again, however, these decisions may not be relied upon as they represent the law prior to the statutory abolition of the distinction between sureties and guarantors in 1939.62 Moreover, Everts v. Matteson, in fact, contains a passage intimating that a surety might benefit from the anti-deficiency provisions.

As a surety usually has redress against the principal obligor, the courts must choose among three possible solutions to the problem: (1) the surety incurs no liability on his undertaking vis-à-vis the promisee if the principal obligation is one for purchase money secured by a mortgage or deed of trust; (2) the surety incurs personal liability vis-à-vis the promisee but has no redress against the vendee; and (3) the surety incurs personal liability and may obtain reimbursement from the vendee. Obviously, the third solution would lend itself to a complete circumvention of section 580b and therefore should be discarded. As follows from the prior discussion the understanding between the vendee and his co-signer could not be upheld as a valid waiver. The decision between the first and second propositions, however, is by no means obvious and involves a difficult balance of policies. Apparently the courts evince an inarticulate preference for the first approach.63

6. Applicability of the Bar of Section 580b to Holders in Due Course of Purchase-Money Notes

Another perplexing problem is the effect of the anti-deficiency legislation, Code of Civil Procedure section 580b in particular, on the law of nego-

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63 In McKnight v. United States, 259 F.2d 540 (9th Cir. 1958), it was held that Cal. Code Civ. Proc. § 580b did not protect a veteran from being obliged to indemnify the Veterans' Administration after it had been compelled to satisfy the vendor under a Loan Guaranty Certificate. The result was rested on the supremacy of the federal law requiring such indemnity. But see United States v. Shimer, 276 F.2d 790 (3d Cir. 1960), which seems to misunderstand the import of the McKnight case.
tiable instruments. Is a party to whom the secured payee negotiates the vendee's purchase-money notes before maturity without informing him that they are secured and represent purchase money subject to the defense of section 580b? There is California authority to the effect that the principles of negotiability override the operation of the recording acts as those acts relate to mortgages and deeds of trust. It is doubtful, however, whether the courts will extend this policy to the clash between the protection accorded a purchaser of real estate and that given to commerce in negotiable instruments. Such a result might appear too conducive to an easy circumvention of the social objectives of section 580b to be palatable to the courts.

C. Land Contracts as a Bar to Deficiency Judgments

1. Rationale of, and Types of Land Contracts Envisaged by, Section 580b

An amendment of 1935 extended the principles of Code of Civil Procedure section 580b to land contracts and prohibited deficiency judgments after "any sale or real property for failure of the purchaser to complete his contract of sale." This expansion of section 580b to include land contracts in addition to purchase-money mortgages and deeds of trust was dictated by the appreciation that land contracts which provide for deferred payment or payments of the purchase price, and which postpone the duty to convey until a part or the whole of the purchase price has been paid, in effect transform the vendor's title into a security interest for purchase money. Hence it appeared only fair and equitable to place all purchase-money security on an equal footing.

In view of the basic policy underlying the amendment of 1935, the courts have drawn the conclusion that section 580b applies only to contracts of sale in which credit is involved and does not apply to sales for cash. In Kerrigan v. Maloo a referee in partition brought an action under Code of Civil Procedure section 785 against a defaulting bidder to recover the difference between the sale price as bid by the defendant and the price obtained on a second partition sale. The court held that section 580b furnished no defense to this action as that section aimed only at private credit sales and was not meant to apply to judicial cash sales. In Goldsworthy v. Dobbins an action was brought by the vendor of certain real estate to compel the vendee to perform the contract of sale. The con-
tract stipulated, *inter alia*, that the purchase price was to be paid in part with cash and in part by the assumption of a first deed of trust and the execution of a second deed of trust to a third party in lieu of a pre-existing second trust deed which was to be reduced in amount. In addition, it was agreed that the vendor should make the monthly payments on the first deed of trust falling due during the escrow and that the vendee should add equivalent amounts to his cash payment. The vendee defaulted and the vendor brought action for specific performance. The trial court rendered an interlocutory decree for specific performance ordering that within fifteen days the vendee make the payments specified in the escrow instructions and that upon such payments the vendor's conveyance be delivered. It was further ordered that in the event the vendee failed to comply, final judgment should be entered for the amounts specified. No timely compliance was had and final judgment was rendered directing the vendee to pay the stipulated amounts and ordering a conveyance upon such payment. The vendee appealed from the decree and argued, among other contentions, that section 580b barred decrees of specific performance for payment of the purchase price against a vendee of real property and that under the final judgment as rendered the vendor might have execution levied on the land and thus end up with a deficiency judgment in violation of the statutory mandate.

The district court of appeal rejected this argument and held that Code of Civil Procedure section 580b does not deprive the vendor of his well-established right to specific performance of a valid contract of sale and that this section, in any event, is not applicable to cash sales. While the general statement with respect to the effect of section 580b on the vendor's right to specific performance certainly overshoots the mark, the limitation of its applicability to credit sales may well become accepted doctrine.

2. Effect of the Bar of Section 580b on the Enforcement of Land Contracts Covered Thereby

Code of Civil Procedure section 580b prohibits deficiency judgments "after any sale of real property for failure of the purchaser to complete his contract of sale." The doctrine of *Brown v. Jensen*, although strictly applicable only to purchase-money mortgages and deeds of trust, calls for caution in not placing too much reliance upon the requirement of a previous sale in connection with the limitation on the vendor's rights under a land contract where he has relied upon his title as his principal security. It is not unlikely that the courts will come to apply the bar of section 580b even in cases of foreclosure without sale by means of quiet title actions. Generally speaking, all the principles governing the applicability of section 580b in

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70 41 Cal. 2d 193, 259 P.2d 425 (1953), discussed supra text following note 25.
the case of purchase-money mortgages and deeds of trust control similarly in the case of land contracts serving as purchase-money security.

A deficiency judgment within the meaning of section 580b as applied to the enforcement of a land contract is a judgment for the balance of the purchase price or for damages flowing from the nonperformance of the contract of sale remaining after the seller has relied upon his title to make himself whole. A money judgment for damages resulting from fraud of the vendee in the conclusion of the contract is not a deficiency judgment as envisaged by that section.

On principle, a vendor's remedies for specific performance or for damages flowing from a breach are, in the case of a land contract stipulating for a credit sale, subject to the limitations of section 580b and the courts are opposed to condoning any circumvention of its policy. Accordingly, it is most improbable that any judgment will be upheld which permits execution against assets of the vendee other than the real property sold, regardless of the theory of relief relied upon. A vendor may seek to recover the unpaid portion of the purchase price at law or in equity; the courts, however, will only decree a sale of the property which was the subject of the land contract and, if opposite, in the case of money judgments will permanently stay execution against any other assets of the vendee except the real estate sold, if and when conveyed by the vendor.

III

FORECLOSURE BY EXERCISE OF A POWER OF SALE AS A BAR TO A DEFICIENCY JUDGMENT

A. Reach of Code of Civil Procedure Section 580d Within the Anti-Deficiency Legislation

Until 1939, foreclosure of mortgages or deeds of trust securing obligations other than for purchase money did not bar resort to the courts to

71 If § 580b be held to apply to the foreclosure of land contracts without sale by means of quiet title decrees the further question arises whether such conclusion precludes a vendor who has terminated his contract in such fashion and has regained clear title from recovering the rental value of the property for the period during which the vendee was in possession after default. As a matter of consistency the answer should be in the affirmative, although recent cases, in effect, have failed to reach such result, Luz v. Lopez, 182 A.C.A. 900, 6 Cal. Rptr. 540 (1960). See the criticism by Professor John R. Hetland, infra at p. 729.

72 See the general discussion of the right of action for damages for fraud with respect to contracts for sale of real estate in Garret v. Perry, 53 Cal. 2d 178, 346 P.2d 758 (1959), dealing with a case of fraud by the seller.


74 Suggestions to the contrary by some law review note writers are totally unfounded.

75 If the judgment is in the form of a money judgment and an abstract thereof recorded prior to the conveyance, the seller will have a lien upon the conveyance (Cal. Code Civ. Proc. § 674) and will thereby be protected against the possibility of an intervening disposition by the vendee.
obtain a judgment for the deficiency. The amount of any such judgment, however, was limited to the difference between the amount of the indebtedness and the fair market value of the property sold on foreclosure at the time of such sale. Code of Civil Procedure section 726 so specified for the case of foreclosure by action, while Code of Civil Procedure section 580a reiterated that limitation for the case of foreclosure under a power of sale. In 1939 the legislature added a section, subsequently numbered Code of Civil Procedure section 580d,\(^7\) which raises a complete bar to a deficiency judgment “upon a note secured by a deed of trust or mortgage upon real property hereafter executed, in any case in which the real property has been sold by the mortgagor [the 1939 statute, by mistake, read mortgagee] or trustee under power of sale contained in such mortgage or deed of trust.” In other words, foreclosure by exercise of the power of sale will bar a deficiency judgment even in cases of ordinary, \(i.e.,\) not purchase-money, mortgages or deeds of trust, except those excluded from the regime of section 580d.

Code of Civil Procedure section 580d in its present form makes two qualifications as to the mortgages or deeds of trust to which it applies. In the first place, the instrument must be executed after the effective date of the act, \(i.e.,\) after September 19, 1939, or March 6, 1941, respectively.\(^7\) Secondly, the section by its terms extends only to actions “upon a note.” Hence mortgages or deeds of trust securing obligations not embodied in a note do not fall within the purview of that provision. In *Freedland v. Greco*\(^7\) the court, by way of a dictum, commented upon the meaning of “note” as used in section 580d without coming to a definite conclusion. The court was confronted with a situation in which a creditor had taken two notes, both for the full amount of the same debt, one of the notes being secured by a chattel mortgage and the other by a deed of trust on real property owned by the debtor. In denying a deficiency judgment following the foreclosure of the deed of trust under the power of sale and of the chattel mortgage by action, the court stated:

> While other sections of the Code of Civil Procedure which deal with deficiency judgments (Code Civ. Proc. §§ 726, 580a, 580b) refer to “debts,” “obligations,” or “contracts” secured by a trust deed [and] may be [employing terms] broader than the word “note” used in section 580b, the fact remains that here we have a note and in order to avoid thwarting the purpose of section 580d by a subterfuge, we must construe that section as embracing a situation such as we have here.\(^7\)

\(^7\)See *supra* text at notes 12 and 13.\(^7\) The two dates in the text are given because of the legislative history of the section, see *supra* text at notes 11 and 12. For an application of this qualification, see *Liebenguth v. Priester*, 64 Cal. App. 2d 343, 148 P.2d 893 (1944).\(^7\) 45 Cal. 2d 462, 289 P.2d 463 (1955).\(^7\) *Id.* at 468, 289 P.2d at 466. The statement quoted was relied upon in *Willys of Marin Co. v. Pierce*, 140 Cal. App. 2d 826, 296 P.2d 25 (1956), holding that a deed of trust given to
In addition, section 580d applies only to mortgages or deeds of trust on real property, that term including incorporeal hereditaments in gross, such as royalty interests in oil rights. Whether a deed subject to a holding agreement for the account of certain creditors constitutes a mortgage within the the purview of section 580d or an assignment for the benefit of creditors depends upon the objective of the parties in the light of the circumstances of the transaction. Needless to say that where an absolute deed is executed as security and therefore creates only a mortgage within the meaning and limits of California Civil Code sections 2925 and 2950, the rights of the mortgagee are subject to the limitations of the anti-deficiency legislation.

B. Other Elements of the Bar of Code of Civil Procedure Section 580d

The prohibition of Code of Civil Procedure section 580d applies only in the instances in which the real property has been sold by the mortgagee or trustee to secure the note upon which the suit is brought. In contrast to the principle laid down by Brown v. Jensen for purchase-money mortgages or deeds of trust, section 580d seems to require that there have been an actual sale by the mortgagee or trustee under the power, and to exclude situations in which the security is exhausted in some other fashion.

Section 580d outlaws only deficiency judgments on notes. It does not proscribe other judgments, such as judgments for the foreclosure of other security interests or the assertion of rights vis-à-vis other lien claimants or a judgment for restitution of leased premises in an unlawful detainer action brought upon default of the tenant.

Like section 580b, section 580d may not be waived in advance, although a subsequent waiver may be permissible. Section 580d furnishes no defense to a subsequent endorser of a note but apparently inures to the benefit of a surety or accommodation co-maker who assumes such position at the execution of the note. An assuming grantee may likewise rely secure an obligation to pay rent stipulated in a lease was not a trust deed securing a note within the meaning of § 580d and stating that “it seems obvious that section 580d does not apply to obligations other than promissory notes.”

81 Jensen v. Friedman, 79 Cal. App. 2d 494, 179 P.2d 855 (1947) (applying § 580c as existing in 1940, i.e., the short-lived precursor of the present § 580d).
82 41 Cal.2d 193, 259 P.2d 425 (1953).
84 Willys of Main Co. v. Pierce, supra note 79. The court discussed the point only with reference to § 580a, but the same rule should apply in respect to § 580d. The court disposed of the applicability of § 580d on other grounds, see supra note 79.
85 Freedland v. Greco, supra note 78; cf. Morello v. Metzenbaum, supra note 80.
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upon that section as a defense in a suit upon the assumption agreement brought by the mortgagee or beneficiary under the deed of trust.87

IV

LIMITATION ON DEFICIENCY JUDGMENTS IMPOSED BY CODE OF CIVIL PROCEDURE SECTIONS 580a AND 726

A. Cases Covered by Sections 580a and 726

While in the cases falling within their purview Code of Civil Procedure sections 580b and 580d raise a complete bar to a deficiency judgment, the bite of Code of Civil Procedure sections 580a and 726 is much less penetrating. In the cases covered by them, these latter sections merely limit the amount of the deficiency judgment to the difference between the amount of the indebtedness and the fair market value of the real property at the time of the sale.88

The applicability of the limiting clauses of section 726 in cases of realty is superseded only by section 580d and, therefore, these clauses govern the foreclosure by action of all mortgages and deeds of trust89 securing obligations other than for purchase money, at least when such instruments are executed after the effective date of section 726, i.e., August 21, 1933.90

The remaining area that is subject to the limiting clauses of section 580a is more difficult to circumscribe, as it is curtailed not only by section 580b but also by section 580d and, in addition, by language contained in the section itself and by the implied bar against retroactivity. Certainly section 580a is inapplicable (1) in the cases falling under section 580b, i.e., the cases involving recovery of purchase money secured by mortgages or

87 Everts v. Matteson, 21 Cal. 2d 437, 132 P.2d 476 (1942) (holding pertaining to § 580a but on grounds applicable also to § 580d).

88 In addition to this substantive limitation on the amount of deficiency judgments, §§ 580a and 726 both contain a procedural restriction as to the time within which proceedings for deficiencies may be instituted. Section 580a limits the period within which an action for a deficiency judgment may be brought following an extra-judicial sale to three months from the time of sale. Section 726 limits the time for an application for such a judgment in a judicial foreclosure to three months from the date of sale. The courts have differentiated between substantive and procedural limitations in the question of retroactivity and have held that the three-month provision is applicable to mortgages and deeds of trust antedating the effective date of CAL. CODE Civ. Proc. § 580a, i.e., August 21, 1933, if the sale takes place after that date, Ware v. Heller, 63 Cal. App. 2d 817, 148 P.2d 410 (1944). It has been held, however, that the three-month limitation does not apply if the sale occurred prior to that date. Slemons v. Patterson, 14 Cal. 2d 612, 96 P.2d 125 (1939); Christina v. Hightower, 22 Cal. App. 2d 339, 70 P.2d 988 (1937); Security-First Nat'l Bank v. Sapkin, 19 Cal. App. 2d 224, 64 P.2d 1097 (1937); Maryland Casualty Co. v. Nottingham, 18 Cal. App. 2d 135, 63 P.2d 854 (1936) (relating to foreclosure sales outside California).

89 The application to trust deeds follows from § 725a.

90 See text at note 19 supra for the applicability of the limitations of § 726 to pre-existing trust deeds.
deeds of trust on realty, and (2) in the cases falling under section 580d, *i.e.*, the cases of foreclosure by the exercise of a power of sale of non-purchase-money mortgages or deeds of trust securing "notes" when such instruments were executed after September 19, 1939, or March 6, 1941, respectively. Positively stated, section 580a still governs in the cases of foreclosure by exercise of a power of sale of non-purchase-money mortgages or deeds of trust when such security instruments either antedate the effective dates of the short-lived section 580c and of section 580d or do not secure "notes."

It might be thought that section 580a comes into play when a non-purchase-money mortgage or deed of trust securing a note and executed after September 19, 1939, and March 6, 1941, is not foreclosed but is exhausted for some other reason. However, it seems very unlikely that the doctrine of *Brown v. Jensen*⁹¹ will thus be made to spill over into the field of section 580a, not the least in view of the more precise language found in that section which limits deficiency judgments "following the exercise of the power of sale in such deed of trust or mortgage." Moreover, section 580a limits deficiency judgments to the excess of the entire amount of the indebtedness over the fair market value *at the time of sale* and expressly authorizes deficiency judgments without sale where "such real property or interest therein has become valueless." Of course, rejection of such a forced construction means that there still remains the possibility of an unlimited recovery of an erstwhile secured indebtedness in all cases in which the obligation is not for purchase money and in which the security has been exhausted without foreclosure.

### B. Scope of the Limitation on Deficiency Judgments Governed by Code of Civil Procedure Sections 580a and 726

Little needs to be added about the general scope of the limitations specified by Code of Civil Procedure sections 580a and 726 as to the amount of deficiency judgments. Most of the principles discussed throughout this article apply also in the cases governed by these sections. Thus, the conditions and limitations restricting the amount of possible deficiency judgments do not control actions for possessory relief⁹² or the enforcement of other property security, whether given by the principal debtor or third parties.⁹³ The protection shields an assuming grantee⁹⁴ and apparently may be invoked by sureties and other parties secondarily liable.⁹⁵ Civil Code section 2953 expressly invalidates waivers of the benefits conferred by sec-

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tions 580a and 726, if agreed upon at the time of, or in connection with, the making or renewing of a loan secured by a mortgage or deed of trust on real property, thereby apparently permitting subsequent waivers.96

The amount of the permissible deficiency judgment depends on the fair market value of the real property at the time of sale. Code of Civil Procedure sections 580a and 726 specify certain formalities as to the proving of such value. The courts have insisted on faithful observance of these requirements.97 Of course, in no event may the amount of the judgment exceed the actual deficiency, i.e., the difference between the indebtedness and the price for which the property was sold. Sections 580a and 726 spell this out specifically ex abudante cautela.

CONCLUSION

The foregoing discussion has endeavored to outline the scope and effect of the existing California statutes limiting deficiency judgments and has focused upon the many perplexing uncertainties and doubts engendered by this legislation. The question of the applicability of the bar of section 580b to mortgages and trust deeds securing non-vendor-financed acquisitions, of its thrust vis-à-vis holders in due course, and of its operation in cases of strict foreclosure of land contracts prompt perhaps the most vexing quandaries. Of course, courts must decide cases before them no matter how impossible it appears to extrapolate a dimly conceived or obscurely defined legislative policy to the controversy at hand. In such conditions courts must ultimately rely on policy judgments of their own, though their preferences must remain consistent with the blurred contours of the legislative mandate.

Are there, then, any rational grounds for a differentiation between vendor and third party financing of acquisitions? Certainly the reasons spelled out by Justice Carter in Brown v. Jensen as underlying the bar against deficiency judgments in the case of purchase money trust deeds appear fabricated and specious and apply just as much to lending company-financing of acquisitions as to vendor-financing thereof. It is hard to perceive why a vendor “knows the value of his security” better than the skilled personnel of a lending institution. Even less valid is the assumption that a vendor means to rely only upon the security and “assumes the risk that it may become worthless” while a lending institution does not do so. Hence,

96 In California Bank v. Stimson, 89 Cal. App. 2d 552, 201 P.2d 39 (1949), the court held that the three-month limitation respecting applications or actions for deficiency judgments was a rule of public policy and therefore not subject to waiver. No differentiation between waivers at the time of the execution of the instruments and subsequent waivers was made. Actually, the waiver before the court was contained in the trust deed and antedated the passage of Cal. Civ. Code § 2953, which provision was not considered by the court. It would seem that subsequent waivers of the benefits of § 580a, including that of the three-month limitation are now permissible, subject, of course, to the restriction of Cal. Code Civ. Proc. § 360.5.

unless it all boils down to the cause that lending institutions are able to marshal a lobby while vendors as a class are not, some other ground must be found to justify such discrimination. The main factor which rationally could be relied upon for that purpose is the proposition that vendors have the last word on the price for which they are willing to part with the property and, therefore, should be burdened with a risk from which mere financiers remain free. It is, however, painful to determine whether this difference in influence on the terms of the bargain justifies so drastic a discrimination in the resulting rights.8

Similar hard choices confront the courts in passing upon the applicability and effects of section 580b to strict foreclosures of land contracts. There appears to be no legitimate reason for distinguishing between foreclosure by sale and strict foreclosure in these situations. On the other hand, once section 580b is deemed to operate without a sale the vendor seems to be restricted exclusively to regaining title and possession of the land regardless how long the defaulting vendee enjoyed the free possession and profits of the land.

It seems to be socially undesirable that the legislature should leave the courts saddled with the determination of policy questions that depend upon such elusive economic factors and preferences. It would be much sounder if the legislature would recanvass the whole field of anti-deficiency legislation and itself make the choices deemed to be appropriate. In doing so, a full inquiry into existing practices of lending institutions in taking deficiency judgments might furnish valuable insights.9

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8 Among the other three jurisdictions which prohibit deficiency judgments in the cases where the purchase price of land is secured by an interest in such land, Montana seems to be the only state where the governing statute expressly limits the bar to mortgages "executed to any vendor of real property or to his heirs, executors, administrators or assigns." Mont. Rev. Codes Ann. §§ 93-6008 (1947).

9 Although the practical utility of deficiency judgments is a much debated subject it is interesting to note that the legislature of North Dakota in 1951 felt compelled to re-establish the availability of limited deficiency judgments although they had been totally abolished in 1937, N.D. Laws 1951, ch. 217.