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Various forms of emergency statutory relief have been devised during the past few years to relieve the economic distress of debtors. One of the most common and popular devices is the legislation which, in the present emergency, has sought to limit the amounts of deficiency judgments following mortgage foreclosures. Not that the evil sought to be remedied exists only in time of emergency, but emergencies do expose to the spotlight certain economic malpractices, which, in more prosperous times, flourish unheeded.

At common law, a mortgage is usually mere collateral for the payment of some primary debt. If the mortgagor should default in paying the debt, the mortgagee might sue in personam upon the obligation. At his option, however, he might first resort to his security on the mortgage, causing a foreclosure and sheriff's sale of the mortgaged property. The amount realized from these proceedings, if any remain after paying the costs and taxes, would be credited toward the unpaid obligation, and a deficiency judgment would then be rendered in the mortgagee's favor for the balance.

The purchaser at the sheriff's sale might be a third person or the mortgagee himself, the property going to the highest bidder. Obviously, the mortgagee would normally not be content to permit a third person to purchase the property at a price far inferior to the market value, and so low as to leave the amount of the debt substantially undiminished. What is normal is, that, if a third person make a nominal or unsubstantial bid, the mortgagee will continue to bid up the property until the price reaches the amount of the debt, or his estimate of the then market value of the property, whichever is the lower. As a result, the mortgagee is, more often than not, the purchaser.

All too often, especially during depressions, when the stirring up of competitive bidding is impossible, the mortgagee, regardless of the market value of

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the property, bids for the property an amount equal to the costs and taxes only. The result is that the mortgagee gets a sheriff's deed to the property, and, in addition, since the amount of his bid was not large enough to extinguish any part of the debt, he gets a deficiency judgment for the identical amount of the original debt, a judgment through which he may seize any other property which the debtor may acquire in the future. In other words, the effect of the proceedings is, that the debtor forfeits the mortgaged property, for which he gets no credit, and remains as liable for the original debt as he ever was.

This plight of the mortgagors is not fanciful or theoretical. During the past few years, in Philadelphia alone, thousands upon thousands of mortgaged properties have been acquired by the mortgagees through a nominal bid of fifty dollars for costs. The removal of this hardship has been the aim of the Mortgage Deficiency Judgment Acts, which provide, in effect, that if the mortgagee seeks to appropriate the mortgaged property, he is bound to credit the mortgagor with the "fair value" of the property, which is determined through legal proceedings.

These statutes have been attacked as violating the "impairment of obligations" clause of the Federal Constitution. One of the most recent cases passing upon this constitutional question is *Beaver County Building & Loan Association v. Winowich et ux.*[1] The Pennsylvania Supreme Court, with only Justice Barnes dissenting,[2] held that the act was invalid, insofar as it affected mortgages entered into before the passage of the act.

It is well established that not all statutes which change preexisting contractual relations are violative of the "impairment of obligations" clause. The legalistic dogma has been devised, that, changes of remedy and form are permissible, but those of substance are not. That formula the majority opinion invokes, saying that "the change wrought by the Pennsylvania Mortgage Deficiency Judgment Act is one not merely of remedy but of substance."[3] Like most dogmas, this one making the formulistic distinction between remedy and substance confuses rather than aids the solution of problems. Constitutional lawyers know, for example, that the United States Supreme Court has held that a legislative enactment, reducing the period of a statute of limitations from twenty years to nine months, has been held not to impair the "obligations of contracts" clause, even though at the end of the nine months the obligee's cause of action was utterly destroyed.[4] Apart from the fact that such a statute

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[1]Beaver County Building & Loan Association v. Winowich et ux., 187 Atl. 481 (1936); the statute passed upon was the Act of Jan. 17, 1934 (Spec. Sess.) P.L. 243 (21 P.S., secs. 806 and note, 807).

[2]Id., 495.

[3]Id., 491.

[4]Terry v. Anderson, 95 U. S. 628 (1877).

is labeled as affecting merely the remedy, a clearer case of taking away substantial rights is hard to find.

The underlying factor which the United States Supreme Court seems to have stressed in cases involving alleged impairments of contracts, is the *reasonableness* of the statute which alters prior relationships. Thus, in *Home Building & Loan Association v. Blaisdell,* the court, recognizing the futility of the dogma distinguishing remedy from substance, said, quoting from prior decisions:

> "No attempt has been made to fix definitely the line between alterations of the remedy, which are to be deemed legitimate, and those which, under the form of modifying the remedy, impair substantial rights. Every case must be determined in its own circumstances. . . . In all such cases, the question becomes, therefore, one of reasonableness, and of that the legislature is primarily the judge."[5]

As a matter of fact, the majority opinion in the *Winowich* case itself casually refers to the test of reasonableness. It is perhaps high time that it be realized that the legalistic formula which distinguishes between remedy and substance at best is merely descriptive of the result which the court may see fit to reach, rather than the reason for reaching the result.

Likewise, the helpless inadequacy of broad generalizations should be recognized, such as, that

> "Any law which enlarges, abridges, or in any manner changes the intention of the parties, as evidenced by their contract, imposing conditions not expressed therein, or dispensing with the performance of those which are a part of it, impairs its obligation, whether the law affects the validity, construction, duration, or enforcement of the contract."[6]

The statute of limitations cases[7] clearly rebut the obvious implications of such a generalization.

It will be noted that in the *Winowich* case no express provision of the mortgage is alleged to have been impaired, but rather, that the common law under which the mortgagor forfeited his property was impaired. It is true that the United States Supreme Court has declared that the laws which were in force at the time of the making of the contract enter into its obligation with the same effect as though expressly incorporated in its terms.[8] However, a

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[5]290 U. S. 398, 430.

[6]187 Atl. 481, 485, citing Story's Commentaries on the Constitution; Bk. 3, ch. 34, sec. 1379.

[7]Terry v. Anderson, 95 U. S. 628 (1877).

[8]Walker v. Whitehead, 16 Wall. 314, 317; 21 L. Ed. 357; Edwards v. Kearzey, 96 U. S. 595, 852, 858 (1934).

literal construction of this proposition would be tantamount to freezing into the "impairment of obligations" clause the entire body of the common law. Such a view would raise difficult barriers before the government in any effort to attempt social or economic reform. As a result, a corollary proposition has been advanced by the United States Supreme Court, to the effect that the "police power" of a state is free from and paramount to the limitation of the "impairment of obligations" clause.[9]

Indeed, the majority opinion in the *Winowich* case concedes that, in the exercise of its "police power", a state may enact legislation which overrides that barrier.[10] However, the majority opinion denies that, "to reduce the obligations of debtors on judgments in personam" can "be said to be an exercise of the 'police power';" it denies that the concept of "police power" is broad enough to include this phase of the general welfare.[11] It is submitted that the majority has confined "police power" too narrowly. In *Home Building & Loan Association v. Blaisdell,* the court said:

> "The *economic* interests of the state may justify the exercise of its continuing and dominant protective power, notwithstanding interference with contract.[12] . . . . With a growing recognition of public needs and the relation of individual right to public security, the court has sought to prevent the perversion of the clause through its use as an instrument to throttle the capacity of the states to protect their fundamental interests."[13]

It is submitted, moreover, that mortgage deficiency judgment acts are analogous to and support the same social and economic policies as underlie usury statutes. In both cases, the objective is to prevent the creditor from profiting unreasonably at the expense of a helpless debtor. Yet it has been held that a statute that makes usurious contracts void and unenforcible does not impair the contractual rights of a creditor who entered into an usurious contract prior to the enactment of the statute.[14] How such a statute is more properly within the "police power" of a state than a mortgage deficiency judgment act is difficult to understand.

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[9]Home Building & Loan Association v. Blaisdell, 290 U. S. 398, 434, 435.

[10]187 Atl. 481, 494.

[11]Id., 494.

[12]290 U. S. 398, 437. Italics ours.

[13]Id., 444.

[14]Griffith v. Connecticut, 218 U. S. 563 (1910). Referred to in Nebbia v. New York, 291 U. S. 532, 535 (1933), for the proposition that usury laws fall within the "police power" of the state. See also Rowecamp et al. v. Mercantile-Commerce Bank & Trust Co. et al., 72 Fed. (2d.) 607; 24 L Ed. 793; Barnitz v. Beverly, 163 U. S. 118, 127; 41 L. Ed. 93.

Much is made by the majority of the argument that the statute "compels a mortgagee to accept real estate at an appraised value in place of money";[15] and that "the plaintiff (mortgagee) must be content with receiving only real estate and no lawful money whatever."[16] The source of such compulsion on the mortgagee is difficult to trace. The statute does not oblige the mortgagee to take the land. It merely provides, in effect, that if he chooses to proceed against the property, rather than upon the personal obligation of the debtor, he must account for the fair value of the property. In all such cases, the mortgagee voluntarily and affirmatively proceeds against the land. What the mortgagee complains of is not that he must proceed against the land, but only that the statute prevents him from perpetrating a heretofore legalized form of highway robbery from the mortgagor. He wants the land, but he still wants, as far as possible, to retain his personal claim against the debtor.

The majority further objects to the statute on the ground that "in the use of the term 'fair value' there is introduced an indefinite and to some extent meaningless standard, ... unless the phrase 'fair value' be held to be synonymous with fair market value."[17] Yet, it has been held that, in fixing public utility rates, "the basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a highway under legislative sanction must be the *fair value* of the property being used by it for the convenience of the public."[18] So too, in eminent domain proceedings, fair value is the standard which determines the amount of compensation. Indeed, this standard of fair value is no more indefinite and meaningless than the measure of damages employed in actions for slander, libel, breach of promise, etc.

Justification is sought to be found in permitting the mortgagee to thus usurp the debtor's property on the theory that, "even though a mortgagee obtains the property at a cheap price, he accomplishes this . . . . in an independent capacity, and not as mortgagee; as a purchaser, he obtained the same title as might have been acquired by any member of the general public in competitive bidding."[19] It would seem that the otherwise unconscionable conduct of the mortgagee is thus permitted to find protection behind the thin veil of the metaphysical and legalistic theory of a separate entity. As for the argument that the mortgagor may protect himself against thus being deprived of his property by express stipulation in the contract,[20] such a view ignores, from a realistic standpoint,

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[15] 187 Atl. 481, 490.
[16] Id., 485.
[17] Id., 491.
[18] Smyth v. Ames, 169 U. S. 466, 546 (1897). Italics ours.
[19] 187 Atl. 481, 492.
[20] Id., 492.

the economic bargaining inequality of the debtor, especially in times of depression.

Perhaps the most incongruous note in the decision is sounded by Chief Justice Kephart in his concurring opinion. He states:

> "This result does not, in my judgment, prevent mortgagee debtors from securing substantial relief in another form of procedure, equally as beneficial as that provided by the act in question. Appellee's counsel could have petitioned the court below to set aside the sheriff's sale for gross inadequacy in price such as would amount in law to a fraud on the debtor's right."[21]

If, as Justice Kephart says, the mortgagee can be prevented from unconscionably taking the debtor's property, if the right to insist on such usurpation is non-existent, how does the statute impair his right to take the property? In a word, the case seems to hold that the Mortgage Deficiency Judgment Act impairs a right which the mortgagee never had. If anything, it would seem that this argument of Justice Kephart, instead of supporting the majority opinion, discloses the weaknesses of it, and places him with the dissenting member of the court. If Chief Justice Kephart is right,[22] thousands upon thousands of mortgagors, whose properties have been taken away upon nominal bids of fifty dollars for costs only, can flood the equity courts with applications for relief. In that event, the statute merely provides an expedient whereby such overloading of the court lists may be avoided.

The best argument advanced by the majority is, that the act applies even if a third party is a purchaser at a nominal bid, and that, to force the mortgagee to credit the mortgagor's debt with the fair value of the property, under such circumstances, might be unjust to the mortgagee.[23] From a practical standpoint, however, the answer is, that the mortgagee who is proceeding against the land does so because he thinks it has some value. As previously indicated, the mortgagee usually does not permit a third person to get the property through a nominal bid. The mortgagee, in all probability, would bid up the property to the value which he sets on the property, or the amount of the debt, whichever is the lower. In any event, even if a third person is a purchaser, there is still the fundamental question of justice, as to whether, in order to give a creditor such a minute part of his claim as a third party pays, after a nominal bid, the

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[21]Id., 495.

[22]Compare Brotherline v. Swires et al., 48 Pa. 68 (1864) where property worth $1500 to $1800 was sold on a $20 bid. The trial court charged that such a sale was fraudulent as a matter of law. On appeal, the Supreme Court held that the sale could be avoided only if the jury found fraud in fact. A venire facias de novo was awarded.

[23]187 Atl. 481, 492.

debtor should be forced to submit to an unconscionable preemption of his property. Moreover, without necessarily attempting to suggest that this argument of the majority is entirely without merit,[24] at least it could not be controlling in the *Winowich* case, because the purchaser was not a third party, but the mortgagee himself.

It will not do to dismiss the undeniable fact of the desirability of such legislation, and to seek refuge behind the trite assertion that, while the court should "be realistic in facing current conditions, it would be recreant to its duty, if it sanctioned the whittling away of constitutional restrictions."[25] That assumes the point to be proved. The answers to most constitutional questions, and the superrefined distinctions built up by the decisions, are rarely spelled out by the Constitution. There is, to be sure, a theoretical distinction between declaring a statute invalid because it is unreasonable or arbitrary, on the one hand, and declaring the law invalid because it is unwise, on the other. And, it is true that courts consistently proclaim themselves unconcerned with the wisdom of legislative policies. But the dye of the economic, social, and political philosophies of the members of any given court will inevitably seep from the standard of what is unwise to color the standard of what is arbitrary. In the last analysis, as Chief Justice Hughes once said, "we are living under a Constitution, but the Constitution is what the Judges say it is."[26]

The conflicting opinions in the *Winowich* case simply represent two distinct schools of philosophy. The one is individualistic, seeking the survival of the fittest; the other champions the theory that society is entitled to protection against unfair individual profiteering.

It is true that the Pennsylvania decision follows the trend in most of the other states on similar statutes, although New York has held such a statute constitutional.[27] Apart from the respect which the New York Court of Appeals merits, it might be observed that there are instances in our constitutional

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[24]The Act might be improved by an amendment providing that, where a third person is the purchaser, and the bid falls below the fair market value of the property, the sale may be set aside and a new one ordered. This would be wholly in keeping with the suggestion of Chief Justice Kephart, and would avoid the possible construction of which the present Act is capable, under which the mortgagee would be compelled to credit the debtor with the fair value of the property, even though a third party purchaser might have entered only a nominal bid. Another possibility would be to provide simply that any purchase of property under foreclosure proceedings, whether by the mortgagee or a third party, at a price below the fair market value, may be set aside and a new sale ordered.

[25]187 Atl. 481, 494.

[26]Pearson & Allen, The Nine Old Men, 94 (1936); E. R. Nichols, Congress or the Supreme Court, 56 (1936).

[27]For cases holding similar acts unconstitutional, see: Vanderbilt v. Brunton Piano Co., 11 N. J. Law 596; Atlantic Loan Co. v. Peterson, 181 Ga. 266; Kresos v. White, Superintendent of Banks, (Ariz.) 54 P. (2d.) 800. Contra: Klinke v. Samuels, 264 N. Y. 144.

history where the majority of states, agreeing on some constitutional issue, were ultimately reversed by the United States Supreme Court. Thus, state workmen's compensation laws were almost unanimously declared unconstitutional until the decision in the *Second Employers' Liability Cases*.[28]

It might be observed, in passing, that the emphasis on *emergency* seems misplaced. To be sure, the evil sought to be remedied is then more widespread. But the utility in enforcing the salutary policy of a carefully prepared deficiency judgment act is no more limited to times of emergency than usury statutes. It may be wondered why such a policy should not be adopted permanently.

Whether or not unfavorable court decisions will check the effort to pass such enactments remains for the future to reveal. Modifications of the statute, especially concerning cases where third parties are purchasers,[29] might open the door to a reconsideration of the constitutional issues. At any rate, until the United States Supreme Court speaks on the subject, "hope springs eternal."

Carlisle, Pa. D. J. Farage
December 1, 1936.

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[28]223 U. S. 1 (1912).
[29]See footnote No. 24.