7/29/57

Memorandum No. 7

Subject: Study No. 24 - Mortgages for future advances.

On May 20 we sent you a copy of the study on this subject prepared by our research consultant, Professor John Merryman of Stanford. The Northern Committee has taken action on this study which is reported in the minutes of its meeting of May 4, 1957 sent to you on May 17. The matter is, therefore, ready for consideration by the Commission at the August, 1957 meeting.

Action

Respectfully submitted,

John R. McDonough, Jr.
Executive Secretary

JRM:ts

May 20, 1957

MORTGAGES FOR FUTURE ADVANCES *

* This Study was made at the direction of the Law Revision Commission by Professor John Henry Merryman of the School of Law, Stanford.

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MORTGAGES FOR FUTURE ADVANCES

In a mortgage for future advances a present lien is created on the property used as security, but the parties agree that all or part of the loan secured is to be made in the future. A familiar example is the building construction loan, in which advances are made to the mortgagor as construction proceeds. There are practical and legal advantages to the parties in this procedure. The mortgagee acquires a lien on land and improvements from the time of the original mortgage which is superior, in appropriate cases, to encumbrances later than the mortgage but prior to one or more of the future advances. Since he advances funds as construction progresses the value of his security increases as the loan grows. The mortgagor avoids paying interest on the total loan during the time he does not need it. The financing cost to him is lower than he would have had to pay had he executed a first mortgage for the initial advance and second and third mortgages for later ones, with their higher interest rates and the necessity for additional title searches. [1]

In California such mortgages are in common use in this and a variety of other situations, some of which are described in the discussion below. Prior to 1935 both real and personal property mortgages to secure future advances were governed entirely by case law. In that year two sections, 2974 and 2975, specifically applicable to chattel security were added to the Civil Code. [2] One result of this legislation was to raise a series of problems peculiar to chattel security for future advances. Real property security is still governed entirely by the cases. Because of problems involved in interpretation of the legislation enacted in 1935 this study was authorized" . . . to determine whether the law respecting mortgages to secure future advances should be revised." [3] The real property problems, being fundamental to comprehension of the legislation, are discussed first.

The major legal problem in mortgages[4] of real property for future advances is that of priority. Most of the reported litigation is in this area. The classic case is a dispute between the mortgagee for future advances and one who has acquired a lien on the property secured after that mortgage became effective but prior to one or more of the subsequent advances under it. In solving such disputes the California courts apply rules which are similar to those of a majority of American jurisdictions and which appear to be well settled.

The existence of a recording act, with its penalties for failure to record mortgages, insures that the disputes will ordinarily occur between parties who examined the record before they acted and who recorded the relevant instruments after they had done so. As a result solution of priority problems depends in part on the provisions of the applicable recording act.

Mortgages Expressed to Cover Future Advances

This type of mortgage indicates on its face, and thus shows on the record, that it is given to secure future advances. Although it may also indicate the specific nature and amounts of the advances or the total amount to be loaned this information is not necessary and its lack does not affect the validity or priority of the mortgage.[5] If properly recorded such mortgages are entitled to priority on all sums advanced before the creation of additional liens.[6]

Priority between subsequent advances and intervening liens is made to turn on a distinction between obligatory and optional advances.[7] If the mortgagee is legally obliged by the agreement between the parties to make subsequent advances he will be entitled to priority as to them even though he has had actual notice of the intervening lien.[8] This result may be supported on the theory that the obligation to make the advances became effective when the mortgage was executed and thus existed from its inception. Being prior in time to the intervening lien it is superior to it. The later payment is not really a new advance; it is merely deferred payment of a prior obligation.[9] Since the mortgage is recorded and shows that it is given to secure future advances, a prospective purchaser or encumbrancer has notice that his lien is possibly inferior to that of the mortgagee. He can, by inquiry, ascertain additional facts such as whether the advances are obligatory or what the total amount of the mortgage is, which will enable him to act wisely.[10] A more practical justification is that a different rule would impair the utility and flexibility of what appears to be a useful financing device while adding little to the protection of the intervening lienor.

If the mortgagee is not under a legal obligation to make future advances they are called optional. The rule is that optional advances made after actual notice[11] of intervening liens are inferior to them.[12] Record notice is not enough.[13] This result seems logical since the mortgagee, by definition, has no legal obligation to make the future advances and thus has little standing to object if he does so knowing that others have preceded him. The requirement of actual notice makes it unnecessary for him to conduct a new title search before making each advance, thus helping preserve the utility of the mortgage for future advances as a security device. The intervening lienor

should have made such a search himself, in any event, and it is not too great a burden to require him to give notice to the mortgagee.

These rules are well settled and it seems undesirable to disturb them. However they raise certain problems in application which require some consideration. For one, the distinction between obligatory and optional advances, while clear enough as a concept, is not always so in practice. Even in the relatively simple case where the mortgage itself contains the understanding of the parties as to the times, amounts and conditions of advances it may not be possible to ascertain without litigation whether the mortgagee is or is not under a legal obligation to make them. In such a case a prospective lienor cannot be sure that by giving notice to the mortgagee he will protect himself by acquiring a security interest superior to any subsequent advances the mortgagee might make. The uncertainty will have the same effect on the mortgagee, who cannot be sure whether any subsequent advances, after notice received, are protected. The probable result will be that the mortgagor will find it more difficult to borrow money on admittedly adequate security. Thus whatever interests are served by having some degree of certainty in business transactions and by encouraging commercial activity are frustrated.

The problem becomes more acute in those situations where the mortgage itself does not include the agreement of the parties as to the times, amounts and conditions of advances. In a number of such cases the parties have agreed orally as to the manner in

which future advances will be made. Such agreements naturally do not appear on the record. The uncertainty about whether they do or do not create a legal obligation on the mortgagee to advance further sums is likely to be greater than if the agreement had been included in the mortgage. A number of such cases have come before the California courts, which have admitted evidence concerning collateral agreements as to the optional or obligatory character of future advances, even when oral.[14] Such cases indicate that uncertainty about whether advances were obligatory or optional is a source of litigation in the field. Consideration might be given to methods of avoiding this problem. This question is discussed infra.

Mortgages Not Expressed to Cover Future Advances: Overstated Present Advance

Some mortgages for future advances do not so state, being in the form of a present loan of a stated sum, but with only part of the sum actually advanced at the time. The understanding of the parties is that future advances to the maximum stated may or will be made. This form of mortgage is a deceptive overstatement of the obligation which troubles courts when they first encounter it.[15] However the rule is that these are valid as mortgages for future advances.[16] An overstatement of the obligation secured by the first mortgage cannot harm the intervening lienor, so the reasoning goes, but can only operate in his favor. The excess of

value of the security over the prior lien is greater than the record would lead him to suppose. To this it might be added that in many cases a prospective lienor will inquire of the mortgagee to learn to what extent the principal of the loan secured has been amortized and whether the mortgagor is in default. In the course of such inquiries the amount actually owed the mortgagee should become apparent. An opposing consideration is that such an overstatement of the loan secured may mislead a person who has a junior lien into failure to enforce it. Another is that an assignee of the mortgagee may be misled by the record into thinking he is acquiring a larger interest than is in fact true. This possibility of fraud can easily be overstated, since in most cases the mortgagee is a bank or other responsible financial institution.

In California and most other jurisdictions[17] the same rules as to priority apply to mortgages of this type as to those expressly made to secure future advances, with one exception; the amount stated as the present advance is the maximum loan which will be given priority.[18] In mortgages expressed to secure future advances no such maximum need be stated and consequently no such limit exists.[19] This difference is probably not of much importance, since the parties can always provide that the maximum amount to be secured is a figure sufficiently large to include most contemplated contingencies.

In all other respects the rules are the same. If the advances are obligatory the mortgagee is protected against intervening

liens regardless of notice concerning them,[20] but if they are optional he loses priority as to advances made after actual notice of intervening encumbrances.[21] Here again it might be pointed out that the record in such cases does not indicate that the mortgage is given to secure future advances, and the prospective intervening lienor cannot expect to learn of this fact, much less whether they are optional or obligatory, unless he makes inquiry of the mortgagee. Consequently it might be thought unrealistic to place the burden of actual notice to the mortgagor on him. Certainly he is not sufficiently warned by the record. While the argument that he cannot be harmed by an overstatement of the lien held by the mortgagor is persuasive, situations can be imagined in which third persons might be misled. If there is any policy to the effect that the record should be reliable and accurate it is frustrated by such a rule, which tends to require prospective lienors to make inquiry of existing mortgagors even in cases where the record shows no evidence that future advances are anticipated. Occasionally inquiry must be less convenient and less informative to the prospective encumbrancer than a straightforward record might be. This problem is discussed further below.

PERSONAL PROPERTY

Until 1935 there were no statutes in California specifically applicable to mortgages of either real or personal property to secure future advances,[22] and the rules developed in the cases appeared to apply to both types.[23] In 1935 a number of sections were added to the Civil Code which changed the law respecting chattel mortgages, including

two specifically applicable to chattel mortgages for future advances. These sections read as follows:

> § 2974. Where a mortgage of live stock, or other animate chattels, or crops is taken to secure mainly, or among other things, funds that may be advanced thereafter from the mortgagee or assigns at the option of either to the mortgagor, mortgagors or any of them, which funds to be advanced shall be for the purpose of financing the mortgagor, mortgagors or any of them during any regular production period or periods involving the property or any part thereof encumbered by or described in said mortgage, and during which period or periods the mortgagor, mortgagors or any of them, may need and request such financing, such mortgage shall be and contine to be (subject to the provisions of sections 2911, 2968, 2969 and 2972 of the Civil Code), until formally released or discharged in the recorder's office, a lien and encumbrance upon the property described therein, of status, effect, rank and standing equal to that established initially and thereafter obtained by such mortgage, as security for the repayment of all sums that may be or become due under such mortgage, and all obligations secured thereby, even though during such period or periods of financing the debt or debts, obligation or obligations secured by such mortgage as they exist at any particular time, may have been repaid in full to the mortgagee or assigns, from proceeds of sale of the mortgaged property, or otherwise by the mortgagor, mortgagors, or any of them. Each such mortgage shall contain a statement that it is given for such purpose. All such mortgages shall be discharged on demand of the mortgagor, in conformity with the provisions of section 2941 of the Civil Code, whenever no sums are owing to the mortgagee, or assigns, thereunder.
>
> § 2975. A mortgage of personal property or crops may be given to secure the repayment of sums that may be advanced, expenditures that may be made, or indebtedness or obligations that may be incurred subsequent to the execution of such mortgage. If the maximum amount the repayment of which is proposed to be secured by such mortgage, is expressed therein (whether the creation of debts in such amount or any part thereof be optional with, or obligatory upon the mortgagee or assigns), such mortgage (subject to the provisions of sections 2911, 2941, 2968, 2969 and 2972 of the Civil Code) shall be and constitute a lien or encumbrance of rank, effect, status and standing equal to that established thereby initially and as it may thereafter obtain, as security for the repayment of any

> sums, expenditures, indebtedness and obligations, owing or due or becoming owing or due thereunder, up to and including such expressed maximum amount which shall be considered only as a limit of the debts, sums, expenditures, indebtedness and obligations that may be secured thereby at any one time, and not to include such as may have existed and been repaid or discharged thereunder. A mortgage of personal property or crops shall also constitute a lien or encumbrance of rank, effect, status and standing equal to that established initially or thereafter obtained thereby, as security for the repayment of all sums or amounts that are necessarily advanced or expended by the mortgagee or assigns, for the maintenance or preservation of the property, or any part thereof, described in such mortgage.

With one minor exception[25] there are no reported decisions interpreting either of these sections, and no legislative history has been found which might throw light on their meaning or function. It seems likely that this legislation was enacted in order to facilitate the extension of credit to farmers under the Federal Farm Credit Act of 1933. One purpose of that act was to create production credit associations to make crop and livestock loans.[26] Conceivably it was at the urging of these associations and other credit institutions that legislation was enacted giving them special priority in appropriate cases. The theory probably was that a clearer and more favorable legal position would encourage lenders to advance credit to farmers and thus hasten economic recovery from the depression. Specific reference in Section 2974 to production loans seems to support this theory, as do statements from persons in the lending business.[27]

It cannot be said that either Section 2974 or 2975 is entirely clear in meaning, and the only reported decision discussing either section has added to the confusion.[28] In Hollywood State Bank v. Cook,

in a statement which can be classified as dictum, the court stated that Section 2975 requires that "it must appear from the mortgage itself that it is given to secure future advances." A careful reading of that section fails to show any such requirement, and the statement of the court may best be dismissed as unnecessary to the decision in the case and unwarranted by the words of the statute. Beyond this dubious contribution the reported cases include nothing which might indicate what the sections mean.

Section 2975 applies to a "mortgage of personal property or crops" while Section 2974 refers to a "mortgage of live stock, other animate chattels, or crops." It would seem logical to conclude that Section 2975 is broad enough to include all mortgages which might fall under Section 2974, since live stock and other animate chattels form only one kind of personal property as defined in Civil Code Sections 658 and 663. Consequently the parties could conceivably draw a mortgage of live stock, other animate chattels or crops under either section, depending on which appeared to them the most advantageous under the circumstances. Under either section it would seem to be possible to obtain priority for optional future advances, either by stating the maximum amount as required by Section 2975 (or) by stating that the purpose of the mortgage is to finance the mortgagor during one or more regular production periods as required by Section 2974.

The hypothesis that Section 2975 is broader in scope than Section 2974 and is applicable to production mortgages is aided by the first and third sentences of Section 2975. The first seems to be very general in that it states that mortgages of personal property or

crops may be given to secure future advances. The third sentence likewise is very general in stating that any advances made under a mortgage of personal property or crops for the purpose of preserving the security under the mortgage are entitled to priority. This language is quite broad and is not even restricted to mortgages given to secure future advances; presumably it applies to any chattel mortgage. It therefore seems logical to think of Section 2975 as the major provision, providing rules applicable to all cases, and Section 2974 as ancillary to it, providing additional special rules applicable to a more limited type of transaction. While the order of the sections might indicate the contrary, it is difficult to interpret their language in any other way.[29]

The second sentence of Section 2975 appears to provide that if a mortgage given to secure future advances states the maximum amount to be secured all advances, whether optional or obligatory, will be entitled to the same priority as that originally established by the mortgage, so long as the total amount owing at any one time does not exceed the stated maximum. The question naturally arises as to what would be the legal effect of the mortgage if the maximum were not stated. Conceivably two views could be taken: one is that Section 2975 merely added to the law in existence in 1935; the other is that Section 2975 in effect repealed the prior law and substituted a new rule for it. If the former view were adopted then the failure to state the maximum would merely result in application of the rules developed in earlier cases. As a practical matter this would mean that optional advances made after notice of intervening liens would be inferior to them.

Failure to state the maximum amount to be secured would thus merely result in loss of priority for optional advances made after notice. However, if the other interpretation were accepted the consequences of failure to state the maximum amount might be quite different. One argument against acceptance of this interpretation is that the nature of such consequences is not suggested in the statute and would have to be left to conjecture. Another is that the first sentence of Section 2975 seems clearly to authorize mortgages for future advances in unqualified terms while the second sentence seems to relate the statement of maximum amount rather closely to the grant of absolute priority for optional advances. Thus the former interpretation seems the more logical one. In any event, the existing ambiguity should be eliminated.

The same question arises in interpreting Section 2974, but in a form which is slightly more difficult to resolve. The first sentence seems to provide that advances made to finance a mortgagor during one or more regular priods of production, under a mortgage of live stock, other animate chattels or crops, are entitled to priority even if optional. The second sentence provides that "Each such mortgage shall contain a statement that it is given for such purpose." The question here is what would be the consequences of failure to include such a statement in the mortgage. Conceivably they might be total invalidity of the mortgage, invalidity with respect to third persons, loss of priority on all future advances, loss of priority on optional advances made after actual notice of intervening liens, or something else. The choice of consequences under this interpretation

would be both difficult and arbitrary. However, the second sentence might be read to mean that the special advantages of the first sentence - i.e., priority for optional advances - will be available to the parties only if such a statement appears in the mortgage. The effect of failure to include the statement would be to make the mortgage subject to the law existing apart from the statute. This interpretation is the better one and would be consistent with that developed above for Section 2975.[30] Again the existing ambiguity should be eliminated.

Assuming the validity of this approach to interpretation, the following paraphrase of Sections 2974 and 2975, arranged parallel to the language of the statutes, seems accurate:

Section 2975	Paraphrase
1. A mortgage of personal property or crops may be given to secure the repayment of sums that may be advanced, expenditures that may be made, or indebtedness or obligations that may be incurred subsequent to the execution of the mortgage.	1. A mortgage of personal property or crops may be given to secure future advances.
2. If the maximum amount of repayment which is proposed to be secured by such mortgage, is expressed therein (whether the creation of debts in such amount or any part thereof be optional with, or obligatory upon the mortgagee or assigns) such mortgage (subject to the provisions of Sections 2911, 2941, 2968, 2969 and 2972 of the Civil Code) shall be and constitute a lien or encumbrance or rank, effect, status and standing equal to that established thereby initially and as it may	2. If the maximum loan to be secured is stated in the mortgage all advances, whether optional or obligatory, up to that amount are entitled to the same priority as that originally established by the mortgage. The stated maximum shall mean the maximum amount that may be owed at any time and shall not include any loans or advances under the mortgage that have already been discharged or repaid. If the maximum loan to be secured is not stated obligatory

thereafter obtain, as security for the payment of any sums, expenditures, indebtedness and obligations, owing or due or becoming owing or due thereunder, up to and including such expressed maximum amount which shall be considered only as a limit of the debts, sums, expenditures, indebtednesses and obligations that may be secured thereby at any one time, and not to include such as may have existed and been repaid or discharged thereunder.

advances are entitled to the same priority as that originally established by the mortgage but optional advances are not if made with actual notice of intervening liens.

3. A mortgage of personal property or crops shall also constitute a lien or encumbrance of rank, effect, status and standing equal to that established initially or thereafter obtained thereby, as security for the repayment of all sums or amounts that are necessarily advanced or expended by the mortgagee or assigns, for the maintenance or preservation of the property, or any part thereof, described in such mortgage.

3. Necessary expenditures made by the mortgagee in order to preserve his security shall be entitled to the same priority as that originally established by the mortgage whether or not the maximum loan to be secured is stated.

Section 2974

4. Where a mortgage of live stock, or other animate chattels, or crops is taken to secure mainly, or among other things, funds that may be advanced thereafter from the mortgagee or assigns at the option of either to the mortgagor, mortgagors or any of them, which funds to be advanced shall be for the purpose of financing the mortgagor, mortgagors or any of them during any regular production period or periods involving the property or any part thereof encumbered by or described in said mortgage, and during which period or periods the mortgagor, mortgagors or any of them, may need and request such financing, such mortgage shall be and continue to be (subject to the provisions of Sections 2911,

4. If livestock, other animate chattels or crops are mortgaged for the purpose of financing the mortgagor during one or more regular production periods advances made for that purpose shall be entitled to the same priority as that originally established by the mortgage, even though the advances are optional and even though made with actual notice of intervening liens.

and the mortgage states that it is made for such purpose,

2968, 2969 and 2972 of the Civil Code), until formally released or discharged in the recorder's office, a lien and encumbrance upon the property described therein, or status, effect, rank and standing equal to that established initially and thereafter obtained by such mortgage, as security for the repayment of all sums that may be or become due under such mortgage, and all obligations secured thereby.

5. Even though during such period or periods of financing the debt or debts, obligation or obligations secured by such mortgage, as they exist at any particular time, may have been repaid in full to the mortgagee or assigns, from proceeds of sale of the mortgaged property, or otherwise by the mortgagor, mortgagors or any of them.

5. Temporary balances in favor of the mortgagor, or temporary repayment in full of amounts owing under the mortgage, shall not extinguish the mortgage.

6. Each such mortgage shall contain a statement that it is given for such purpose.

6. Unless a mortgage given to finance the mortgagor during a production period states that it is such a mortgage optional advances made after actual notice of intervening liens do not have priority over such liens.

7. All such mortgages shall be discharged on demand of the mortgagor, in conformity with the provisions of Section 2941 of the Civil Code, whenever no sums are owing to the mortgagee, or assigns, thereunder.

7. When all sums owing under the mortgage are paid the mortgage shall be discharged on demand of the mortgagor, in conformity with the provisions of Section 2941 of the Civil Code.

POSSIBLE REVISION

In this section problems which have appeared in the preceding discussion or which have been suggested by attorneys are examined and the possibility of statutory revision considered.

Real Property

Any consideration of revision of the California law applicable to real property mortgages to secure future advances is met by the fact that the great weight of authority in other American jurisdictions and in England is on the side of the existing law.[31] Although there are major variations in a few of the states and minor variations in others[32] most conform to the analysis developed above. It would probably be unwise to change uniform settled rules in favor of what might appear in theory to be a more desirable approach without a thorough investigation of the consequences. Such an investigation would assume the proportions of a field study and lies outside the scope of the present report. The problems which might merit such a field study are set out below, together with some of the more obvious factors bearing on their solution.

As the law now stands optional future advances are inferior to liens as to which the mortgagee has actual notice when the advances are made, while obligatory advances have the same priority as that originally established by the mortgage. This distinction between optional and obligatory advances has been sufficiently troublesome to

lead to a substantial amount of reported litigation.[33] Attempts to avoid this problem might assume either of two forms: abolition of the distinction or clarification of it in such a way as to make clear to one who consults the record whether advances are of one kind or another. The existing distinction between optional and obligatory advances could be abolished by giving both kinds of advance the same priority as that now enjoyed by obligatory advances, as one alternative, or optional advances, as the other. Either kind of action would make a significant change in the law.

If the priority of obligatory advances was reduced to that of optional advances institutions which finance building construction (in which mortgages for obligatory future advances are most frequently used) would be seriously affected. They might substitute a different financing device, similar to the one used in Maryland, in cases where maximum priority was desired.[34] However it is possible that banks would stop obliging themselves to make future advances in building construction loans, either substituting a simple mortgage for the full amount or an optional mortgage for future advances. In the former case the undeniable advantages to the parties of a useful security device would have been lost. In the latter case the mortgagor would be placed in a difficult position, since he would not be assured that future advances would be made when needed in order to continue with construction.

As an alternative it would be possible to give optional advances the same priority as that now given obligatory advances. This is the effect of Sections 2974 and 2975 of the Civil Code in chattel security

cases, and it might be argued that what works for chattel security should work equally well for real property security. However there are two important distinguishing considerations. One is that chattel security transactions are generally for a shorter term and serve different purposes than real property security. Chattel security is more a branch of commercial law than property law and thus not always susceptible to identical treatment. The other consideration is that different third parties are involved. In real property cases priority disputes involve purchasers, junior mortgagees, materialmen and mechanics, while in chattel security cases the third party is usually a purchaser, a junior mortgagee or judgment lienor.

The special considerations applicable to mechanics and materialmen seem especially relevant. To give optional future advances priority over their liens even after actual notice has been given could, in cases where the mortgagor becomes insolvent and the property secured is not sufficiently valuable to pay all lienors and debtors, result in serious loss to them. These, of course, are the cases where priority becomes important. It thus seems that any such rule might, in effect, make mechanics' and materialmen's liens less valuable than they now are. Since these persons are in a somewhat different position than lending institutions in their degree of familiarity with the legal problems involved, their access to counsel, and particularly in their ability, as a practical matter, to refuse to provide labor, services and materials in cases which might appear to involve the risk of non-payment, such a rule might be thought unjust to them. When the advances are obligatory mechanics' and

materialmen's liens are in no better position, but in those cases there is the advantage to them that the mortgagee must make additional advances. These funds in the hands of the mortgagor will presumably be available to pay their claims.[35]

It might also place the mortgagor in an undesirable position. Presumably a bank which would acquire no greater priority from obligatory advances than it would from optional ones would tend to restrict its practice to optional advances whenever possible. A mortgagor might then be refused advances by the mortgagee and find it difficult to obtain the money elsewhere, since other lenders would be reluctant to rely on a lien which would be inferior to any subsequent advances the mortgagee might make. This would also make it possible for the original mortgagee to take advantage of the mortgagor's unfortunate position in various ways. Advances might be made only if higher interest was paid or if additional security was furnished, etc. Requiring the mortgage to state the maximum loan to be secured might limit this problem slightly, but it would always be possible for the parties to state a sufficiently high amount that the security value of the property in excess of it would be slight, or even nonexistent.

The alternative procedure of clarifying the distinction between optional and obligatory future advances also presents difficulties. Legislation designed to achieve such clarification would have to be relatively complex and detailed, since its objective would be to distinguish between advances that actually were obligatory or optional. This might be done by requiring that the parties, if they wish the advances to be treated as obligatory, agree on the precise amounts,

times and conditions of all advances to be made under the mortgage. In order for this information to be helpful to third parties it would have to appear on the record, preferably in the mortgage itself. The effect on existing law would be obvious. Mortgages expressed to secure future advances would have to express the amounts to be advanced, as is not now the case.[36] The overstated present advance type of mortgage to secure future advances would, in effect, be abolished in all except cases in which the advances were optional.[37] Collateral oral agreements would not be admissable to establish the nature of the advances.[38] Presumably failure to meet the requirements of the statute would result in advances being considered optional for priority purposes. Assuming such legislation were acceptable to financing institutions and thus reasonably likely to be enacted the danger would remain that the result might be more confusion (although of a different kind) and litigation than the case law rule it replaced.

A related problem is created by the rule that allows collateral unrecorded agreements, oral or in writing, to be admitted to show that future advances were anticipated (in the overstated present advance situation) and to show the amounts, times and conditions of such advances. Some of the litigation about whether advances are optional or obligatory may be traced to the uncertainty and difficulty of proof this rule causes. It is conceivable that a statute requiring such details to appear in the mortgage or collateral recorded instrument would be useful. It might state that advances made after notice of intervening liens would be inferior to them unless the record showed that the advances were obligatory. Or it

might limit consideration of the nature of the advances, in priority disputes, to the record, with the provision that advances not shown by the record to be obligatory should be declared optional (for purposes of priority). Neither approach would be satisfactory unless there were also some description of the statements in the mortgage or collateral recorded agreement which would result in the advances actually being obligatory, since presumably the purpose of varying the priority is to protect the mortgagee when he is under a legal obligation to make the advances. This approach would raise the same group of problems as those discussed in the preceding paragraph and should not be adopted without the kind of field study there recommended.

These considerations lead to the conclusion that revision of the law in an attempt to abolish or clarify the distinction between optional and future advances should not proceed without thorough study of the practical consequences to mortgagees, mortgagors and typical classes of intervening lienor. The recommendation is that in the absence of such studies no attempt be made to revise the law in this area.

Another problem is raised by the overstated present advance type of mortgage.[39] The problem is that the record does not and cannot show that future advances are contemplated, and consequently it seems unrealistic to expect an intervening encumbrancer to give actual notice to the mortgagee in such a way as to acquire priority over subsequent optional advances. This problem has been met in England, under the Law of Property Act (1925)[40] by the provision

that record notice is sufficient to establish priority over optional advances where the original mortgage does not show on the record that it is given to secure future advances. Such a rule would not appear to cause any great hardship to mortgagees since it would not affect their priorities in any way and would simply place the burden of examining the record on them in those cases in which the mortgage is for an overstated present advance with a collateral agreement that future advances will be optional. However, it is difficult to escape the reasoning, set out in several California cases,[41] that the overstatement cannot really harm the intervening lienor, especially since he can, and in most cases would, learn the details of the transaction by making inquiry of the mortgagee.[42] Thus though some such revision of the law appears logical and harmless, it is not clear that it would serve any major useful purpose.

A final consideration is that any revision of the law affecting real property mortgages would presumably change the law applicable to mortgages of personal property and crops. This follows because of the conclusion reached above that except in the narrow area covered by Sections 2974 and 2975 of the Civil Code the same rules apply to both groups of cases.[43] For all these reasons the recommendation is that no revision be attempted at this time with respect to the law governing mortgages of real property to secure future advances.

Personal Property

In considering revision of the law relating to mortgages of chattels to secure future advances no such uniformity is

encountered as that which exists in the real property cases. Only one jurisdiction in the United States has a statute similar in language to either Section 2974 or 2975.[44] The major problem is that of clarity. The existing statutes are unclear in meaning and effect. It seems desirable to revise them in such a way as to remove major doubts about their meaning and clarify their relation to the law in existence when they were enacted. The following recommendations are based on the interpretation of Sections 2974 and 2975 of the Civil Code developed above.[45]

Section 2974 appears to be the major offender, but the evidence indicates that it is not frequently used by lending institutions.[46] This fact, coupled with the conclusion that all cases falling under Section 2974 could also be covered by Section 2975, would seem to justify repeal of the section. A possible objection is that under Section 2975 the maximum amount to be secured must be stated in order to secure full priority for optional future advances. Under Section 2974 this is not necessary. However, assuming that Section 2974 is seldom used this consideration seems unimportant. Section 2974 also provides that temporary balances in favor of the mortgagor or temporary repayment in full of amounts owing under the mortgage shall not extinguish the mortgage. It is arguable that the prior case law established a similar rule for all such mortgages, and that repeal of Section 2974 would thus not remove it from the law. This matter is discussed further below. The recommendation is that Section 2974 be repealed.

Section 2975 should be retained in substance, but it could be improved a great deal by rephrasing. In addition at least one troublesome problem of interpretation could be avoided by enacting as part of Section 2975 the rule of the Buck case [47] which was included in Section 2974 but omitted from Section 2975. This has to do with the result of a temporary repayment in full of the mortgage. It is common for mortgages of this type to be given on a kind of "open account" basis, with the amount owing fluctuating widely depending on the needs and the often seasonal income of the mortgagor. This is particularly true when the mortgagee acts as marketing agent for the mortgagor and credits the proceeds of sale to the account secured. Uncertainty as to the effect of temporary repayment of all outstanding sums has led to the practice, in some lending institutions, of purposely leaving a small balance owing in order to avoid inadvertantly discharging the mortgage by payment before the parties intend it to be extinguished. Prior to the 1935 legislation it was held in the Buck case that temporary payment in full did not discharge the mortgage, but enactment of a similar provision in Section 2974, while omitting any reference to the problem in Section 2975, has caused uncertainty. On the theory that the 1935 legislation merely added to the existing law and did not completely replace it it can be logically argued that the rule of the Buck case is still in effect. However, enactment of a similar provision in the new Section 2975 would remove all doubt about the matter.

Another problem is the effect, under Section 2975, of failure to state the maximum amount owing. The interpretation developed above,

to the effect that in such a case the law independent of the statute would govern, seems logical.[48] However it might be thought desirable to include in any recommended revision of the law some statement which would remove doubt about the matter. The following proposal for a revision of Section 2975 attempts to meet these requirements. The proposed statutory language appears in italics and comments concerning the purpose or meaning of each provision in Roman type.

Mortgages of personal property or crops may be given to secure future advances. This appears to convey the meaning of the first sentence of the present statute in fewer words. If the maximum amount to be secured is stated in the mortgage the lien for all advances to that amount, whether optional or obligatory, has the same priority as that originally established by the mortgage. This is a restatement in shorter and clearer form of part of the second sentence of Section 2975. There is no intention to change the meaning. Thus "has the same priority as" seems to say as much as "shall be and constitute a lien or encumbrance of rank, effect, status and standing equal to." And "that originally established by the mortgage" should mean at least as much as "that established thereby initially and as it may thereafter obtain." If the maximum amount to be secured is not stated the lien for all optional advances made after actual notice of intervening liens is inferior to them in priority. This is the rule which existed prior to 1935 and which, under the interpretation developed above, survived enactment of Sections 2974 and 2975. It is stated here in order to remove any existing

uncertainty. The stated maximum shall mean the maximum amount secured at any time and does not include amounts already discharged or repaid. This is a restatement of the last part of the second sentence and is not intended to change the meaning. Repayment in full of amounts owing under the mortgage does not extinguish the mortgage. This provision is the equivalent of a similar one in Section 2974. It is added here in order to clarify the law on the theory that the rule established in the Buck case survived the enactment of Sections 2974 and 2975 in 1935. Necessary expenditures made by the mortgagee to preserve the security constitute liens having the same priority as that originally established by the mortgage. This is the rule under the cases for real property mortgages, [49] and it was formerly contained in the last sentence of Section 2975. It is continued here in briefer and clearer form.

FOOTNOTES

1. See Osborne, Mortgages § 113 (1951); 4 Am L. Prop. § 16.70 (1952); Although the corporate mortgage is in some ways similar to a mortgage for future advances it raises many problems of an entirely different kind and has accordingly been omitted from this study. See 3 Glenn, Mortgages §§ 405-406.3 (1943); Osborne, Mortgages § 123 (1951); 4 Am. L. Prop. § 16.78 (1952).
2. Cal. Stat. 1935, c. 817, §§ 8, 9.
3. Cal. Stat. 1956, res. c. 35.
4. The same rules apply to trust deeds to secure future advances, Atkinson v. Foote, 44 Cal. App. 149, 186 Pac. 831 (1919), and by analogy they have been applied to the assignment of a chose in action to secure future advances, Willard v. National Supply Co., 51 Cal. App.2d 555, 125 P.2d 519 (1942). Prior to 1935 chattel mortgages for future advances were subject to the same rules. See Frank H. Buck Co. v. Buck, 162 Cal. 300, 200 Pac. 392 (1921).
5. Frank H. Buck Co. v. Buck, 162 Cal. 300, 200 Pac. 392 (1921); Tapia v. De Martini, 77 Cal. 383, 19 Pac. 641 (1888); Oaks v. Weingartner, 105 Cal. App. 2d 598, 234 P.2d 194 (1951). In Connecticut, Maryland and New Hampshire the maximum amount must be stated. Matz v. Arick, 76 Conn. 388, 56 Atl. 630 (1904); Stoughton v. Pasco,

5 Conn. 442 (1825); Hewitt, The Rule in Matz v. Arick, 2 Conn. B. J. 237 (1928); Md. Code art. 66, c. 2 (Flack 1951); In re Shapiro, 34 F. Supp. 737 (D.C. Md. 1940); High Grade Brick Co. v. Amos, 95 Md. 571, 52 Atl. 582, 53 Atl. 148 (1902); Watkins, Maryland Mortgages for Future Advances, 4 Md. L. Rev. 110 (1940); N. H. Rev. Stat. c. 479:3-479:5 (1955); Mica Products Co. v. Heath, 81 N.H. 470, 28 Atl. 805 (1925). In Georgia the statute requires that the mortgage "specify the debt to secure which it is given." This has not been interpreted to require that the maximum amount be stated if it can be otherwise ascertained. Ga. Code § 67-102 (1955); Allen v. Lathrop, 46 Ga. 133 (1872).

6. This proposition is assumed in most of the cases, but it is so obvious that none have stated it. See 3 Glenn, Mortgages § 400 (1943); Osborne, Mortgages § 118 (1951); 4 Am. L. Prop. § 16.73 (1952).

7. The distinction between optional and obligatory advances was not made in the leading case of Tapia v. De Martini, 77 Cal. 383, 19 Pac. 641 (1888) or in Hall v. Glass, 123 Cal. 500, 56 Pac. 336, 69 Am. St. Rep. 77 (1899) but all the later California cases recognize and apply it. In Maryland the distinction is not observed in that neither type is given priority. See authorities cited supra, n. 5. In Mississippi and Texas the reverse situation exists; both optional and obligatory advances are given priority, even though actual notice of the

intervening lien has been received before the advance is made. Consequently the distinction is not of importance in determining priorities. Gray v. Helm, 60 Miss. 131 (1882); Witczinski v. Everman, 51 Miss. 841 (1876); First National Bank v. Zarofonetis, 15 S.W.2d 155 (Tex. Civ. App. 1929); Willis v. Sanger, 15 Tex. Civ. App. 655, 40 S.W. 229 (1897).

8. Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928); Fickling v. Jackman, 203 Cal. 657, 265 Pac. 810 (1928); Willard v. National Supply Co., 51 Cal. App.2d 555, 125 P.2d 519 (1942); Lumber and Builders Supply Co. v. Ritz, 134 Cal. App. 607, 25 P. 2d 1002 (1933); Wood Lumber Co. v. Mulholland, 118 Cal. App. 475, 5 P.2d 669 (1931); Atkinson v. Foote, 44 Cal. App. 149, 186 Pac. 831 (1919); Valley Lumber Co. v. Wright, 2 Cal. App. 288, 84 Pac. 58 (1905).

9. In Maryland, mortgages for obligatory future advances are not given priority. However, if the bank credits the full amount of the loan to the account of the mortgagor under an agreement that stated amounts will be released at stated intervals the effect desired is achieved. The distinction seems to be based on the idea that the irrevocable credit to the mortgagor's account is more like an escrow loan than a mortgage for future advances. Se Md. Code art. 66, c. 2 (Flack 1951); White Eagle Polish American Building & Loan Assn. v.

Canton Lumber Co., 168 Md. 199, 178 Atl. 214 (1934); Eisinger Mill & Lumber Co. v. Dillon, 159 Md. 185, 150 Atl. 271 (1930); New Baltimore Loan & Savings Assn. v. Tracey, 142 Md. 219, 120 Atl. 441 (1923); Western National Bank v. Jenkins, 131 Md. 250, 101 Atl. 667 (1917); 3 Glenn, Mortgages § 400.1 (1943); Osborne, Mortgages § 115 (1951); Watkins, Maryland Mortgages for Future Advances, 4 Md. L. Rev. 111 (1940).

In Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928), an arrangement of this type was treated as a mortgage for obligatory future advances.

10. Presumably the mortgagee is expected to respond frankly to such inquiries. The cases do not indicate what the consequences might be should he refuse. However bankers state that they give such information freely to persons with interests beyond mere curiosity.

11. Although the decisions speak of the necessity for "actual notice" the context always indicates that they mean to say only that record notice is insufficient. See cases collected in annotation, 138 A.L.R. 586 (1942). In Atkinson v. Foote, 44 Cal. App. 149, 186 Pac. 831 (1919) the court held that notice to the attorney (agent) was notice to the client (principal). The reasoning was that this was something more than record notice and thus sufficient. No other discussions of the question have been found.

12. Savings & Loan Society v. Burnett, 106 Cal. 514, 39 Pac. 922 (1895); Tapia v. De Martini, 77 Cal. 383, 19 Pac. 641 (1888); Yost-Lynn Lumber Co. v. Williams, 121 Cal. App 571,

9 P. 2d 324 (1932); Althouse v. Provident Mutual Building-Loan Assn, 59 Cal. App. 31, 209 Pac. 1018 (1922); W. P. Fuller & Co. V. McClure, 48 Cal. App. 185, 191 Pac. 1027 (1920); Atkinson v. Foote, 44 Cal. App. 149, 186 Pac. 831 (1919). In New Hampshire optional mortgages for future advances are valid only as to the present advance made. N. H. Rev. Stat. c. 479:3-479:4 (1955); Stavers v. Philbrick, 68 N.H. 379, 36 Atl. 16 (1895); Abbott v. Thompson, 58 N.H. 255 (1878). In 1955 this statute was amended in language which appears to change the rule to one more in conformity with the majority. N. H. Rev. Stat. c. 479:4 (supp. 1955). In Mississippi and Texas optional advances have priority even though actual notice has been received. See authorities cited supra, n. 7.

13. In Hall v. Glass, 123 Cal. 500, 56 Pac. 336, 69 Am. St. Rep. 77 (1899), a case dealing with a crop mortgage, the court appeared to approve the rule that recording was sufficient notice to give priority over subsequent optional advances. However all the other cases, including later ones, are contra.

In three jurisdictions record notice has been held sufficient to destroy priority of subsequent optional advances. Ladue v. Detroit & M. R. Co., 13 Mich. 380, 87 Am. Dec. 759 (1865); Spader v. Lawler, 17 Ohio 371, 49 Am. Dec. 461 (1848); Kuhn v. Southern Ohio Loan & Trust Co., 101 Ohio St. 34, 126 N. E. 820 (1920); McClure v. Roman, 52 Pa. 458 (1896); Bank of Commerce's Appeal, 44 Pa. 423 (1863); Bank of Montgomery County's Appeal, 36 Pa. 170, 3 Grant Cas. 300

(1860); Ter-Hoven v. Kerns, 2 Pa. 96 (1845).

14. Hall v. Glass, 123 Cal. 500, 56 Pac. 336, 69 Am. St. Rep. 77 (1899); Lumber & Builders Supply Co. v. Ritz, 134 Cal. App. 607, 25 P.2d 1002 (1933); W. P. Fuller & Co. v. McClure, 48 Cal. App. 185, 191 Pac. 1027 (1920).

15. Tapia v. De Martini, 77 Cal. 383, 19 Pac. 641 (1880); Tully v. Harloe, 35 Cal. 302, 95 Am Dec. 102 (1868).

16. Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928); Tapia v. De Martini, 77 Cal. 383, 19 Pac. 641 (1880); Tully v. Harloe, 35 Cal. 302, 95 Am. Dec. 102 (1868); W. P. Fuller & Co. v. McClure, 48 Cal. App. 185, 191 Pac. 1027 (1920); Valley Lumber Co. v. Wright, 2 Cal. App. 288, 84 Pac. 58 (1905). In Connecticut such mortgages are protected only as to the amounts originally advanced and all subsequent advances are inferior to intervening liens. The restrictive statutes in New Hampshire (discussed supra, n. 12) and Maryland (discussed supra, n. 5, 9) appear to make them void. See 3 Glenn, Mortgages § 403 (1943); Osborne, Mortgages § 122 (1951); 4 Am. L. Prop. § 16.77 (1952).

17. 3 Glenn, Mortgages § 398 (1943); Osborne, Mortgages § 116 (1951); 4 Am. L. Prop. § 16.72 (1952).

18. Tapia v. DeMartini, 77 Cal. 383, 19 Pac. 641 (1880); Tully v. Harloe, 35 Cal. 302, 95 Am. Dec. 102 (1868).

19. See discussion supra, n. 5.

20. Tapia v. DeMartini, 77 Cal. 383, 19 Pac. 641 (1880), appears to ignore the distinction between optional and obligatory advances in these cases, but later decisions apply it as

stated in the text. Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928); Valley Lumber Co. v. Wright, 2 Cal. App. 288, 84 Pac. 58 (1905).

21. Savings & Loan Society v. Burnett, 106 Cal. 514, 39 Pac. 922 (1895). In England under the Law of Property Act (1925) recording the intervening lien places the mortgagee of the overstated present advance type on notice. See Fisher & Lightwood's Law of Mortgages 508-9 (7th ed. 1931).

22. Except the very general provision in Civil Code Section 2884 that "A lien may be created by contract, to take immediate effect, as security for the performance of obligation not then in existence."

23. Frank H. Buck Co. v. Buck, 162 Cal. 300, 200 Pac. (1921); Tully v. Harloe, 35 Cal. 302, 95 Am. Dec. 102 (1868); Willard v. National Supply Co., 51 Cal. App.2d 555, 125 P. 2d 519 (1942).

24. Cal. Civ. Code §§ 2974, 2975.

25. Hollywood State Bank v. Cook, 99 Cal. App.2d 338, 221 P.2d 988 (1950).

26. There is a helpful discussion of this legislation in Preston and Bennett, Agricultural Credit Legislation of 1933, 42 J. Pol. Econ. 6 (1934).

27. "I am quite sure that the bill which became Chapter 817 of the Statutes of 1935, which added these two sections to the code and made other changes in the sections dealing with chattel mortgages, was sponsored by the production credit associations." Letter of August 3, 1956 from

Edward D. Landels, Legislative Representative for the California Bankers Association.

"Some time ago I inquired into the legislative history but didn't get far. One informant was under the impression that the sections had been sponsored by the Federal Land Bank or some other agency connected with the Farm Credit Administration." Letter of August 1, 1956 from E. H. Corbin, Vice President, Legal Department, Security-First National Bank of Los Angeles.

28. See note 25 supra.

29. "It has always been my opinion that Section 2975 is the section dealing with Chattel Mortgages generally, and that Section 2974 was added to cover mortgages given to secure loans made for the purpose of financing a mortgagor during regular production periods. All Chattel mortgages are subject to the provisions of Section 2975. However, if the mortgage is for the special purposes set forth in Section 2974, then the additional rights or benefits conferred by this section are available to the parties. In other words, Section 2974 is merely supplemental to Section 2975." Letter of October 10, 1956 from Percy A. Smith, Attorney for the Production Credit Corporation, Federal Intermediate Land Bank and Bank for Cooperatives of Berkeley.

30. Mr. Percy A. Smith, in the letter cited in the previous footnote, suggests the same interpretation as that developed in the text. A similar approach was taken by the writer of the material on chattel mortgages in California Jurisprudence. See 10 Cal. Jur.2d, Chattel Mortgages §§ 14-17 (1953).

31. The cases are collected and discussed in 3 Glenn, Mortgages §§ 392-406.3 (1943); Osborne, Mortgages §§ 113-124 (1951); 4 Am. L. Prop. §§ 16.70-16.79 (1952).

32. See discussion in notes 5, 7, 9, 12, 13, 16 and 21, supra.

33. Fickling v. Jackson, 203 Cal. 657, 265 Pac. 810 (1928); Savings and Loan Society v. Burnett, 106 Cal. 514, 30 Pac. 922 (1895); Willard v. National Supply Co., 51 Cal. App.2d 555, 125 P.2d 519 (1942); Lumber and Builders Supply Co. v. Ritz, 134 Cal. App. 607, 25 P.2d 1002 (1933); Lanz v. First Mortgage Corp., 121 Cal. App. 587, 9 P.2d 316 (1932); Yost-Linn Lumber Co. v. Williams, 121 Cal. App. 571, 9 P.2d 324 (1932); Wood Lumber Co. v. Mulholland, 118 Cal. App. 475, 5 P.2d 669 (1931); Atkinson v. Foote, 44 Cal. App. 149, 186 Pac. 831 (1919); Valley Lumber Co. v. Wright, 2 Cal. App. 288, 84 Pac. 58 (1905). In some of these cases it is not clear whether the nature of the advances were litigated below, although in most it appears to have been an issue at the trial.

34. See note 9, supra. This alternative might not be available since in Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928) a similar device was treated by the court as a mortgage to secure future advances.

35. In Smith v. Anglo-California Trust Co., 205 Cal. 496, 271 Pac. 898 (1928) the court required the mortgagee to hold funds not yet advanced when the mortgagor died available to satisfy claims of mechanics and materialmen, because the advances were obligatory.

36. See note 5, supra and accompanying text.

37. This would follow because of the requirement that the mortgage or collateral recorded instrument contain the full agreement of the parties.

38. See note 14 supra and accompanying text.

39. See notes 15-21 supra and accompanying text.

40. Discussed in Fisher & Lightwood's Law of Mortgages 508-9 (7th ed. 1931).

41. Tapia v. DeMartini, 77 Cal. 383, 19 Pac. 641 (1880); Tully v. Harloe, 35 Cal. 302, 95 Am. Dec. 102 (1868).

42. It would also be possible for a junior lienor to send stop notices to superior mortgagees of record in all cases. While this might be a practical way of insuring the maximum available priority it would tend in some cases to be the kind of idle and useless act that the law should not require. And it would still not help the prospective lienor learn from the record the details which might help him decide whether he wants to extend credit at all.

43. See note 30 supra and accompanying text.

44. Arizona has statutes enacted in 1941 which are almost identical with Sections 2974 and 2975 of the California Civil Code. Presumably the California legislation was used as a model by the Arizona legislature. See Ariz. Rev. Stat. §§ 33-771 to 33-773 (1956). For a collection of state laws and summaries of court decisions see Conditional Sale & Chattel Mortgage Reporter.

Sections 9-204 and 9-312 of the Uniform Commercial Code contain provisions applicable to chattel security for future advances. Since these provisions are integral parts

of the Code itself and do not mean much apart from that context consideration of them as a possible model for revision of Sections 2974 and 2975 seemed unwise. The approach taken by Article 9 of the Code is so different from that embodied in the California statutes that piecemeal adoption would tend toward confusion, rather than clarity. See generally American Law Institute and National Conference of Commissioners on Uniform State Laws, Uniform Commercial Code: Final Text Edition, Art. 9 (1951); Cooper, New Wines and New Bottles: The Uniform Commercial Code and the California Law of Chattel Security, 27 So. Calif. L. Rev. 265 (1954).

45. See notes 22-30 supra and accompanying text.

46. "With respect to Section 2974; although this Section has been in the code for many years, my experience is that the banks and other financial institutions make very little use of it. Section 2975 is used almost exclusively. I, personally, have never drawn a mortgage pursuant to Section 2974. I use Section 2975 exclusively. I have never had a request from the California Bankers Association since the Section was adopted for a form of mortgage under it to be given to any of its member banks. I have, however, over the years prepared several forms of mortgage under Section 2975 for use by members of the Association. I have talked with Mr. Kenneth Johnson, Esq., General Counsel for the Bank of America, and he tells me his bank makes very little use of Section 2974." Letter of July 30, 1956 from J. F. Shuman of Morrison, Foerster, Holloway, Shuman & Clark, counsel

for the California Bankers Association.

47. Frank H. Buck Co. v. Buck, 162 Cal. 300, 200 Pac. 392 (1921).

48. See note 30 supra and accompanying text.

49. Savings & Loan Society v. Burnett, 106 Cal. 514, 39 Pac. 922 (1895).

5/17/57

MINUTES OF MEETING

OF

NORTHERN COMMITTEE

May 4, 1957
San Francisco

Members

Mr. Thomas E. Stanton, Jr.
Professor Samuel D. Thurman

Staff

Mr. John R. McDonough, Jr.

STUDY NO. 24 - MORTGAGES FOR FUTURE ADVANCES

The Committee discussed with Mr. Merryman his report, the recommendations made therein, and the revision of Civil Code Sections 2974 and 2975 proposed by him. The Committee makes the following recommendations:

1. That Mr. Merryman's study be accepted and approved for publication by the Commission.

2. That the Commission determine whether a field study of real property mortgages for future advances should be made for the purpose of determining whether the Commission should recommend to the Legislature:

(a) That all advances be given the priority presently accorded obligatory advances;

(b) That all advances be given the priority presently accorded optional advances; or

(c) That if the present distinction between obligatory and optional advances is retained, a mortgage for future advances be required to state that advances to be made thereunder are obligatory in order to have the priority presently accorded to such advances.

3. That the Commission determine whether a similar field study should be made with respect to personal property mortgages for future advances.

4. That if no field study is undertaken the Commission recommend no revision of existing law relating to mortgages for future advances except the following:

(a) That Civil Code Section 2974 be repealed.

(b) That Civil Code Section 2975 be revised to read as follows: *

2975. Mortgages of personal property or crops may be given to secure future advances. If the maximum amount to be secured is stated in the mortgage, the lien for all advances to that amount, whether optional or obligatory, has the same priority as that originally established by the mortgage. If the maximum amount to be secured is not stated, the lien for all optional advances made after actual notice of intervening liens is inferior to them in priority.

The stated maximum amount means the maximum amount secured at any one time, and does not include amounts already

* The proposed revision is shown in strike-out and underline following this statement of Section 2975 as it would read if revised as recommended.

repaid or discharged. Repayment in full of amounts owing under the mortgage does not extinguish the mortgage.

Necessary expenditures made by the mortgagee to preserve the security constitute liens having the same priority as that originally established by the mortgage.

Not in Merryman draft

Within the meaning of this section, future advances means sums to be paid in the future by the mortgagee to the mortgagor or for his account pursuant to the terms of the mortgage.

The following shows the revision of Section 2975 in strike-out and underline:

2975. ~~A mortgage~~ Mortgages of personal property or crops may be given to secure future advances. ~~the repayment of sums that may be advanced, expenditures that may be made, or indebtednesses or obligations that may be incurred subsequent to the execution of such mortgage.~~ If the maximum amount ~~the repayment of which is proposed~~ to be secured ~~by such~~ is stated in the mortgage, ~~is expressed therein (whether the creation of debts in such amount or any part thereof be optional with, or obligatory upon the mortgagee or assigns), such mortgage (subject to the provisions of sections 2911, 2941, 2968, 2969 and 2972 of the Civil Code) shall be and constitute~~ a the lien for all advances to that amount, whether optional or obligatory, has the same priority as ~~or encumbrance of rank, effect, status~~

~~and-standing-equal-to~~ that originally established by the mortgage. If the maximum amount to be secured is not stated, the lien for all optional advances made after actual notice of intervening liens is inferior to them in priority. ~~thereby-initially-and-as-it-may thereafter-obtain,-as-security-for-the-repayment-of-any-sums, expenditures,-indebtednesses-and-obligations,-owing-or-due-or becoming-owing-or-due-thereunder,-up-to-and-including-such-expressed-maximum-amount-which-shall-be-considered-only-as-a-limit-of-the debts,-sum,-expenditures,-indebtednesses-and-obligations-that-may be~~

The stated maximum amount means the maximum amount secured ~~thereby~~ at any one time, and does not ~~to~~ include ~~such-as-may-have existed~~ amounts already ~~and-been~~ repaid or discharged ~~thereunder.~~ Repayment in full of amounts owing under the mortgage does not extinguish the mortgage. ~~A-mortgage-of-personal-property-or-crops shall-also-constitute-a-lien-or-encumbrance-of-rank,-effect,-status and-standing-equal-to-that-established-initially-or-thereafter obtained-thereby,-as-security-for-the-repayment-of-all-sums-or amounts-that-are-necessarily-advanced-or-expended-by-the-mortgagee-or-assigns,-for-the-maintenance-or-preservation-of-the-property, or-any-part-thereof,-described-in-such-mortgage.~~

Necessary expenditures made by the mortgagee to preserve the security constitute liens having the same priority as that originally established by the mortgage.

Within the meaning of this section, future advances means sums to be paid in the future by the mortgagee to the mortgagor or for his account pursuant to the terms of the mortgage.

STUDY NO. 23 - RESCISSION OF CONTRACTS

At the beginning of the discussion Professor Lawrence Sullivan distributed copies of a lengthy outline of his proposed study on this subject. He then outlined orally a number of the points covered in the outline. Several of these points were discussed at some length. It was agreed that the members of the Committee and the Executive Secretary would read and discuss Mr. Sullivan's outline and that the Executive Secretary would then communicate to him any suggestion which we might have concerning the study. Mr. Sullivan expressed his intention of completing the study at a relatively early date.

STUDY NO. 33 - SURVIVAL OF TORT ACTIONS

Mr. Stanton was unable to be present during this part of the meeting. Mr. Thurman and the Executive Secretary discussed with Mr. Killion the legislative history of survival of tort actions in California and a number of questions relating to the study which were raised by Mr. Killion. Mr. Killion expressed the view that all tort actions should survive but that the estate should not have a right to recover any element of damages (such as pain and suffering) which the decedent might have recovered had he survived but which did not result in diminution of the estate. Mr. Killion was given a rough outline of the points which it was suggested might be covered in the study. There was discussion of a completion date but none was decided upon. However, Mr. Killion stated that he would like to complete the study within the next month.

Respectfully submitted,

John R. McDonough, Jr.
Executive Secretary