#D-39.200 5/17/78

Memorandum 78-35

Subject: Study D-39.200 - Enforcement of Judgments (Comprehensive Statute--Retroactive Application of Exemptions)

The question of the retroactive application of exemptions has arisen at several prior Commission meetings. This memorandum presents some background material on this issue and proposes a section (which would be added to Chapter 7 of the Enforcement of Judgments Law) to deal with the problem.

Background

California decisions have consistently held that to grant a new or increased exemption in the process of enforcement of a contractual obligation that was incurred before the change in the exemption would violate the Contract Clause of Article 1, Section 10 of the United States Constitution and Article 1, Section 9 of the California Constitution. See In re Rauer's Collection Co., 87 Cal. App.2d, 248, 253-54, 196 P.2d 803 (1948) (increase in homestead exemption) (attached as Exhibit 1); Daylin Medical & Surgical Supply, Inc. v. Thomas, 69 Cal. App.3d Supp. 37, 41-42, 137 Cal. Rptr. 826 (1977) (time for claiming dwelling exemption extended); Smith v. Hume, 29 Cal. App.2d Supp. 747, 749, 74 P.2d 566 (1937) (new motor vehicle exemption); Medical Fin. Ass'n v. Wood, 20 Cal. App.2d Supp. 749, 751, 63 P.2d 1219 (1936) (new motor vehicle exemption). Early decisions of the federal courts sitting in California reached similar conclusions. See The Queen, 93 F. 834 (N.D. Cal. 1899) (seamen's earnings exemption); In re Fox, 16 F. Supp. 320 (S.D. Cal. 1936) (motor vehicle exemption). This rule has also been applied in bankruptcy cases with the result that the debtor is restricted to the exemption in effect at the time of the earliest of scheduled debts. See England v. Sanderson, 236 F.2d 641, 643 (9th Cir. 1956), rev'g In re Sanderson, 134 F. Supp. 484, 485 (N.D. Cal. 1955); In re Towers, 146 F. Supp. 882, 885-86, aff'd sub nom. Towers v. Curry, 247 F.2d 738, 739 (9th Cir. 1957).

The later of these cases almost completely ignore the gradual erosion of the rigid application of the Contract Clause by the United States Supreme Court beginning in Home Building & Loan Association v. Blaisdell, 290 U.S. 398 (1934), which upheld the Minnesota Mortgage

Moratorium Law. California decisions concerning the retroactive application of revisions in the community property and sovereign immunity laws have engaged in a more modern, sophisticated analysis of the constitutional issues. See, e.g., Robertson v. Willis, 77 Cal. App.3d 358, 367-69, __ Cal. Rptr. ___ (1978) (community property); Flournoy v. State of California, 230 Cal. App.2d 520, 530-37, 41 Cal. Rptr. 190 (1964) (sovereign immunity). These cases have applied a balancing approach, relying heavily on the analysis developed in Hochman, The Supreme Court and the Consitutionality of Retroactive Legislation, 73 Harv. L. Rev. 692 (1960). See also Reppy, Retroactivity of the 1975 California Community Property Reforms, 48 So. Cal. L. Rev. 977 (1975). Although the particular interests in these cases differ to some extent from the interests in the exemption cases, it is still surprising that the courts have adhered to a rigid interpretation of the Contract Clause and vested rights doctrine when the question of retroactive application of exemptions arises.

Recent decisions in at least two other states have recognized the erosion of the Contract Clause and upheld the retroactive application of increased exemptions to preexisting debts. In Hooter v. Wilson, 273 So.2d 516 (La. 1973), the Louisiana Supreme Court reasoned:

> It may be said in relation to the garnishment exemptions that the creditor not only read into the contract the statutory exemptions provided at the time of the contract, but necessarily read into that exemption law the right of the state in the exercise of its police power to change the exemptions for the protection of the welfare of the people of this state. . . .
>
> . . . There was no vested contractual obligation that this particular debtor would have wages available for the remedy of garnishment if he failed to pay the debt. When the state changed the remedy by increasing the exemption, it did not abrogate the remedy; it did not make the remedy any less certain than it was at the time of the contract; it simply in the interest of public welfare increased the debtor's exemption so that he and his family might be saved from being a charge upon the state. [273 So.2d at 521-22; citations omitted]

The court also noted that the creditor could have availed himself of other remedies at the time the contract was made, such as a chattel mortgage or conditional sale.

The Louisiana Court of Appeal followed Hooter in Ouachita Nat'l Bank v. Rowan, 345 So.2d 1014 (La. Ct. App. 1977) and applied a homestead exemption which was increased between the time the obligation was

incurred and the time the judgment was rendered under which levy took place. The court held that there was no impairment of a contract and that even if there was the impairment was justified by the economic interest of the state. Accord Natchitoches Collections, Inc. v. Gorum, 274 So.2d 449 (La. Ct. App. 1973).

The Oregon Supreme Court held in Wilkinson v. Carpenter, 277 Or. 557, 561 P.2d 607 (1977), that the amount of the homestead exemption should be determined at the time of sale. A copy of this opinion is attached hereto as Exhibit 3. The court noted the changed interpretation of the Contract Clause after Blaisdell and followed a balancing approach. The Oregon court followed Hooter in reasoning that the state had a reserved power to increase statutory exemptions for the protection and welfare of its people, stating that "[s]o long as the increase is reasonable and does not destroy the value of the contract by destroying any meaningful remedy, it does not violate the contract clause." 561 P.2d at 611. The court found that the increase from $7,500 to $12,000 was not unreasonable in light of current economic conditions.

Most commentators urge the views set forth in these recent decisions. See, e.g., Countryman, For a New Exemption Policy in Bankruptcy, 14 Rutgers L. Rev. 678, 726-32 (1960); Reppy, Retroactivity of the 1975 California Community Property Reforms, 48 So. Cal. L. Rev. 977, 1120 n.470 (1975); Comment, 1 Stan. L. Rev. 350 (1949); Note, 68 Yale L.J. 1459, 1471-72 (1959). A copy of the Stanford Law Review Comment is attached as Exhibit 2.

Similarly, Section 23(b) of the Uniform Exemptions Act also would apply exemptions retroactively:

> All provisions of this Act apply to the collection of claims arising before and after the effective date and to the enforcement of judgments rendered or entered before and after that date, but do not govern a levy made before that date.

It should be apparent from the foregoing discussion that the staff is of the opinion that exemptions should be applied to preexisting contracts. Despite the recently decided Daylin case, cited supra, we believe that the California Supreme Court would be likely to follow the Louisiana and Oregon courts if confronted with an explicit legislative determination that exemptions should apply to preexisting contracts.

Alternatives

Constitutional arguments aside, the staff believes that it is clearly undesirable to restrict a debtor to the exemptions in effect at the time an obligation is incurred. We see no reason to treat debtors whose property is being levied upon in 1980 differently because one was sued under a 1975 contract and another under a 1960 contract. Exemptions are increased and added primarily to take account of inflation and increased prices and also to recognize the increasing importance of certain types of assets, such as retirement benefits. This purpose is largely frustrated if the time of contracting is determinative of exemption rights.

There are three alternative times at which the applicable exemptions may be determined: the time judgment is entered, the time a lien is created on the property claimed as exempt, and the time the exemption is claimed.

From a policy standpoint, the staff believes that the ideal time for determining the applicable exemptions is the time when the exemption is claimed. This policy is in accord with the notion that legislative increases in and additions to exemptions should be made as effective as possible. It is also easy to administer because the court determining exemptions need not look to some prior time to find the applicable exemptions. However, the vested rights doctrine would probably invalidate such an approach. Prior to the acquisition of a lien, the unsecured judgment creditor has no right to specific property of the debtor. The acquisition of a lien in effect elevates the creditor to the status of a secured creditor. See S. Riesenfeld, Creditors' Remedies and Debtors' Protection 54 (2d ed. 1975). Although the same analysis was applied under the vested rights doctrine as under the Contract Clause in Blaisdell and in other cases such as Robertson v. Willis, supra, involving the retroactive application of the community property reforms, we think it unlikely that the courts would hurdle the Contract Clause and also override the centuries-old respect for liens.

The staff considers the alternative of tying exemptions to the time of entry of the judgment to be undesirable. It is an easily administered alternative, since the time judgment was entered is certain and easy to

ascertain, but serious inequities akin to those arising under existing law would occur because a judgment may be enforced under the draft statute for 20 years.

The staff recommends that the applicable exemptions be determined at the time a lien is obtained on the property claimed as exempt. This policy is consistent with the Uniform Exemptions Act and the recent decisions in Louisiana and Oregon and respects the importance of the lien acquired by the judgment creditor. When a lien has been acquired, the creditor has an expectation that the property will be available for the satisfaction of the judgment. The only drawback of this approach is that the time of acquisition of a lien may vary from item to item so that the determination of the applicable exemption at the hearing on the exemption claim will be more cumbersome, though not necessarily difficult. It should also be noted that an exemption in effect prior to judgment may be applicable under this alternative because the postjudgment lien may relate back to the acquisition of an attachment lien. We do not view this as a serious problem, however, because attachment of the property of individuals is now quite restricted and because there are additional exemptions available in attachment.

Proposed Section

The staff proposes the adoption of the following provision:

> 707.___. (a) The determination of whether property is exempt or of the amount of an exemption shall be made pursuant to the exemption statutes in effect at the time the judgment creditor acquires a lien on the property for which an exemption is claimed.
>
> (b) All contracts shall be deemed to have been made in recognition of the power of the state to alter and to make additions to statutes providing exemptions from the enforcement of money judgments.
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> Comment. Section 707.___ is new. Subdivision (a) rejects the case law rule that the judgment debtor could take advantage of only the exemptions in effect at the time an obligation was incurred. See, e.g., In re Rauer's Collection Co., 87 Cal. App.2d 248, 253-54, 196 P.2d 803, ___ (1948); Daylin Medical & Surgical Supply, Inc. v. Thomas, 69 Cal. App.3d Supp. 37, 41-42, 137 Cal. Rptr. 826, ___ (1977); Smith v. Hume, 29 Cal. App.2d Supp. 747, 749, 74 P.2d 566, ___ (1937); Medical Fin. Ass'n v. Wood, 20 Cal. App.2d Supp. 749, 751, 63 P.2d 1219, ___ (1936).
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> Subdivision (b) reserves the power of the state to change and add to existing exemptions in line with recent decisions in other

jurisdictions. See, e.g., Wilkinson v. Carpenter, 277 Or. 557, 561 P.2d 607 (1977); Hooter v. Wilson, 273 So.2d 516 (La. 1973).

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

Exhibit 1

Excerpt from In re Rauer's Collection Co., 87 Cal. App. 2d 248, 196 P.2d 803 (1948).

APPEAL from an order of the Superior Court of San Mateo County denying petition to levy execution on a homestead. Aylett R. Cotton, Judge. Reversed with directions.

Jerome L. Schiller for Appellant.

Frank V. Kington for Respondents.

BRAY, J.—The superior court made an "Order Denying Petition to Levy Execution on Homestead" in a proceeding brought under the provisions of sections 1245 to 1258, inclusive, of the Civil Code. The petitioner therein appeals. The questions raised concern the effect of a certain declaration of homestead upon the property of respondents, who at all times herein mentioned were, and are, husband and wife.

In 1937, respondents Claude C. Higgins and Anna Higgins purchased with community funds certain real property in San Mateo County. The deed, dated July 28, 1937, and recorded December 4, 1937, conveyed the property to them as *joint tenants*, with the right of survivorship. Thereafter and on August 14, 1939, both respondents signed, and on August 15th recorded, a declaration of homestead on this property. The declaration states that Claude Higgins and Anna Higgins are husband and wife; that Claude is the head of a family, consisting of himself, his said wife, and their three minor children, all actually residing on the land (describing it); that it is their intention to use it as a home, and that they claim it, together with the dwelling house thereon, as a homestead; that the actual cash value of the premises is estimated to be $4,500; and that all of it is necessary for the use and enjoyment of the homestead; "That the character of said property sought to be homesteaded is as follows: That the said real property is *the Community property in Joint-Tenancy* of the Declarants. . . ." (Emphasis added.) No attack is made upon the validity of the declaration.

In 1940, petitioner, on an assigned claim, brought suit in the Superior Court of San Mateo County against respondent Claude Higgins. On December 10, 1945, judgment for approximately $950 was rendered in favor of petitioner and against Claude. On appeal to this court, the judgment was affirmed.[1] On February 6, 1946, an abstract of the judgment was recorded in San Mateo County, and on July 16, 1947, execution was levied by the sheriff on the homesteaded property. The same day, petitioner, pursuant to the provisions of section 1245 of the Civil Code, applied to the superior court for the appointment of appraisers to value the property. Respondent Anna Higgins appeared and answered the petition, setting forth that she was not a party to the judgment; that the property was held in joint tenancy by her and Claude; that its value was less than $6,000; that it could not be divided without material injury to it; and asked that the petition be denied.

The court duly appointed three appraisers. On September 23, 1947, their reports were filed. They found that there were no liens or encumbrances of record and that the property could not be divided without material injury. No challenge of these findings is made. Two of the appraisers valued the property at $5,850, the third at $4,775. On September 29th, petitioner moved the court to adopt the majority report of the appraisers and to direct a sale of the property under the writ of execution. This motion was resisted by respondent Anna. The court, in its order, found that the property was held in joint tenancy and "that the actual cash value of said real property is less than $6000." It then denied the petition.

AMOUNT OF EXEMPTION

The first question to be determined is the amount of homestead exemption to be allowed. In 1939, when the homestead was declared, section 1260 of the Civil Code provided that

[1] (*Rauer's Law etc. Co. v. Higgins*, 75 Cal.App.2d 804 [174 P.2d 480].)

the homestead exemption of the head of a family was $5,000 over liens and encumbrances at the time of any levy. In 1945, section 1260 was amended to allow an exemption of $6,000. Respondents contend, and the court apparently agreed, that the exemption to be applied is that of the date of recording the abstract of judgment, or $6,000. Petitioner contends that it is that of the date of incurring the indebtedness. The record on this appeal fails to disclose the date of the incurring of the indebtedness upon which this litigation is based. However, in the record before this court in the former appeal (see footnote, p. 324) of which record this court may take judicial notice, the trial court found that an account was stated between the parties on June 2, 1939. At that time, as well as at the time of recording the declaration and in fact ever since 1872, the amount of homestead exemption for the head of a family was $5,000.

The question of the effect as to creditors then existing of an increase in the amount of the statutory homestead exemption has not been passed upon heretofore in this state. In the case of *Cohen* v. *Davis*, 20 Cal. 187, the court was considering the effect of an amendment in 1860 of the homestead laws of 1851. It held that to avail himself of the provisions of the later act it was necessary for an owner who had previously filed a declaration of homestead to file a new one after the 1860 act took effect, and that as the owner had failed to file such new declaration, his rights were measured by the earlier act. *Gluckauf* v. *Bliven*, 23 Cal. 312, is to the same effect. The holdings in both cases, however, are based upon the express wording of the act, which, in effect, stated that all persons holding homesteads had one year in which to file the new declaration of homestead provided by the act.

In *McNabb* v. *Byrnes*, 92 Cal.App. 337 [268 P. 428], the court was considering a complaint based upon a declaration of homestead made in 1922. Objection was made that the declaration did not contain a statement that no former declaration of homestead had been made by the parties. In 1927, section 1263 of the Civil Code had been amended providing a new subdivision (5) which permitted such a statement to be made in the declaration. After holding that this was not a mandatory requirement, the court held that subdivision (5), which had been added after the declaration of homestead had been recorded, was "not retroactive in its effect." (P. 342.)

[1] That the increase in exemption cannot be given a retroactive interpretation, as it would be an impairment of the obligation of contracts, and that the creditor is entitled to rely upon the exemption statutes as of the time the obligation was incurred, is well established. *Medical Finance Assn. v. Wood*, 20 Cal.App.2d Supp. 749 [63 P.2d 1219], and *Smith v. Hume*, 29 Cal.App.2d Supp. 747 [74 P.2d 566], dealt with the enactment in 1935 of section 690.24 of the Code of Civil Procedure, making a motor vehicle of a value less than $100 exempt from execution. No such exemption had theretofore existed. In both cases it was held that to give a retroactive effect to this statute would be in violation of the state and federal Constitutions, as it would impair the obligation of contracts.

In *The Queen*, 98 F. 834, it was held that a California statute exempting from execution seamen's wages not exceeding $100, "as applied to previous contracts made with seamen, at a time when no such exemption is allowed, would materially lessen and impair the obligation of such contracts." (P. 837.) See also *In re Fox*, 16 F.Supp. 320, and Waples on Homestead and Exemption (1892), pp. 227-229.

" 'It is settled that every statute will be construed to operate prospectively unless the legislative intent to the contrary is clearly expressed. . . . The rule that a statute is presumed to operate prospectively only, unless an intent to the contrary clearly appears, is especially applicable to cases where retroactive operation of the statute would impair the obligations of contracts or interfere with vested rights.' (*Jones v. Union Oil Co.* (1933), 218 Cal. 775, 777, 778 [25 P.2d 5, 6]; to same effect *People v. Allied Architects Assn.* (1927), 201 Cal. 428, 437 [257 P. 511].) . . .

"But even if a retroactive intent can be found in the statute, the application of the new exemption to executions issued on judgments based on preexisting contracts is prevented by the provisions of the Constitutions of the United States (art. I, sec. 10) and of California (art. I, sec. 16), forbidding laws impairing the obligation of contracts. . . . Statutory provisions creating new, or increasing old, exemptions have been considered several times by the United States Supreme Court, and it has uniformly held that their application to executions based on preexisting contracts would violate the provision of the federal Constitution above referred to. (*Gunn v. Barry* (1873), 15 Wall. 610 [21 L.Ed. 212]; *Edwards v. Kearsey*

(1878), 98 U. S. 595 [24 L.Ed. 793]; *Bank of Minden* v. *Clement* (1921), 256 U. S. 126 [41 S.Ct. 408, 65 L.Ed. 857]; *W. B. Worthen Co.* v. *Thomas* (1934), 292 U. S. 426 [54 S.Ct. 816, 78 L.Ed. 1344, 93 A.L.R. 173].)" (*Medical Finance Assn.* v. *Wood*, *supra* [29 Cal.App.2d Supp. 749, 750, 751].)

"While it is competent for the legislature to change the form of remedy, if it can do so without impairing the obligation of contract, a statute increasing the exemption of debtors is void to the extent that it is applicable to contracts made prior to its enactment." (12 Cal.Jur., p. 333.)

93 American Law Reports, page 178 states that "the now generally accepted view" is that the remedy is inseparable from the contract itself, and contracts not reduced to judgment are held to be substantially impaired by the authorization of a new or increased exemption.

[2] As a prospective and not a retroactive interpretation must be given to the 1945 amendment to section 1260, it is obvious that the exemption to which respondents are entitled is that which was in existence at the time of the creation of the debt upon which the judgment is founded, namely, $5,000.

Mention is made by respondents of the amendment of section 1260 in 1947, raising the homestead exemption to $7,500. This, like the 1945 amendment, cannot be given a retroactive effect so far as petitioner is concerned.

In holding that the amendment is not retroactive, we expressly are not holding, as petitioner would have us do, that to avail themselves of the increased exemption as to debts created, or contracts entered into, after the effective date of the amendment, it is necessary for the property owners who theretofore filed declarations of homestead to file new declarations.

Exhibit 2

Comment, 1 Stan. L. Rev. 350 (1949)

Contracts Clause Prevents Exemption Change

CREDITORS' RIGHTS — EXEMPTION STATUTES — INCREASED HOMESTEAD EXEMPTION UNCONSTITUTIONAL IF APPLIED RETROACTIVELY. — In 1939, Claude Higgins became indebted to plaintiff's assignor. In that same year, Higgins and his wife recorded a declaration of homestead on property they had previously purchased. At that time the homestead exemption of the head of a family was $5,000.[1] Plaintiff brought suit against Higgins in 1940 on the assigned claim. Effective September 15, 1945, the legislature increased the exemption to $6,000.[2] Plaintiff was awarded judgment for approximately $950 on December 10, 1945. This judgment was affirmed in 1946,[3] and execution was levied on the homestead property in 1947. Plaintiff, as judgment creditor, petitioned to have the homestead property sold under the writ of execution.[4] The trial court denied the petition because it found the value of the homestead property was under $6,000. On appeal, *held*, the 1945 amendment which increased the amount of the homestead exemption cannot be applied retroactively. To determine the applicable homestead exemption, the court must look to the exemption in force when the debt was incurred. In re *Rauer's Collection Co.*, 87 Adv. Cal. App. 321, 196 P.2d 803 (1st Dist. 1948).

Denial of retroactive effect to the amendment which enlarged the homestead exemption seems to defeat the attempt of the legislature to keep abreast of inflation. It is important to consider whether the court or the legislature might have applied this section of the Civil Code to pre-existing debts.

The court reasoned that to give the amendment retroactive operation would violate state and national constitutional provisions forbidding state impairment of the obligations of contracts. The courts have not always held this way. In a dictum in an early case,[5] Chief Justice Taney said, "a state may regulate . . . . the modes of proceeding in its courts in relation to past contracts . . . .

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1. CAL. CIV. CODE § 1260 (Deering, 1941).

2. CAL. CIV. CODE § 1260 (Deering, Supp. 1945).

3. Rauer's Law & Collection Co. v. Higgins, 76 Cal. App.2d 854, 174 P.2d 450 (1st Dist. 1946).

4. CAL. CIV. CODE § 1245 (Deering, 1941) prescribes the procedure to be followed in reaching the value of the property in excess of the homestead exemption.

5. Bronson v. Kinzie, 1 How. 311 (U.S. 1843).

according to its own views of policy and humanity."[6] Relying on this dictum, several courts gave retroactive effect to statutes that increased exemptions.[7] But in 1872, in the case of *Gunn v. Barry*,[8] the Supreme Court of the United States held such a Georgia statute unconstitutional. The Court said this legislation involved the impairment of a substantial right and was "to that extent utterly void."[9] The Court reasoned that the legal remedies for the enforcement of a contract, which exist at the time and place where it is made, are a part of its obligation. *Edwards v. Kearzey*,[10] decided in 1877, reaffirmed the doctrine of *Gunn v. Barry* and repudiated the dictum of Chief Justice Taney. Since then, both federal and state courts have held increased or newly created exemptions to impair the obligation of contract, if applied retroactively.[11]

It may be argued that the theory underlying *Gunn v. Barry* is unsound. The obligations of a contract are those things the parties agree to do. Unless the debtor agrees to subject his property to the payment of his debts, as by mortgage or pledge, the contract imposes no obligation on the property.[12] Until the creditor has reduced his claim to judgment, there is a mere personal obligation on the part of the debtor, and his property is not obligated in any way.[13] Since exemption laws operate on the property of the debtor and do not in any way affect his personal obligation, they cannot be said to impair the obligation of contract. They apply only to the relief which the creditor may get by virtue of his judgment. The conclusion is that exemption laws are merely procedural.

6. *Id.* at 315.

7. Snelder v. Heidelberger, 45 Ala. 126 (1871); Hardeman v. Downer, 39 Ga. 425 (1869); Cunic v. Douglas, 3 Kan. 123 (1865); Hill v. Kesler, 63 N.C. 426 (1869); Morse v. Goold, 11 N.Y. 281 (1854).

8. 15 Wall. 610 (U.S. 1872).

9. *Id.* at 623.

10. 96 U.S. 595 (1877).

11. E.g. W. B. Worthen Co. v. Thomas, 292 U.S. 426 (1934) (exemption of insurance proceeds); Bank of Minden v. Clement, 256 U.S. 126 (1921) (exemption of insurance proceeds); *In re* Fox, 16 F. Supp. 320 (S.D. Cal. 1936) (automobile exemption denied in bankruptcy); The Queen, 93 Fed. 834 (N.D. Cal. 1899) (exemption of wages); Medical Finance Ass'n v. Wood, 26 Cal. App.2d Supp. 749, 63 P.2d 1219 (Cal. Super. 1936) (exemption of personalty); Harrington v. Godbee, 157 Ga. 343, 121 S.E. 312 (1924) (homestead exemption).

12. GLENN, THE RIGHTS AND REMEDIES OF CREDITORS RESPECTING THEIR DEBTOR'S PROPERTY § 3 (1915).

13. 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES §§ 9, 13 (rev. ed. 1940); GLENN, *op. cit. supra* note 12, § 7.

Cases which involve conflict of laws support this argument.[14] Where a contract is made in one state and the creditor sues in another,[15] almost all courts hold that the exemption law of the forum applies.[16] This is so whether the law of the forum allows a greater[17] or lesser[18] exemption than does the place where the contract is made and is to be performed.[19] These cases are inconsistent with the doctrine of *Gunn v. Barry*. They are based on the theory that "exemption laws are *not* part of the contract; they are part of the remedy and subject to the law of the forum."[20] Contrary to this, the Court said in both *Gunn v. Barry*[21] and *Edwards v. Kearzey*[22] that exemption laws *are* part of the contract and that the proper remedy is that of the state where the contract was made. In short, the conflicts cases treat exemption laws as procedural, while *Gunn v. Barry* treats them as substantive.

The distinction between matters of substance and matters of procedure obviously may be based on a difference of degree; what is regarded as procedural in one instance may be regarded as substantive in another.[23] Nevertheless, this does not justify the divergence of result in the above cases: the parties and their relationship to each other are identical. The creditor's remedy is impaired just as effectively in the conflicts situation as it is when an exemption increase is applied retroactively. There is no reason why exemption statutes cannot be regarded as procedural in their application to pre-existing contracts.

But enticing as it is to argue that the debtor has only a personal obligation which is not affected by a changed exemption, there are strong arguments the other way. A creditor has "a common natural right to collect his debt by subjecting his debtor

14. Chicago, R.I. & Pac. Ry. v. Sturm, 174 U.S. 710 (1899); Sanders v. Fertilizer Works, 292 U.S. 190 (1934); Merchants Bank v. Weaver, 213 N.C. 767, 197 S.E. 551 (1938). *But cf.* State *ex rel.* Fulton v. Heinrich, 48 Ohio App. 455, 194 N.E. 395 (1934).

15. A domestic creditor who proceeds against a domestic debtor in a foreign jurisdiction with intent to avoid domestic exemption laws may be enjoined. Griggs v. Docter, 89 Wis. 161, 61 N.W. 761 (1895).

16. Stumberg, Conflict of Laws 130, note 17 (1937). Restatement, Conflict of Laws § 600 (1934) "The law of the forum determines matters pertaining to . . . . what property of a judgment defendant within the state is exempt from execution."

17. Pinson v. Murphy, 220 Ky. 464, 295 S.W. 442 (1927).

18. Chicago, R.I. & Pac. Ry. v. Sturm, 174 U.S. 710 (1899).

19. Minor, Conflict of Laws § 209 (1901).

20. Chicago, R.I. & Pac. Ry. v. Sturm, 174 U.S. 710, 717 (1899).

21. 13 Wall. 610 (U.S. 1872).

22. 96 U.S. 595, 607 (1877).

23. Sampson v. Channell, 110 F.2d 754 (C.C.A. 1st 1940).

to due process of law."[24] This is true even though he has no claim against his debtor's property until his debt is reduced to judgment. That right would be worthless if it could not be enforced by recourse to the debtor's property. This right can be protected by reading into the contract the means of enforcement existing at the time the contract is made.

Another solution to the problem, not inconsistent with *Gunn v. Barry*, is suggested by the *Minnesota Mortgage Moratorium* case.[25] There the Supreme Court upheld the validity of an emergency statute extending the redemption period of existing mortgages. The Court reasoned that the state has a reserved power to protect the interest of its people; an emergency may furnish the occasion for an exercise of this power, and an economic crisis threatening the people's loss of homes and lands which furnish shelter and support is such an emergency. The principle established by this decision has not been confined to mortgage cases. On the strength of it, a Federal District Court in Iowa held constitutional a statute[26] that temporarily increased exemptions and applied them to pre-existing contracts.[27] And in 1945, the Supreme Court enunciated that a "governing constitutional principle"[28] was derived from the *Mortgage Moratorium* case and cases following it:[29] "When a widely diffused public interest has become enmeshed in a network of multitudinous private arrangements, the authority of the State to safeguard the vital interests of its people is not to be gainsaid by abstracting one such arrangement from its public context and treating it as though it were an isolated private contract constitutionally immune from impairment."[30]

This theory reduces the problem to a balancing of the interests of the community against the sanctity of contracts. In striking this balance the legislation must be reasonably limited and ap-

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24. 1 GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES § 7 (rev. ed. 1940).

25. Home Building and Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934), 34 COL. L. REV. 361, 47 HARV. L. REV. 650, 32 MICH. L. REV. 545.

26. Iowa Laws 1933, c. 177.

27. *In re* Durband, 8 F. Supp. 65 (N.D. Iowa 1934).

28. East N.Y. Savings Bank v. Hahn, 326 U.S. 230, 232 (1945).

29. Faitoute Iron and Steel Co. v. Asbury Park, 316 U.S. 502 (1942); Gelfert v. National City Bank, 313 U.S. 221 (1941); Veix v. Sixth Ward Ass'n, 310 U.S. 32 (1940); Honeyman v. Jacobs, 306 U.S. 539 (1939).

30. See note 28 *supra*.

propriate to the inducing cause." The statute in the principal case would meet these requirements if the legislature were to make it a temporary emergency measure. While the moratorium law was the product of the depression, and the exemption increase in the principal case was a product of inflation, the purpose of both statutes was the same—to prevent widespread loss of homes by families unable to cope with economic problems not of their own making." Since the courts continue to follow *Gunn v. Barry*, the legislature should recognize this possible method of protecting present debtors from the loss of their homes due to inflated real estate prices."

Exhibit 3

277 Or. 857

Kenneth R. WILKINSON and Gladys D. Wilkinson, husband and wife, Appellants,

v.

Crystal R. CARPENTER and William D. Carpenter, Respondents.

Supreme Court of Oregon, Department 1.

Argued and Submitted Jan. 7, 1977.

Decided March 17, 1977.

Judgment creditors moved to set amount of homestead exemption in realty subject to execution. The Circuit Court, Multnomah County, Clifford B. Olsen, J., set the amount in accordance with amendment increasing amount of exemption and creditors appealed. The Supreme Court, Howell, J., held that amendment applied to prior judgment and did not unconstitutionally impair obligation of contract.

Affirmed.

1. **Homestead** ⇐7

Statute increasing amount of homestead exemption applied where notice of exemption claim and execution sale took place following its enactment, although judgment preceded its enactment. ORS 23.240.

2. **Homestead** ⇐4

Homestead exemption is proper subject for legislative action and is intended not only to insure indigent individuals comforts of home but also to protect general economic welfare of all citizens, creditors and debtors alike, by promoting stability and security of society. ORS 23.240.

3. **Constitutional Law** ⇐180
Homestead ⇐4

Statute increasing homestead exemption did not, as applied to prior judgment, unconstitutionally impair obligation of contracts, since increase from $7,500 to $12,000 was reasonable and any impairment did not appear to be substantial when balanced against governmental object pursued. ORS

23.240; Const. art. 1, § 21; U.S.C.A.Const. art. 1, § 10, cl. 1.

Warren C. Deras, Portland, argued the cause and filed a brief for appellant.

Mark M. McCulloch of Powers & McCulloch, Portland, argued the cause and filed a brief for respondent.

Before DENECKE, C. J., and HOWELL, LENT and BRADSHAW, JJ.

HOWELL, Justice.

Plaintiffs filed a motion for an order setting the amount of the homestead exemption claimed by defendants in certain real property which was subject to execution in satisfaction of plaintiffs' prior judgment against defendants.[1] After a hearing, the court set the amount of the homestead exemption at $12,000. Plaintiffs appeal, claiming that the amount of the allowable homestead exemption should have been set at $7,500, as provided in ORS 23.240 as of the date of the prior judgment, rather than at $12,000 as provided by the same statute as amended effective September, 1975.

The facts are not in dispute. On August 6, 1975, a decree was entered granting plaintiffs a judgment against defendants for sums exceeding $155,000. The obligation giving rise to this judgment was a contract entered into between plaintiffs and defendants on October 6, 1973. On September 13, 1975, the statute increasing the homestead exemption to $12,000 became effective. On January 6, 1976, a writ of execution was levied upon defendants' real property. On January 21, 1976, defendants filed a notice of claimed homestead exemption. On February 10, 1976, the property was sold to plaintiffs on execution for $140,000. The next day plaintiffs filed their motion for an order setting the amount of the homestead exemption.

On appeal from the order entered on their motion, plaintiffs contend that the statute increasing the homestead exemption to $12,000 should not be construed to apply to an execution on a judgment entered prior to its effective date, and that if the statute is construed to apply to such a judgment, it would be an unconstitutional impairment of the obligation of contracts under Article I, Section 10, of the United States Constitution.

The applicable part of the statute increasing the homestead exemption provided as follows:

"Section 5. ORS 23.240 is amended to read:

"23.240. (1) A homestead shall be exempt from sale on execution, from the lien of every judgment and from liability in any form for the debts of the owner to the amount in value of [$7,500] $12,000, except as otherwise provided by law. When two or more members of a household are debtors whose interests in the homestead are subject to sale on execution, the lien of a judgment or liability in any form, their combined exemptions under this section shall not exceed $12,000. The homestead must be the actual abode of and occupied by the owner, his spouse, parent or child, but such exemption shall not be impaired by:

"(a) Temporary removal or temporary absence with the intention to reoccupy the same as a homestead;

"(b) Removal or absence from the property; or

"(c) The sale of the property.

"(2) The exemption shall extend to the proceeds derived from such sale to an amount not exceeding [$7,500] $12,000 held, with the intention to procure another homestead therewith, for a period not exceeding one year." Oregon Laws 1975, ch. 208, § 5. (New material underscored; old material in brackets.)

This court has previously noted that the homestead statute should be liberally construed in favor of the debtor's exemption. *See, e. g., Fleischhauer v. Bilstad, et al. Gray et ux.*, 233 Or. 578, 591, 379 P.2d 880 (1963). Under the terms of the statute, the judgment debtor's homestead is "exempt from sale on execution," but the exemption

1. *See Wilkinson v. Carpenter*, 276 Or. 311, 554 P.2d 512 (1976).

is not automatic and must be affirmatively asserted before the sale or it is lost. *See* ORS 23.270. *Compare* ORS 23.170. Since the exemption applies to the sale on execution and may be asserted at any time prior to such sale, it would appear that the appropriate time to measure the value of the exemption would be the time of the sale on execution.

[1] In this case, the statute increasing the exemption became effective on September 13, 1975. Notice of defendants' homestead exemption claim was filed on January 21, 1976, and the execution sale took place on February 10, 1976. Under the terms of the statute in effect at that time, defendants were entitled to a homestead exemption of $12,000.

Plaintiff also contends that an application of the increased exemption to an obligation arising under a pre-existing contract would impair the obligation of that contract in violation of Article I, Section 10, of the U.S. Constitution. That section provides that "No state shall * * * pass any * * * law impairing the obligation of contracts." *See also* Oregon Constitution, Art. I, § 21.

Early decisions of the United States Supreme Court often applied the contract clause rigidly to state statutes which made any significant change either in the obligations of pre-existing contracts or in the underlying remedies. *See, e. g., Gunn v. Barry*, 82 U.S. (15 Wall.) 610, 21 L.Ed. 212 (1873); *Edwards v. Kearzey*, 96 U.S. 595, 24 L.Ed. 793 (1878); *Bank of Minden v. Clement*, 256 U.S. 126, 41 S.Ct. 408, 65 L.Ed. 857 (1921).[2]

In *Edwards v. Kearzey*, supra, the Supreme Court held that a state statute which doubled the homestead exemption by raising it from $500 to $1,000 was unconstitutional as an impairment of the obligation of contracts as applied to liabilities incurred on contracts executed prior to the statute. However, we do not believe that the same conclusion must necessarily follow in this case, because it is clear from our review of the more recent Supreme Court decisions in this area that the Court's interpretation of the contract clause has changed significantly since 1878.

In *Home Building & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 54 S.Ct. 231, 78 L.Ed. 413 (1934), the Court conducted a complete reexamination of the contract clause and concluded that "the prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula." 290 U.S. at 428, 54 S.Ct. at 236. The *Blaisdell* Court upheld a state moratorium on mortgage foreclosure sales during the depression years despite the fact that the performance of existing contracts would be frustrated by that moratorium. This was a significant departure from past decisions, and it marked the beginning of a new era in the interpretation of the contract clause. *See generally* G. Gunther, Constitutional Law 611 (9th ed. 1975).

In its most recent discussion of the contract clause, the Supreme Court described the *Blaisdell* case as follows:

"* * * The *Blaisdell* opinion, which amounted to a comprehensive restatement of the principles underlying the application of the Contract Clause, makes it quite clear that '[n]ot only is the constitutional provision qualified by the measure of control which the State retains over remedial processes, but the State also continues to possess authority to safeguard the vital interests of its people. It does not matter that legislation appropriate to that end "has the result of modifying or abrogating contracts already in

2. However, during that same period, exceptions were increasingly carved out of the prohibition when laws passed in the exercise of the "police power" at least arguably impaired the obligations or the remedies of pre existing contracts in the furtherance of the general health, safety and welfare of the people. *See, e. g., Northwestern Fertilizing Co. v. Hyde Park*, 97 U.S. 659, 24 L.Ed. 1036 (1878). *Stone v. State of Mississippi*, 101 U.S. 814, 25 L.Ed. 1079 (1880); *Atlantic Coast Line R. Co. v. Goldsboro*, 232 U.S. 548, 34 S.Ct. 364, 58 L.Ed. 721 (1914). These decisions foreshadowed the shift that later developed toward a more flexible interpretation of the contract clause.

For a general discussion of the use of the term "police power" see Linde, *Without "Due Process,"* 49 Or.L.Rev. 125, 146-58 (1970).

effect." *Stephenson v. Binford*, 287 U.S. 251, 276, 53 S.Ct. 181, 189, 77 L.Ed. 288. Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order. . . . This principle of harmonizing the constitutional prohibition with the necessary residuum of state power has had progressive recognition in the decisions of this Court.' 290 U.S., at 434–435, 54 S.Ct. [231] at 238–239. Moreover, the 'economic interests of the State may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts.' *Id.*, at 437, 54 S.Ct. [231] at 238–239." *El Paso v. Simmons*, 379 U.S. 497, 508, 85 S.Ct. 577, 583–584, 13 L.Ed.2d 446 (1965).

In an earlier decision, *East New York Bank v. Hahn*, 326 U.S. 230, 232, 66 S.Ct. 69, 70, 90 L.Ed. 34 (1945), Justice Frankfurter also reviewed the *Blaisdell* case, as well as subsequent decisions which had considered the contract clause, and he concluded that those cases

"* * * yield this governing constitutional principle: when a widely diffused public interest has become enmeshed in a network of multitudinous private arrangements, the authority of the State 'to safeguard the vital interests of its people,' 290 U.S. at 434, 54 S.Ct. [221], at page 239 is not to be gainsaid by abstracting one such arrangement from its public context and treating it as though it were an isolated private contract constitutionally immune from impairment."

Quoting *Manigault v. Springs*, 199 U.S. 473, 26 S.Ct. 127, 50 L.Ed. 274 (1905), Justice Frankfurter then went on to add that

"the power 'which in its various ramifications is known as the police power, is an exercise of the sovereign right of the Government to protect the . . . general welfare of the people, and is paramount to any rights under contracts between individuals.' 199 U.S. at 480, 26 S.Ct. [127] at page 130. Once we are in this domain of the reserve power of a State we must respect the 'wide discretion on the part of the legislature in determining what is and what is not necessary.' *Ibid.* So far as the constitutional issue is concerned, 'the power of the State when otherwise justified,' *Marcus Brown Co. v. Feldman*, 256 U.S. 170, 198, 41 S.Ct. 465, 486, 65 L.Ed. 877, is not diminished because a private contract may be affected." 326 U.S. at 232–33, 66 S.Ct. at 70.

Therefore, it seems plain that the dictates of the contract clause can no longer be viewed in the same absolute terms which prevailed in earlier times. Modern decisions point out that the prohibition of the contract clause must be balanced against or "harmonized" with the legislative powers reserved to the states:

"* * * [W]hatever is reserved of state power must be consistent with the fair intent of the constitutional limitation of that power. *The reserved power cannot be construed so as to destroy the limitation, nor is the limitation to be construed to destroy the reserved power in its essential aspects. They must be construed in harmony with each other.* This principle precludes a construction which would permit the State to adopt as its policy the repudiation of debts or the destruction of contracts or the denial of means to enforce them." *Home Building & Loan Ass'n v. Blaisdell*, supra 290 U.S. at 439, 54 S.Ct. at 240. (Emphasis added.)

Accord El Paso v. Simmons, supra, 379 U.S. at 509, 85 S.Ct. 577. *See also Cuyahoga Met. Housing Auth. v. Cleveland*, 342 F.Supp. 250, 254 (N.D.Ohio 1972) ("This standard when distilled to its essence is one of reasonableness, or a balancing test." Pursuant to this modern, more flexible approach, state legislation which reflects "the use of reasonable means to safeguard the economic structure upon which the good of all depends," does not violate the contract clause for "the reservation of the reasonable exercise of the protective power of the State is read into all contracts." *Home Building & Loan Ass'n v. Blaisdell*, supra,

290 U.S. at 442, 444, 54 S.Ct. at 242. Under this standard, the real issue is "whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end." *Id.* at 438, 54 S.Ct. at 240. *See also El Paso v. Simmons*, supra, 379 U.S. at 509, 85 S.Ct. at 584:

> "'It is the motive, the policy, the object, that must characterize the legislative act, to affect it with the imputation of violating the obligation of contracts.'" (*Quoting Ogden v. Saunders*, 25 U.S. 12 (Wheat.) 213, 219, 6 L.Ed. 606 (1827).

See generally Hale, *The Supreme Court and the Contract Clause. III*, 57 Harv.L.Rev. 852, 880-84 (1944).

The legislative act in question in this case provided for an increase in the homestead exemption from $7,500 to $12,000. It has been said that the purpose of such exemptions

> "'is to provide a place for the family and its surviving members, where they may reside and enjoy the comforts of home, freed from any anxiety that it may be taken from them against their will, either by reason of their own necessity or improvidence, or *from the importunity of their creditors.*'
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> "* * *
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> "If the homestead rule makes any sense at all, it ought to be flexible enough to allow the value of the homestead to keep pace with the times, and thus in reality, and not in mere fiction, grant the debt ridden and poverty stricken the 'comforts of home.'" *In re Towers*, 146 F.Supp. 882, 885-86, n. 2 (N.D.Cal.1956), *quoting In re Fath's Estate*, 132 Cal. 609, 613, 64 P. 995 (1909). (Emphasis in 146 F.Supp. at 885)

[2] The creation of such exemptions is certainly a proper subject for legislative action. The purpose is not only to insure indigent individuals the comforts of home, but also to protect the general economic welfare of all citizens, creditors and debtors alike, by promoting the stability and security of our society. Periodic increases in such exemptions reflect similar considerations. As the Louisiana Supreme Court recently noted when considering a statutory increase in the garnishment exemption:

> "* * * When the state changed the remedy by increasing the exemption, it did not abrogate the remedy; it did not make the remedy any less certain than it was at the time of the contract; it simply in the interest of public welfare increased the debtor's exemption so that he and his family might be saved from being a charge upon the state." *Hooter v. Wilson*, 278 So.2d 516, 522 (La.1973).

Undoubtedly, any increase in the statutory homestead exemption may impair the value of some pre-existing contracts, at least indirectly, by exempting additional assets from execution and thereby restricting the remedy available for breach. However, if the statutory remedy of sale on execution, ORS 23.410 et seq., is to be read into the contract between the plaintiff and the defendant, the reserved power of the state to increase the statutory exemptions for the protection and welfare of its people must also be included. *El Paso v. Simmons*, supra, 379 U.S. at 508, 85 S.Ct. 577; *Home Building & Loan Ass'n v. Blaisdell*, supra, 290 U.S. at 434-35, 54 S.Ct. 231. So long as the increase is reasonable and does not destroy the value of the contract by destroying any meaningful remedy, it does not violate the contract clause. "In all such cases the question becomes, therefore, one of reasonableness, and of that the legislature is primarily the judge." 290 U.S. at 430, 54 S.Ct. at 237.

[3] We conclude that any indirect contractual impairment which may have occurred as a result of the increased homestead exemption is not unconstitutional since the increase was reasonable, and any impairment would not appear to be substantial when balanced against the governmental objective being pursued. *See El Paso v. Simmons*, supra; *Home Building & Loan Ass'n v. Blaisdell*, supra. *See also Koch v. Yunich*, 533 F.2d 80, 86 (2d Cir. 1976); *Minn. Gas Co. v. Public Service Comm'n*, 522 F.2d 581, 584 (8th Cir. 1975), *cert. denied* 424 U.S. 915 (1976); *Guest v. Fitzpatrick*, 409 F.Supp. 818, 822-24 (E.D.

Pa.1976); *Jamaica Savings Bank v. Lefkowits*, 390 F.Supp. 1357, 1360–1362 (E.D. N.Y.) *aff'd* 423 U.S. 802, 96 S.Ct. 10, 46 L.Ed.2d 29 (1975); *Aerojet-General Corp. v. Askew*, 368 F.Supp. 901, 906–08 (N.D.Fla. 1973), *aff'd* 511 F.2d 710 (5th Cir.), *cert. denied* 423 U.S. 908, 96 S.Ct. 210, 46 L.Ed.2d 137 (1975); *Cuyahoga Met. Housing Auth. v. Cleveland*, supra at 258–59; *California Teach. Assn. v. Newport Mesa Unified Sch. Dist.*, 338 F.Supp. 436, 443–44 (C.D.Cal. 1971); *Hooter v. Wilson*, supra at 520–22.

Moreover, in our view, this result is not necessarily inconsistent with the conclusion reached by the Court in *Edwards v. Kearsey*, supra. The doubling of the exemption in that case from $500 to $1,000 may well have "so affect[ed] that remedy as substantially to impair and lessen the value of the contract" under the economic conditions existing in 1878. 96 U.S. at 607. Indeed, the concurring opinions in *Edwards* specifically distinguished the statute before that Court from statutes directing "'that the necessary implements of agriculture, or the tools of a mechanic, or articles of necessity in household furniture, shall, like wearing apparel, be not liable to execution on judgments.'" 96 U.S. at 610, *quoting Bronson v. Kinzie*, 42 U.S. (1 How.) 311, 315, 11 L.Ed. 143 (1843). In their view, the exemption provided in the case before them was "so large, that, in regard to the mass of contracts and the situation and circumstances of debtors as they are ordinarily found to exist, it would seriously affect the efficiency of remedies for the collection of debts, and that it must, therefore, be held to be void." 96 U.S. at 611. *See also* 96 U.S. at 606.

Like the Supreme Court's interpretation of the contract clause, economic conditions have changed substantially since 1878. In our view, the legislature's action in increasing the homestead exemption from $7,500 to $12,000 was not unreasonable in light of current economic conditions, and certainly the increase was not "so large, that * * it would seriously affect the efficiency of remedies for the collection of debts."

Affirmed.