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Notes

Proposed Changes in Minnesota Mortgage Law

Minnesota presently provides for a one year statutory redemption period after a mortgage foreclosure sale. A number of states have recently shortened their postsale redemption periods and it has been advocated that Minnesota do the same. Also, Minnesota is one of three states which does not enforce an assignment of rents clause, effective at default, when executed contemporaneously with the mortgage instrument. The author of this Note, in considering the need for change in these two aspects of Minnesota mortgage law, examines the basis and policy of the present laws and the effect of the proposed reforms on mortgage lending and the parties involved. He concludes that public policy would be served without substantially prejudicing mortgage debtors if the length of the statutory redemption period were substantially reduced, and that the enforcement of an assignment of rents clause executed contemporaneously with the mortgage instrument is necessary to give the mortgagee adequate security for loans secured by income-producing property.

INTRODUCTION

Many jurisdictions have statutes providing for a lengthy period following foreclosure sales during which a defaulting mortgagor may redeem his mortgaged property. These statutes are designed to afford the mortgagor an adequate opportunity to protect his interest in the property. As will be shown, however, they have served largely to expose mortgage lenders to expense and frustration. Consequently, a number of jurisdictions have recently amended their statutes to shorten the redemption period. Similar

1. See generally 2 Glenn, Mortgages §§ 227–43 (1943); Osborne, Mortgages §§ 307–10 (1951) [hereinafter cited as Osborne].
2. Illinois has shortened its redemption period from 15 months following the time of sale to 12 months from the time of service or six months from the time of sale, whichever is later. Ill. Rev. Stat. ch. 77, § 18e (1963); see Bernard, Legal Aspects of 1961 Mortgage and Redemption Law Legislation in Illinois, 43 Chicago B. Record 229 (1962).

Indiana formerly postponed the foreclosure sale for one year following the filing of the complaint in the foreclosure proceedings. This period has been reduced to six months. Ind. Ann. Stat. § 3–1801 (Supp. 1964).

A 1961 amendment to the Iowa statute permits the parties to agree in the mortgage instrument to a six month postsale redemption period in place of
reduction of Minnesota’s one year period\(^3\) has recently been proposed.

Minnesota also currently prohibits the inclusion in a mortgage instrument of any provision under which all of the rents and profits arising from the mortgaged property after default are assigned to the mortgagee. In this respect, Minnesota differs from other “lien” theory states, the majority of which permit such provisions to enable mortgagees to protect their security between default and foreclosure sale by applying all rents and profits received during this period to the mortgage debt. It is arguable that the Minnesota rule is founded on public policy considerations of dubious validity and that it imposes an unjustifiable risk upon a mortgagee’s security interest.

The purpose of this Note is to discuss and consider proposed

the normal one year period if the mortgagee waives his right to a deficiency judgment and the mortgaged property is less than 10 acres in area. IOWA CODE § 628.26 (1962).

In 1963, Maine’s one year redemption period was shortened to six months. ME. REV. STAT. ANN. ch. 177, §§ 4-A, 7-A (Supp. 1963).

Michigan substantially modified its one year postsale redemption period by a 1964 amendment. The period is now six months for mortgages on commercial and industrial property, multiple dwellings of more than four units, and residential dwellings located on less than three acres of land where the balance due on the mortgage debt is more than 3% of the original loan. MICH. STAT. ANN. § 27A.3240 (Supp. 1964).

Nebraska provides for redemption before sale by staying the order of sale for nine months if the mortgagor requests. This period has been reduced to six months for mortgages with more than 10 years to run on subdivision property or residential property of less than three acres in area, and to three months for similar property where the mortgage will not mature for 20 years or more. NEB. REV. STAT. § 25-1506 (Supp. 1969).

The South Dakota statute, which normally provides for a one year postsale redemption period, was amended in 1963 to allow the parties to agree to a period of 180 days if the property is less than three acres in area S. D. Sess. Laws 1963, ch. 236.

In Washington the postsale period has been reduced to eight months as opposed to 12 if the mortgagee waives his right to a deficiency judgment and the mortgage instrument states that the property is not used for agricultural or farming purposes. WASH. REV. CODE § 6.24.140 (Supp. 1963).

Wisconsin amended its provision which postponed sale for one year following a judgment of foreclosure, shortening the period to six months if, (1) the mortgagee elects in his complaint to waive a deficiency judgment and permit the mortgagor to remain in possession during the period, (2) the mortgage instrument allowed such an election, and (3) the mortgaged real estate is less than three acres in area. WIS. STAT. § 278.101 (1963).

3. MINN. STAT. § 550.23 (1961) provides for a 12 month redemption period following sale under foreclosure by advertisement, and § 551.10 provides for a one year period from the order confirming sale under foreclosure by action.
changes in these two aspects of Minnesota mortgage law in the light of legal theory, practical considerations, and public policy.

I. THE STATUTORY REDEMPTION PERIOD

At common law a mortgage instrument took the form of a conveyance subject to condition subsequent — payment of the mortgage debt. Upon the mortgagor's default, his property interest was automatically forfeited and title in the mortgagee became absolute. The courts of equity tempered the harshness of this rule by creating an "equity of redemption" by virtue of which absolute vesting of the mortgagee's title was postponed for some time following default to afford the mortgagor an opportunity to "redeem." This equitable right to redeem could be extinguished by foreclosure proceedings. In addition to the equity of redemption, however, half of the states have enacted statutes providing for a further redemption privilege exercisable after the foreclosure sale. These statutes permit the defaulting mortgagor,

4. Osborns § 6. It is unclear whether equity intervened to prevent a forfeiture on the ground that the conveyance of the land was intended only to afford the mortgage security, or to expand the scope of its jurisdiction at the expense of the law courts. At first equity permitted redemption after default only in special cases, but later it became a matter of right. Ibid.

5. Formerly, under a theory of "strict foreclosure," the mortgagee obtained a court order that his title would indefeasibly vest unless the mortgagor exercised his "equity of redemption" within a stipulated period. However, strict foreclosure has been replaced by other methods involving public sale of the land. See Osborns § 10. It was thought that by introducing a sale the full value of the property would be liquidated at foreclosure so that any value in excess of the amount of the debt could be retained by the mortgagor. However, this hope has not always been realized because public sales have not drawn bidders. See Prather, Foreclosure of the Security Interest, 1957 U. Ill. L.F. 440, 445. For a general discussion of foreclosure in the United States, see Teft, The Myth of Strict Foreclosure, 4 U. Chi. L. Rev. 575, 588-91 (1937).

In Minnesota the mortgagee may foreclose by judicial action, Minn. Stat. §§ 581.01-12 (1961), or by exercising a power of sale contained in the mortgage instrument, Minn. Stat. § 580.01-30 (1961). These methods are common in most states. For a summary of methods of foreclosure and other mortgage provisions of each state, see Sherman, Mortgage and Real Estate Investment Guide 1-185 (Nov. 1964 ed.). For a map illustrating the usual methods of foreclosure in each state, see Bridewell, The Effects of Defective Mortgage Laws on Home Financing, 5 Law & Contemp. Prob. 545, 547 (1938).

6. Twenty-five states do not provide for redemption after sale; eight states provide for a period of six months or less; 15 states provide for a one year period; two states have a two year period. See Sherman, op. cit. supra note 5, at 1-185 (para. 8 of each state unit).

Indiana, Nebraska, Oklahoma, and Wisconsin provide for a statutory
during the redemption period, (1) to redeem his property by tendering to the purchaser the amount of the sale price plus interest and costs and (2) to retain possession of the property. Presumably the enactment of the redemption statutes reflects a feeling that the equitable right of redemption was inadequate to protect the mortgagor. Legislatures apparently sought primarily to avert ultimate loss of possession by providing the mortgagor more time to refinance his indebtedness or otherwise to redeem his property. It was also thought that the availability of the additional period would induce higher bidding at foreclosure sales since the mortgagor or one of his creditors would probably redeem if the sale price did not fairly reflect the market value of the property.

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period of redemption following the entry of judgment in the foreclosure action during which the order of sale cannot be issued. See INDIANA ANN. STAT. § 8-1801 (Supp. 1964); NEBR. REV. STAT. § 25-1506 (Supp. 1963); OKLA. STAT. tit. 46, § 4 (1961); WIS. STAT. §§ 278.10, .101 (1963). Such statutes delay recovery by lenders of their investments just as do those which create a redemption period after the sale. But bidders are undoubtedly more attracted by a foreclosure sale which is not followed by a lengthy redemption period.

7. The mortgagor's creditors may also redeem, both from a foreclosure by action, MINN. STAT. § 581.10 (1961), and from a foreclosure by exercise of the power of sale contained in a mortgage instrument, MINN. STAT. § 580.24 (1961). If the purchaser at the foreclosure sale pays taxes or assessments to prevent penalty, or any insurance premiums or installments on superior mortgages, the sum paid will be added to the amount otherwise required for redemption. MINN. STAT. § 582.03 (1961).

8. Eight of the 25 states which provide for a statutory redemption period after sale grant the purchaser the right to possession during the period. See Sherman, op. cit. supra note 5, at 1-185 (para. 8 of each state unit). In Idaho and Nevada the purchaser has a right to rents though the debtor has the right to possession. The amount required to redeem is reduced by the amount of the rents collected. IDAHO CODE ANN. § 11-407 (1948); NEV. REV. STAT. § 21.250 (1961).

9. "These early redemption statutes came as a result of depression periods, and may be associated with the general collapse of land values, the failure of governmental public land policy, and governmental relief and moratory measures in connection with the sale of public land." SKILTON, GOVERNMENT AND THE MORTGAGE DEBTOR 20 (1944).

10. In Durfee & Doddridge, Redemption From Foreclosure Sale — The Uniform Mortgage Act, 23 MICH. L. REV. 825, 838-41 (1925), the authors conclude that the only justifiable rationale for the redemption statutes lies in whatever stimulus they may afford to active bidding since a long postsale period would not be necessary merely to secure refinancing. This could be accomplished by a statute requiring a lapse of time between filing or notice and the sale. See also KY. REV. STAT. § 426.220 (1962), which provides for a postsale redemption period only if the property is sold for less than % of its appraised value.
However, experience has revealed that neither objective has been attained. As for the first, debtors who are incapable of averting foreclosure by refinancing during the equitable redemption period usually have not found it feasible to refinance after foreclosure. If the mortgagor has accumulated considerable equity in the property, he will usually be able to avoid foreclosure by refinancing in the first place; the mortgagor with little equity either has little incentive to refinance or will find it difficult to do so. With respect to the second objective, the existence of a redemption period has not encouraged higher bidding because few people appear at foreclosure sales and, as noted above, redemption during this period is rare. In fact, the delay in vesting of title incident to the statutory redemption period has actually discouraged prospective purchasers from participating in foreclosure sales.

It appears that, rather than assisting the economically deprived, the statutory period merely facilitates abuse by the slovenly and indiscreet. An unpublished study of the reasons

11. Comment, 28 WASH. L. REV. 39, 42–43 (1953), argues that the redemption period should be abolished because few mortgages are foreclosed, redemption is infrequent when they are, and refinancing is usually available prior to foreclosure if at all.

In addition to the availability of refinancing prior to foreclosure, it may be easier to meet the mortgage obligation before rather than after foreclosure. MINN. STAT. § 580.30 (1961), provides that:

In any proceedings for the foreclosure of a real estate mortgage, whether by action or by advertisement, if at any time before the sale of the premises under such foreclosure the mortgagor, the owner, or any holder of any subsequent encumbrance or lien, or any one for them, shall pay ... the amount actually due thereon and constituting the default actually existing in the conditions of the mortgage at the time of the commencement of the foreclosure proceedings, including insurance, delinquent taxes, if any, upon the premises, interest to date of payment, ... the mortgage shall be fully reinstated ... .

A parallel provision applying to foreclosure by action may be found at § 581.07. These provisions have been construed to permit reinstatement of the mortgage upon payment only of the payments of principal and interest in default, notwithstanding the presence in the mortgage instrument of an “acceleration clause” making the entire debt due upon default. See First Nat’l Bank v. Schunk, 201 Minn. 359, 362, 276 N.W. 290, 292 (1938) (dictum).

Redemption from sale is not without its undesirable results. ... And it certainly caps the wall we have built to keep the public away from the public sale. The best market for land is found among those who desire it for immediate use, and to them, obviously, the redemption feature is prohibitive. ... Substantially, redemption statutes limit the sale to those who already have a stake in the land.

Durfee & Doddridge, supra note 10, at 841 n.51.
underlying foreclosure of Minnesota VA and FHA mortgages between 1961 and 1964 reveals that about 75 percent of them arose from "non-economic" causes—improper regard for the mortgage obligation, bad faith, financial carelessness, or marital difficulties.¹³

Not only do lengthy redemption periods fail to protect needy mortgagors, but they have proven to be particularly burdensome to mortgage lenders.¹⁴ Lenders normally tolerate delinquency for several months before foreclosing.¹⁵ Once commenced, foreclosure procedures take another month or two.¹⁶ Since the purchaser at the foreclosure sale is almost invariably the mortgagee and redemption rarely occurs, the effect of the one year redemption period in most cases is the further deferral of realization by the mortgagee of his security. The total length of time from the mortgagor's default to the end of the redemption period often exceeds 18 months. During this period the mortgagee is exposed to the risk that falling real estate prices, normal depreciation, or the mortgagor's neglect will substantially diminish the value of his security. He is also deprived of interest on his investment for this period unless the mortgagor or another eligible party redeems. Moreover, since defaulting mortgagors usually fail to pay taxes and assessments levied upon the property, these obligations must be discharged before resale.¹⁷ Insofar as it may be presumed that

¹³. The study classified these as noneconomic reasons since the debtor in each instance could have discharged his obligation if he possessed a proper motivation and/or a modicum of financial foresight. The remaining 25% of the foreclosures resulted, according to the study, for "economic" reasons—the mortgagor either lost his job or illness prevented him from earning enough income to pay his debt.

¹⁴. A recent study of single-family conventional mortgage foreclosures by savings and loan associations concluded that improper regard for the mortgage obligation accounted for 34% of the foreclosures during the period in question, excessive installment obligations caused another 19%, and marital difficulty produced 5%. KENDALL, ANATOMY OF THE RESIDENTIAL MORTGAGE 78 (1964).

¹⁵. The mortgage lending market is dominated by institutional lenders. As of 1960, life insurance companies had 42 billion dollars invested in mortgages, savings and loan associations held 60 billion dollars worth, and mutual saving banks and commercial banks held 55 billion dollars in mortgages. BRYANT, MORTGAGE LENDING 73 (2d ed. 1962).

¹⁶. Lenders often attempt a "forebearance" plan by which it is agreed that the mortgagor need pay only interest for a certain period, with payments on principal to be resumed thereafter. Wall Street J., Feb. 11, 1965, p. 7, col. 1.

¹⁷. MINN. STAT. § 580.03 (1961) requires six weeks published notice and service of a copy of the notice on the person in possession four weeks before sale.

¹⁷. If redemption occurs the redeemer must reimburse the buyer for taxes, assessments, and insurance outlays. MINN. STAT. § 582.03 (1961).
mortgagees' expenses and risks have a direct impact on the terms of mortgage financing, prospective mortgagors may be expected to bear the ultimate burden imposed by long redemption periods in the form of inflated interest rates or margin requirements. Some period of redemption after sale seems both necessary and desirable. Due to the absence of competitive bidding and the fact that mortgagees seldom bid more than the amount of the outstanding debt, the foreclosure sale, like any other forced sale, is a poor device for realizing the full market value of property. A subsequent period of redemption will afford the mortgagor an opportunity to recoup his equity even if the sale price is appreciably below market value, since he can market his statutory right to redeem and is entitled to any amount in excess of the mortgage debt paid by anyone else who does redeem. Moreover, at least a short period ought to be available for redemption after sale to afford mortgagors a final opportunity to avoid being dispossessed of their property. The preforeclosure period may in some cases be inadequate for a mortgagor completely to exhaust available credit sources, particularly if he has been sick or out of work or has otherwise experienced a temporary crisis. Finally, the existence of some postsale foreclosure period will probably deter mortgagees from foreclosing too hastily.

However, all these objectives could be obtained through the use of a period substantially shorter than 12 months. And a shorter period would reduce the burdens upon mortgagees—ultimately borne by the borrowing public—incident to postsale redemption periods. While the highly competitive nature of the mortgage market may distort the impact of such a change, it is likely that a reduction of costs would produce, (1) an increase in loan-value ratios, (2) a reduction in mortgage interest rates, and/or (3) an increase in return to the mortgagees. Thus, Minnesota could substantially shorten its statutory redemption period without losing its advantages.

The redemption period need not be the same for all kinds of property. Factors which ought to be considered in determining the length of the period for each kind of property are: its nature, the risk that it will diminish in value as a result of the mortgagor's active conduct or negligence during the period, the extent of the mortgagor's equity, and the effectiveness of the mortgagor's

18. See note 12 supra and accompanying text.

19. The mortgagee has little incentive to bid more than the debt since generally his only purpose is to realize the amount of the debt from his security.
preforeclosure opportunities to satisfy his obligations. For example, early termination of residential or farm occupancy would probably be socially less desirable than termination of a commercial or industrial occupancy. The risk of deterioration may be substantially greater for commercial and residential property than for farm property; farm land cannot be greatly diminished in value even in a year's time, while mismanagement or lack of care of commercial and residential property may destroy its value in a relatively short period. It would seem that mortgagors with a large equity should have a relatively longer period to redeem. Farm mortgagors should have a relatively short period since they often have personalty available with which to secure a loan to pay off delinquent installments prior to foreclosure. In contrast, low equity residential mortgagors may own little unencumbered personal property and consequently require a longer period to raise the necessary funds. On the other hand, farm mortgages usually secure substantially larger debts than residential mortgages, so that a farm mortgagor may need a longer period in which to re-finance than does his urban counterpart.

20. For an exhaustive discussion of urban mortgages current to 1953, see Morton, Urban Mortgage Lending (1956).

21. A bill was introduced into the 1965 session of the Minnesota legislature which would have reduced the one year redemption period presently applicable to all property to (1) four months for industrial, commercial, and multiple dwelling mortgagors, and (2) six months for residential mortgagors on less than three acres (including multiple dwellings of four units or less) where the balance due on the principal of the mortgage exceeds 20% of the original mortgage loan. For all remaining property, including farms of five acres or over and residences where the existing balance of the mortgage is 25% or less of the original amount, the redemption period would remain one year. Minn. House File No. 1960, 64th Sess. (1965); Minn. Senate File No. 749, 64th Sess. (1965). No action was taken on this proposal.


Most farmers would still enjoy a one year period under the Minnesota proposal. They may have been so favored to permit the gathering of two harvests to finance a redemption, so that a single crop failure will not produce a fatal delinquency. State statutes that differentiate usually allow farmers the longest redemption period. See Iowa Code § 628.26 (1962); Mich. Stat. Ann. § 27A.3240 (Supp. 1964); Neb. Rev. Stat. § 25-1506 (Supp. 1963); S.D. Sess. Laws 1963, ch. 236; Wis. Stat. § 278.10 (1963).

Many residential mortgagors would also enjoy a one year period under the Minnesota proposal. Those who defaulted before liquidating 25% of the original loan, however, would have only four months. This distinction based upon relative outstanding indebtedness may have merit. While it can be argued that a mortgagor with a large amount to pay should have a longer
II. THE ASSIGNMENT OF RENTS PROHIBITION

A small minority of states currently follow the "title theory" of mortgage law, while a majority, including Minnesota, adhere to the "lien theory." Under the title theory the mortgage instrument is deemed a conveyance of legal title to the property to the mortgagee subject to defeasance on the payment of the debt. Since the mortgagee rather than the mortgagor holds title while the debt remains outstanding, the former is entitled to possess and enjoy the property immediately upon the execution of the mortgage. Though he usually permits the mortgagor to retain possession, the title mortgagee may at default obtain possession, collect rents and profits, and apply them to the mortgage debt.

redemption period instead of a shorter one, it would appear more convincing to urge that a debtor with little equity is less likely to redeem and accordingly may have less incentive to maintain the property during the period. See Mich. Stat. Ann. § 27A.3240 (Supp. 1964) which provides for a six month period instead of one year for residential mortgages on property of less than three acres if the outstanding balance is more than 2% of the original loan. See also Kan. Gen. Stat. Ann. § 60-3429 (Supp. 1961), restricting the period to six months rather than the usual 18 months for a purchase money mortgage less than 2% of which has been repaid.

Although commercial and industrial mortgagors would have but a two month statutory redemption period, the total redemption period would extend to at least four or five months after default since the foreclosure procedure alone takes two months.

22. Alabama, Georgia, Maine, Maryland, New Hampshire, Pennsylvania, Rhode Island. See Osborne §§ 13–16; Prather, supra note 5, at 450.
24. Mortgagors are not anxious to take possession since they would then be held to the duties of a "mortgagee in possession." See note 43 infra.
25. In title states the mortgagee may obtain possession at any time by an action at law for ejectment. However, ejectment is very cumbersome. The action itself may take a period of time. Once in possession the mortgagee has the obligation to account as a "mortgagee in possession." See note 43 infra. Further, if the mortgagee takes possession, leases subsequent to the execution of the mortgage instrument may be terminated at the will of the lessee. For these reasons the mortgagee in a title state prefers to have a receiver appointed to collect the rents. However, a court of equity will appoint a receiver only if the legal remedy of ejectment is inadequate. Therefore, to obtain a receiver the mortgagee must establish that the land alone is inadequate to secure the debt even though he has a right to possession and with it the rents and profits. Osborne § 148. In addition to relieving the mortgagee of the burden of entering possession and being held to an accounting, the appointment of a receiver is advantageous since the receiver has the option of affirming leases made subsequent to the mortgage. Id. § 154.
These possessory rights afford him protection against waste and milking by the mortgagor. In contrast, the "lien" mortgagor is given substantially fewer rights. The mortgage instrument is not regarded as conveying him legal title, but only a security interest. Rights of ownership and possession thus remain in the mortgagor until foreclosure and expiration of the redemption period, and the mortgagor is not entitled to rents and profits until that time.

To strengthen their security interest, lien state mortgagors often bargain for an assignment of rents from the mortgagor.

26. The Minnesota court has broadly defined waste: "[A] mortgagor is chargeable with waste ... whenever, through the fault of the mortgagor, the mortgagee loses some part of the security which he had when he took his mortgage." Nielsen v. Heald, 151 Minn. 181, 184, 186 N.W. 299, 300 (1922). The Nielsen court held that failure to pay interest on prior mortgages or taxes on the property was waste. Ibid. Failure to pay assessments or insurance or to make necessary repairs is also considered waste. Mutual Benefit Life Ins. Co. v. Canby Inv. Co., 190 Minn. 144, 146, 251 N.W. 129, 131 (1933).

27. "Milking" has become a standard term denoting spoilage of the mortgaged property, rent reduction and lease cancellations by the mortgagor for a cash consideration, and prepayment of rent—all devices by which the hard-pressed mortgagor saps the value from the pledged assets." Note, The Mortgagee's Right to Rents After Default, 50 YALE L.J. 1424 n.1 (1941). Execution of leases requiring prepayment of all or a substantial portion of the rent, and the assignment of future rents to a third person are commonly used methods for milking mortgaged property. Osborne § 158.

28. For general discussion of the lien theory, see Durfee, The Lien or Equitable Theory of the Mortgage—Some Generalizations, 10 MICH. L. REV. 587 (1912); Lloyd, Mortgages—The Genesis of the Lien Theory, 32 YALE L.J. 233 (1933); Sturges & Clark, Legal Theory and Real Property Mortgages, 37 YALE L.J. 691 (1928).

A third, intermediate theory is similar to the title theory except that the mortgagee has no right to possession until default. States which adhere to this view are Arkansas, Connecticut, Delaware, Illinois, Massachusetts, Mississippi, Missouri, New Jersey, North Carolina, Ohio, Vermont, Virginia, and West Virginia. Prather, supra note 5, at 400.

29. The essence of the title-lien distinction is the right to possession. See Kratovil, REAL ESTATE LAW § 369 (1964).


An assignment of rents clause may not be necessary in states which follow the title or intermediate theory, since the mortgagee in such a state has a right to possession upon default if not before, notes 25 & 28 supra, and ordinarily could utilize this right as a lever with which to obtain rents even without an assignment clause. However, the title mortgagee may wish to obtain an assignment of rents, since the consent of the mortgagor to an assignment may influence the court in determining whether to appoint a receiver to collect the rents. Osborne § 150, at 370. For a number of reasons the mortgagee prefers to have a receiver collect the rents rather than to repossess himself. See note 25 supra.
The assignment may be included in the mortgage, made contemporaneously with the mortgage as a separate agreement, or be consummated subsequent to the mortgage for new consideration. In return for the right to whatever rents and profits are produced by the mortgaged property after the occurrence of a stipulated condition, usually default, a typical assignment contract obligates the mortgagee to apply the proceeds to taxes, insurance, repairs, assessments, and the mortgage debt, and to account for their use to the mortgagor.

An assignment of rents may be advantageous to both mortgagee and mortgagor. It enhances the mortgagee's security interest by permitting him to reach the rents and profits before he obtains the property itself. It may make foreclosure unnecessary and unattractive where rents and profits closely approximate the mortgage installments. Even if foreclosure should become necessary, rents previously collected may have reduced the outstanding mortgage indebtedness enough to make a deficiency judgment unnecessary. The assignment gives the mortgagee a claim to the rents prior to subsequent creditors of the defaulting mortgagor. Finally, an assignment of rents may afford the security of a mortgagee greater protection against milking than that afforded by

31. The new consideration usually takes the form of some concession to the mortgagor. See Seifert v. Mutual Benefit Life Ins. Co., 203 Minn. 415, 417, 281 N.W. 770, 771 (1938) (mortgagee agreed to bid full amount of debt in case of a sale); Prudential Ins. Co. v. A. Enkema Holding Co., 196 Minn. 154, 264 N.W. 576 (1936) (mortgagee agreed to delay foreclosing for delinquency in interest payments); Farmers Trust Co. v. Prudden, 84 Minn. 126, 86 N.W. 887 (1901) (extension of time for payment).

32. Although the assignment clause is conditioned to take effect upon a particular event, it must be activated by the mortgagee at that time. Conduct sufficient to activate the assignment varies among the states. A formal demand for rents with notice to the mortgagor's lessee, the initiation of a foreclosure suit, and the appointment of a receiver are common methods. The requirement that the assignment be activated is to protect the mortgagor — if the assignment were absolute he would be liable for rents collected after the effective date though the mortgagee had not demanded them. See Note, 50 YALE L.J. 1424, 1428 (1941).

33. Berick, The Mortgagee's Right to Rents, 8 U. CINC. L. REV. 250, 284 n.118 (1934), points out that by ruling assignment clauses invalid, the courts favor the mortgagor's tenants, creditors, and assigns.

Most debtors who default have other creditors who will attach the rents. Of course it may be questioned whether the mortgagee should be favored over general creditors, but it is arguable that he should as to the rents since his investment is producing them.

34. If the mortgagee notifies the mortgagor's tenant of the assignment the mortgagee is not thereafter bound by rental reductions or prepayments to which the mortgagor and tenant agree, even when arranged before the mort-
appointment of a receiver.\textsuperscript{35}

In 25 of the 28 lien theory states, an assignment of rents clause included in the mortgage instrument or executed contemporaneously with it is valid and enforceable.\textsuperscript{36} However, the Minnesota court has reasoned that since the statute establishing the lien theory provides that a mortgage shall not "be deemed a conveyance, so as to enable the owner of the mortgage to recover\n
the mortgagor's default. See Kratovil, \textit{Mortgages—Problems in Possession, Rents, and Mortgagee Liability}, 11 \textit{De Paul L. Rev.} 1, 14 & nn.42–43 (1961). The appointment of a receiver would bar such agreements only after default.\textsuperscript{35}

35. Although the court's power to appoint a receiver to collect the rents and profits was not abrogated by the lien statute, it is exercised cautiously. The test was stated in \textit{Nielson v. Heald}, 151 Minn. 181, 186 N.W. 299 (1923):

The inadequacy of the security and the insolvency of those personally liable for the debt, are not of themselves sufficient grounds for the appointment of a receiver, for the rents and profits are not part of the security . . . . To obtain the appointment of a receiver, the mortgagee must show not only that the security is inadequate and the debtor insolvent, but also that his security is becoming impaired through the wrongful failure of the mortgagor . . . to protect the property from waste.

\textit{Id.} at 185, 186 N.W. at 301. (Emphasis added.)

The criteria of insolvency, inadequacy of security, and failure to protect from waste have been followed in other cases. See Minneapolis Sav. & Loan Ass'n v. Yolton, 193 Minn. 682, 220 N.W. 282 (1935); Larson v. Orfield, 155 Minn. 282, 193 N.W. 453 (1923); Donnelly v. Butts, 137 Minn. 1, 162 N.W. 674 (1917); \textit{National Fire Ins. Co. v. Broadbent}, 77 Minn. 175, 79 N.W. 676 (1899). Because of the strict standard which must be met to obtain appointment of a receiver, few mortgagees are able to invoke the protection of this remedy.

36. Annot., 91 A.L.R. 1217 (1934); Annot., 4 A.L.R. 1405 (1919); see, e.g., \textit{Title Guarantee & Trust Co. v. Monsen}, 11 Cal. 2d 621, 81 P.2d 944 (1938); Hall v. Goldsworthy, 136 Kan. 247, 14 P.2d 659 (1932); Sullivan v. Rosson, 238 N.Y. 217, 119 N.E. 405 (1918). See also \textit{Swan v. Inderlied}, 187 N.Y. 372, 80 N.E. 195 (1907), where an assignment was found valid since rents are separable incident of possession and can be assigned through the mortgagor retains the right to possession. See also Berick, \textit{supra} note 38, at 296; Note, 6 \textit{Brooklyn L. Rev.} 25 (1936). Notwithstanding the existence of a legislative policy favoring the retention of possession by the mortgagor pending final termination of his rights, a number of states regard contemporaneous or included rent assignments as valid and enforceable. See Geraldson, \textit{Clauses Increasing the Possessory Rights of Mortgagees}, 10 Wis. L. Rev. 492, 505 (1935), which concludes that no apparent correlation exists between the validity or invalidity of a mortgage provision assigning rents and profits and the absence or presence of statutes favoring possession by the mortgagee.

possession of the real property without a foreclosure," and since rents are an important incident of possession, an assignment of rents accruing while the mortgagor remains in possession which is contained in the mortgage instrument or made as part of the mortgage transaction is also prohibited. Yet an assignment of rents made contemporaneously with the mortgage or included in it for the limited purpose of paying delinquent taxes, insurance premiums, and necessary repair costs is held valid and enforceable. Thus notwithstanding the strong policy favoring continued possession by the mortgagor, the limited assignment has been enforced as a valid exercise of the mortgagee's right to preserve his

38. E.g., Erickson-Hellekson-Vye Co. v. A. Wells Co., 217 Minn. 361, 15 N.W.2d 162 (1944); Mutual Benefit Life Ins. Co. v. Canby Inv. Co., 190 Minn. 144, 251 N.W. 129 (1933); Fidelity-Philadelphia Trust Co. v. West, 178 Minn. 160, 226 N.W. 406 (1929).

In Orr v. Bennett, 185 Minn. 443, 446, 161 N.W. 165 (1917), the court articulated the rule as follows:

[T]he mortgagor has the right of possession and the right to the rents and profits of the land incident to possession during the statutory year allowed for redemption and until the foreclosure is complete; and any stipulation in the mortgage, or contemporaneous with it, pledging the rents and profits of the mortgaged land to the payment of the mortgage debt contravenes the policy of this statute and is void. . . .

In rejecting the contention that rents are a separable incident of possession and therefore assignable, the court in Gardner v. W. M. Prindle & Co., 185 Minn. 147, 149, 240 N. W. 351, 352 (1932), reasoned that if rents were severable and so freely assignable, mortgagees could often secure for themselves, without foreclosure, the equivalent of the complete right to possession and so circumvent the statute. However, in a recent case the FHA had been assigned a Minnesota mortgage containing an assignment of rents clause when the mortgagor defaulted. The federal court held that the FHA could enforce the clause. In answering the claim that the assignment was invalid under Minn. Stat. § 559.17 (1961), the court said:

We are not confronted with the rights of the original mortgagee under the assignment, but with the vested rights of an arm of the Government. In authorizing the insurance of loans under the circumstances herein, Congress was exercising a constitutional function, and the rights of the United States thereunder must necessarily be decided by Federal law. . . .

United States v. Academy Apartments, Inc., 230 F. Supp. 110, 118 (D. Minn. 1969). The case seems to hold that the FHA can, for overriding federal interests, enforce an assignment of rents clause contained in any mortgage assigned to it though the mortgage is on Minnesota property.

security which encroaches only minimally upon the possessory rights of the mortgagor, though in either case the mortgagee is clearly recovering an incident of possession without foreclosure. The court has also created another exception to the rule against assignment of rents: an assignment made subsequent to the execution of the mortgage may pledge rents for application to the mortgage debt as well as to taxes, insurance, and repairs. In fact the mortgagor in such instances may validly authorize the mortgagee to take possession of the premises to facilitate his collection of the rents. Finally, it seems unlikely that an executed assignment would be considered invalid; i.e., a mortgagee who actually receives rents pursuant to an assignment clause in the mortgage will probably be allowed to apply them to the mortgage debt.

40. In comparing the limited assignment with an assignment to be applied to the debt, the court in Cullen v. Minnesota Loan & Trust Co., supra, said that the limited assignment was not “oppressive” to the debtor, the same “technical objections” did not apply to it, and there are “strong equities” in favor of its enforcement. Id. at 7, 61 N.W. at 820. Yet, applying the rents to the debt would not seem to be any more oppressive to the debtor than applying them to delinquent taxes or insurance premiums. The debtor is responsible for payment of all three items and the rents would not be applied to the debt until his default. It is not clear what the Cullen court meant by “technical objections.” However, it is indicated in Cullen that the limited assignment could be enforced in equity without the taking of possession. The court intimates that to effectuate an unlimited assignment, possession would have to be taken by the mortgagee and this would be a “process of foreclosure.” Ibid. This distinction is unsound since an unlimited pledge could be enforced through the use of a receiver, without the mortgagee taking possession. A more plausible distinction is that the assignment of rents to be applied to the debt gives the mortgagee additional security whereas the assignment to prevent waste merely preserves the original security. The “strong equities” in favor of the limited assignment are easily recognized. The mortgagee is a secured creditor and has a right to preserve his security. The failure of the mortgagor to pay taxes or insurance payments or to make necessary repairs jeopardizes that security.


The court’s rationale in finding that a subsequent assignment does not conflict with the statute is that it is the transfer of an interest which the mortgagor has against the tenants rather than a conveyance of an interest in real estate. Ibid. The Prudden court’s interpretation of the statute as prohibiting only a “conveyance” of an interest in real estate, though plausible, see note 44 infra, is inconsistent with the construction given the statute in prohibiting assignments of rents in the mortgage instrument.

42. See cases cited note 41 supra.

43. This distinction would seem to follow from the court’s treatment of the doctrine of “mortgagee in possession.” The doctrine has two attributes: (1)
Aside from whether the legislature ever intended the lien statute to restrict the free assignability of rents, the current status of Minnesota law on the subject is not easily justified. No reason appears for distinguishing between an unlimited assignment in the mortgage, which is invalid, and the same assignment made subsequent to the mortgage, which is valid. To be sure, it

a mortgagee who enters into possession with the consent of the mortgagor may remain to collect rents and profits until the debt is paid; (2) the mortgagee then has a number of duties to the mortgagor including an obligation to account. The doctrine originated in common-law mortgage law, under which the mortgagee had title and could enter into possession at any time. However, some lien states still permit the mortgagee to become a "mortgagee in possession" by entering peaceably.

Minnesota law provides that a mortgagee may enforce a right to obtain possession which is granted to him subsequent to the execution of the mortgage instrument. See Taylor v. Slingerland, 39 Minn. 470, 40 N.W. 575 (1888), for a discussion of the early evolution of the doctrine in Minnesota. But the court has also held that once in possession the mortgagee may remain even though he was given the right to enter in the mortgage instrument. Beberman v. Frisch, 242 Minn. 12, 64 N.W.2d 132 (1954); Gandrud v. Hansen, 210 Minn. 125, 297 N.W. 730 (1941); Lemon v. Dworsky, 210 Minn. 112, 297 N.W. 329 (1941); Anderson v. Minnesota Loan & Trust Co., 68 Minn. 491, 71 N.W. 665 (1897). The distinction between mortgagees who have taken possession and those who have not is based upon a construction of Minn. Stat. § 559.17 (1961), which provides that "a mortgage of real property is not to be deemed a conveyance so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure." By emphasizing the word "recover" the court has been able to hold that if the mortgagee possessed the property at time of suit, it made no difference that his "right" to take possession was given in the mortgage instrument. Presumably the same reasoning would give the mortgagee a right to retain rents received prior to suit no matter where he had been given the "right" to receive the rents.

44. It may plausibly be argued that the sole intent of the legislature was to repeal the title theory and establish the lien theory without limiting the incidents and features of the lien. The statute, quoted in text accompanying note 37 supra, can be so read by treating the last clause—"so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure"—as modifying "conveyance" and not as barring a mortgage instrument from conferring possessory rights upon the mortgagee without foreclosure. The reasonableness of this construction is manifested by the fact that 25 lien states, many of them with statutes similar to Minnesota's, allow a contemporaneous, unlimited assignment. See, e.g., Cal. Civ. Proc. Code § 744, Nev. Rev. Stat. § 40.050 (1957), and Utah Code Ann. § 78-40-8 (1953), which provide that "A mortgage of real property shall not be deemed a conveyance, whatever its terms, so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure and sale." The Florida and Colorado statutes are quite similar to the Minnesota and California, Nevada, and Utah statutes. Colo. Rev. Stat. Ann. § 118-6-17 (1953); Fla. Stat. § 697.02 (1961).

45. See note 41 supra. The additional consideration that the mortgagor may receive for a subsequent assignment furnishes no valid distinction
may be argued that if mortgagees were allowed to bargain for an unlimited pledge of rents as an integral part of the original mortgage transaction, the parties' unequal bargaining position would enable the mortgagee to coerce the mortgagor's acceptance of the provision. Yet the likelihood that an assignment subsequent to the mortgage was obtained by coercion would appear to be substantially greater. Such an agreement usually is entered into only by a defaulting mortgagor who, in return for his mortgagee's promise to delay foreclosure, consents to an unlimited assignment of rents and profits. Under these circumstances overreaching is not only possible, but quite probable. Furthermore, insofar as an opportunistic mortgagor may refuse to make an assignment subsequent to the creation of the mortgage and instead divert the rents accruing prior to foreclosure to his personal use, it is arguable that the Minnesota rule encourages foreclosures and the mismanagement of mortgaged land. In addition, by requiring that an unlimited assignment be made subsequent to the creation of the mortgage in order to be valid, the rule adds a substantial element of risk and uncertainty to the mortgagee's investment which will doubtless be reflected in the terms extended to all mortgagors.

The enforcement of an unlimited assignment of rents and profits made contemporaneously with or in the mortgage instrument would not encroach unduly upon the possessory interests since such consideration could have been required by the mortgage instrument if an assignment were given when it was executed. In any event, if consideration is significant the validity of an unlimited assignment could be conditioned on the mortgagee's giving additional consideration for it. As a practical matter, however, the mortgagor will nearly always receive additional consideration whether or not it is promised. This is because mortgagees will almost certainly delay foreclosure as long as substantial rents are being applied to the debt.

46. The court has never referred to the danger of widespread coercion as a reason for not enforcing contemporaneous unlimited assignments. It has relied solely on statutory interpretation.

47. See note 41 supra and accompanying text.

48. Considering the existing case law, it might be to the advantage of the mortgagee to include the assignment in a separate agreement. Clearly, an unlimited assignment included in the mortgage instrument would be terminated at foreclosure since the mortgage is then discharged. See Gardner v. W. M. Prindle & Co., 185 Minn. 147, 240 N.W. 351 (1932), in which the mortgagee could not enforce his assignment after foreclosure though the clause provided for doing so if the mortgagee purchased at the foreclosure sale. However, in Farmers Trust Co. v. Prudden, 84 Minn. 126, 86 N.W. 887 (1901), where the assignment was executed subsequent to the mortgage, and thus in a separate instrument, the mortgagee was permitted to enforce the assignment after the foreclosure sale.
of the mortgagor, since the rents will be applied to the debt and
an agreement to delay foreclosure may be facilitated. Moreover,
the risk of mismanagement following default poses a particular
threat to the security of a mortgagee of income-producing prop-
erty. Consequently, the added security afforded by a general as-
signment executed contemporaneously with the mortgage instru-
ment should encourage lenders to assume this risk. The vast
majority of mortgagors in default who, to prevent or delay fore-
closure, have given an unlimited pledge subsequent to execution
of the mortgage instrument, would be unaffected by this change.
On the other hand, a contemporaneous assignment would prevent
an opportunistic mortgagor in default from "milking" the property
pending foreclosure, i.e., obtaining rental payments covering
periods of future occupancy or granting rental reductions for such
periods. While it may be argued that mortgage provisions which
entitle mortgagees to valuable possessory rights without fore-
closure contravene the lien theory, the presence of the lien label
ought not be controlling. Rather, the validity of these pledges
should be determined and would seem to be well justified by a
practical consideration of the interests of mortgagor and mort-
gagee.

49. But see note 44 supra.
50. See note 44 supra and accompanying text.
51. Under existing Minnesota law the mortgagee may have difficulty
enforcing an unlimited assignment even if such a clause were permitted. If
a tenant's rental payments were overdue, the mortgagee could obtain them
by an action against the tenant to enforce the assignment. See Mutual
Benefit Life Ins. Co. v. Canby Inv. Co., 190 Minn. 144, 251 N.W. 129 (1933)
(unlimited assignment). However, under present Minnesota law it may be
difficult for the mortgagee to assure that rents due in the future will come
into his hands rather than the mortgagor's. Of course if he gained possession
with the consent of the mortgagor he would be a "mortgagee in possession"
and could collect the rents. The only other feasible way to enforce the
assignment would be by obtaining the appointment of a receiver. In Minne-
apolis Sav. & Loan Ass'n v. Yolton, 193 Minn. 632, 259 N.W. 382 (1935),
the mortgagee sought the appointment of a receiver to enforce a limited
assignment. It can be inferred from the opinion in that case that it is
necessary for a mortgagee seeking the appointment of a receiver to enforce
an assignment to show the existence of the same factors required for appoint-
ment of a receiver in any other case—waste, inadequate security, and in-
solvency of the mortgagor. Thus to give the mortgagee a realistic method of
enforcing his assignment the new legislation should provide for the appoint-
ment of a receiver in instances where it is necessary to enforce the assign-
ment. The Michigan courts have interpreted the remedial statute allowing
an assignment in mortgages on commercial and industrial property, Mich.
Stat. Ann. § 26.1137(1) (Supp. 1963), as permitting the mortgagee to obtain
N.W.2d 515, 520 (1960).
CONCLUSION

Some period of redemption after foreclosure sale is desirable to maximize the mortgagor's ability to recoup his equity in the property or to arrange for redemption. However, the statutory period could be substantially shorter than that currently provided by Minnesota law and yet sufficiently protect the debtor. The justifications for the shorter period are: the loss created by defaulting mortgagors who remain in possession after foreclosure without redeeming is borne by the entire borrowing public; Minnesota does not permit acceleration of the entire mortgage debt upon default; and redeeming mortgagors can generally effectuate redemption in a shorter time. Also, permitting the mortgagee of income-producing property to obtain the added security of an assignment clause in the mortgage seems justified. The exceptions to the prohibition illustrate that the policy is not to prevent the mortgagee from ever reaching the rents, but only to prevent an assignment at the time of the mortgage. However, considering the slight detriment to the debtor which arises from an assignment and the need of the mortgagee of income-producing property for security in addition to the land, this paternalistic policy seems unjustified.