REPRINTED FROM

New York Law Journal

SERVING THE BENCH AND BAR SINCE 1888

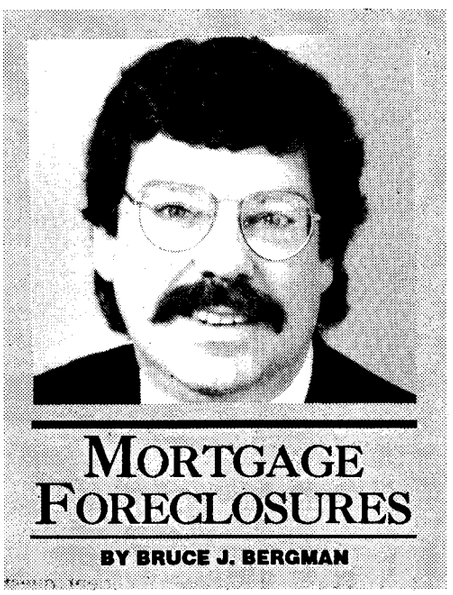
106 YEARS OF SERVICE

VOLUME 213—NO. 54 NEW YORK, WEDNESDAY, MARCH 22, 1995  PRICE $2.50

# REAL ESTATE UPDATE

# Lenders' Legal Fees

## *Vintage Government Mortgage: What Was the Drafter Thinking?*




FOR WANT OF an elemental sentence or two which would hardly challenge a law school neophyte, lenders' available legal fees are being lost in some mortgage foreclosure cases. Lest this dismal pronouncement (from a lender's vantage point) convey only gloom, note that a white horse has galloped into town. The Fannie/Freddie mortgage form arguably did not provide legal fees to a mortgagee if the case proceeded to a conclusion. When the form was revised in October 1991, though, the problem was solved — at least when a mortgage of that time or thereafter will be the subject of a foreclosure.

Recompense for counsel fees in the mortgage foreclosure case is most often a particularly meaningful subject — for reasons which should be obvious. If a foreclosing plaintiff's legal expense is reimbursed, it is a happy event, both for that plaintiff and counsel who is ultimately the recipient of the payment for services rendered. To the extent that the financial burden of prosecuting a foreclosure is reduced, protecting a lender's rights is made that much easier. And this is all the more welcome in an arena generally described with a plethora of unpleasant adjectives: technical, arcane, time consuming, distasteful, traumatic.

### Mutual Agreement

So by way of further introduction, how does an award of legal fees come about in the foreclosure case? The well recognized American rule is that each party to a lawsuit must bear its own counsel fees.[1] That prevailing maxim can be altered, however, either by statute or contractual agreement between the parties.[2]

Although no statute in New York obliges payment of legal fees by one party to the other in a mortgage foreclosure case, contract — that is, the mortgage itself — can so specify. New York courts have been consistent in ruling that legal fees are awardable to a foreclosing plaintiff in the judgment of foreclosure and sale where the mortgage so provides.[3] In plain language, if a mortgage holder wants the opportunity to be reimbursed for the sums it pays counsel to prosecute the mortgage foreclosure action, the mortgage should say so.

Not surprisingly, there is a bit more to the equation than that, but not much. Although a legal fee clause in a mortgage is effective, if the provision appears solely in the note (or bond), it will be insufficient.[4] Neither the statutory nor the title company forms of mortgage in New York contain an efficacious legal fee provision.[5]

If attorneys fees are to be recouped, the amount is decreed by the court upon application by plaintiff's counsel and made a part of the judgment of foreclosure and sale.[6] How much the plaintiff has paid or has agreed to pay its counsel is not the measure of reimbursement.[7] Rather, reasonableness must control.[8] Even with all these cogent principles, courts can be disconcertingly parsimonious when assessing legal fees, and though there is no authority for it (when the legal fee clause is in the mortgage) they occasionally decline to make the award.[9]

If it is so effortless to insert a legal fee clause into a mortgage (and it really *is*),[10] what then is the problem? The response is the draftsmanship of the standard FNMA/FHLMC form of mortgage as it existed for so many years.

Because a significant percentage of mortgage paper is sold on the secondary market, there is a frequently irresistible compulsion to use this form. Among the pre-1991 form's many shortcomings (again from a lender's point of view) is the coverage of legal fees. If a defaulting borrower wishes to reinstate, the mortgage clearly obliges the payment of legal fees. The imperative is based upon this lucid language from paragraph 18 (Borrower's Right to Have Lender's Enforcement of This Security Instrument Discontinued), subsection (c), imposing this condition:

> I pay all of lender's reasonable expenses in enforcing this security instrument including, for example, reasonable attorneys fees . . .

There is no doubt about the cited language. But where reinstatement or satisfaction is *not* the issue; where instead the foreclosure proceeds to judgment, when legal fees would otherwise be assessed if available, precision disappears and the best that is left may be ambiguity.

In the pre-1991 FNMA/FHLMC mortgage form there are only two provisions which seem to apply to the legal fee formulation. One is non-uniform covenant 19 (Lender's Rights if Borrower Fails to Keep Promises and Agreements), the second paragraph of which roads as follows:

> If lender requires immediate payment in full, lender may bring a lawsuit to take away all of my remaining rights in the property and have the property sold. At this sale lender or another person may acquire the property. This is known as "foreclosure and sale." In any lawsuit for foreclosure and sale, lender will have the right to collect all costs allowed by law.

This *looks* like the portion of the mortgage which would apply to counsel fees in foreclosure. The handicap is that payment is provided solely for "all costs allowed by law." Law in New York does not contemplate legal fees in a mortgage foreclosure action. Thus, it is up to the mortgage *contract*. But the mortgage

---

**Bruce J. Bergman,** *a partner in Certilman Balin Adler & Hyman in East Meadow, New York, is the author of the two-volume treatise,* Bergman on New York Mortgage Foreclosures, *Matthew Bender & Co. Inc. (rev. 1995).*

contract refers back to law, so unending circularity short-circuits the lender. This clause will not support legal fees.

The only other provision holding any promise is paragraph 7, inopportunely entitled "Lender's Right to Protect Its Rights in the Property: Mortgage Insurance." The first portion of that paragraph reads:

> If: (A) I do not keep my promises and agreements made in the security instrument, or (B) someone, including me, begins a legal proceeding that may significantly affect lender's rights in the property (such as a legal proceeding in bankruptcy, in probate, for condemnation or to enforce laws or regulations), lender may do and pay for whatever is necessary to protect the value of the property and lender's rights in the property. Lender's actions may include appearing in court, paying reasonable attorneys fees and entering on the property to make repairs. Lender must give me notice before lender may take any of these actions. Although lender may take action under this paragraph 7, lender does not have to do so.

That language does not sound like it was designed to provide legal fees to a foreclosing lender (a conclusion some courts have reached),[11] *except* if broken down into its elements in this way:

> If: . . . I do not keep my promises and agreements made in the security instrument . . . lender may do and pay for whatever is necessary to protect lender's rights in the property. Lender's actions may include appearing in court, paying reasonable attorneys' fees . . .

*Now* it appears as if the mortgage drafter intended this verbiage to cover legal fees if a borrower defaults and a foreclosure ensues. Stated in the words of the paragraph, if the borrower fails to keep a promise and the lender protects its rights.

## A Judge's Interpretation

The ultimate predicament and lament is this. The portion of the mortgage which is supposed to address legal fees in foreclosure (paragraph 19) clearly fails. And that is the place where it should be dealt with. The only other place a mortgagee might be saved can readily be interpreted to apply to protecting the mortgage and the property from third party assaults — not to fund attorneys fees in a foreclosure case. And if the drafter of the mortgage wanted a foreclosing lender to receive a counsel fee award it would have been an effortless task. Either the mortgage's author egregiously blundered, or never meant to so benefit the lender.

In the end, the true interpretation is whatever a judge says it is in a particular case. Sadly for lenders and servicers, anecdotally, cases where the ruling is against granting legal fees are on the rise. (Those are unreported decisions). Thus, if the mortgage being foreclosed is the FNMA-FHLMC form in use before October 1991, collection of legal fees if the action goes to a conclusion remains problematical.

The fall of 1991 brought a welcome change. Paragraph 21 — the cure letter provision — contains this enlightened verbiage in its second paragraph:

> If lender requires immediate payment in full, lender may bring a lawsuit to take away all of my remaining rights in the property and have the property sold . . . In any lawsuit for foreclosure and sale, lender will have the right . . . to add all reasonable attorneys' fees to the amount I owe lender, which fees shall become part of the sums secured.

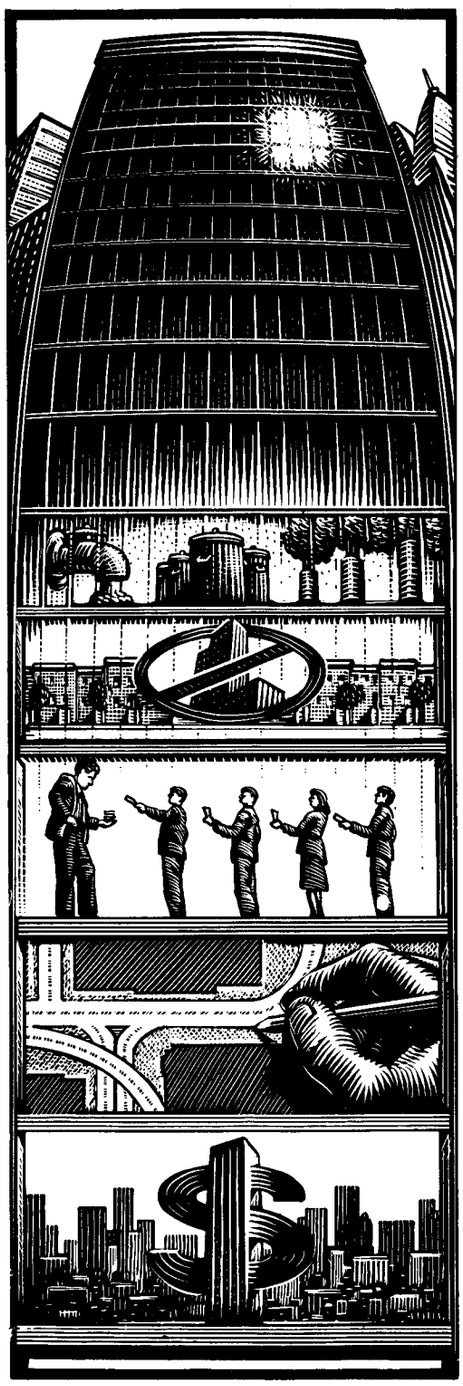


ILLUSTRATION BY JOHN MacDONALD

Problem solved — for newer mortgages anyway. For vintage Fannie/-Freddie documents, the dilemma persists.

(1) *Chappeo v. Mitchell*, 84 NY2d 345, 618 NYS2d 626, ___ NE2d ___ (1994); *Hooper Assocs. v. AGS Computers*, 74 NY2d 487, 549 NYS2d 365, 548 NE2d 487 (1989); *First Nat'l Bank of Highland v. J. & J. Milano Inc.*, 160 AD2d 670, 553 NYS2d 448 (2d Dept. 1990); *Trendi Sportswear v. Air France*, 146 Misc2d 111, 549 NYS2d 561 (Sup.Ct. 1989); *Alyeska Pipeline Serv. Co. v. Wilderness Soc'y*, 421 U.S. 240, 95 S.Ct. 1612, 44 L.Ed.2d 141 (1975).

(2) *Hooper Assocs. v. AGS Computers*, 74 NY2d 487, 549 NYS2d 365, 548 NE2d 487 (1989); *Paroff v. Muss*, 171 AD2d 782, 567 NYS2d 502 (2d Dept. 1991); *Rivkin v. Brackman*, 167 AD2d 239, 561 NYS2d 738 (1st Dept. 1990); *First Nat'l Bank of Highland v. J. & J. Milano Inc.*, 160 AD2d 670, 553 NYS2d 448 (2d Dept. 1990); *Barba v. Lindissimo Boutique Inc.*, 119 Misc2d 117, 564 NYS2d 698 (Sup.Ct. 1991); *Trendi Sportswear v. Air France*, 146 Misc2d 111, 549 NYS2d 561 (Sup.Ct. 1989). See also *Matter of A.G. Ship Maintenance Corp. v. Lezak*, 69 NY2d 1, 511 NYS2d 216, 503 NE2d 681 (1986); *City of Elmira v. Larry Walker Inc.*, 150 AD2d 129, 546 NYS2d 183 (3d Dept. 1989). *Cross v. Zyburo*, 185 AD2d 967, 587 NYS2d 670 (2d Dept. 1992); *Locascio v., Acquavella*, 185 AD2d 689, 586 NYS2d 78 (4th Dept. 1992); *Sibley Mort. Corp. v. Sobotka*, 155 Misc2d 616, 589 NYS2d 279 (1992).

(3) *Matter of Nicfur-Cruz Realty Corp.*, 50 B.R. 162 (Bankr. SDNY 1985); In re *Berry Estates Inc.*, 47 B.R. 1004 Bankr. SDNY 1985); In re *Guccione*, 41 B.R. 289 (Bankr. SDNY 1984); *United States v. Bedford Assocs.*, 548 F.Supp. 748 (SDNY 1982); In re *Am. Motors Prod. Corp.*, 98 F2d 774 (2d Cir. 1938); *Chelsea/22 Assocs. v. Fleissner*, 540 NYS2d 815 (App. Div. 1st Dept. 1989); *Kenneth Pregno Agency Ltd. v. Letterese*, 112 AD2d 1032, 492 NYS2d 824 (2d Dept. 1985); *Community Sav. Bank v. Shaad*, 105 AD2d 1063, 482 NYS2d 162 (4th Dept. 1984); *Fed Land Bank of Springfield, Mass. v. Ambrosano*, 89 AD2d 730, 453 NYS2d 857 (3d Dept. 1982); *Inter-City Investor Corp. v. Kessler*, 56 AD2d 645, 391 NYS2d 894 (2d Dept. 1977); *Avco Fin. Servs. v. Bentley*, 116 Misc2d 34, 455 NYS2d 62 (1982); *Bank of Smithtown v. Pelletier, NYLJ*, Oct. 26, 1977, at 14, col. 6 (Sup.Ct. Suffolk Co., De Luca, J.); *Scheible v. Leinen*, 67 Misc2d 457, 324 NYS2d 197 (1971); *City of Utica v. Gold Medal Packing Corp.* 54 Misc2d 721, 283 NYS2d 603 (1967).

(4) *Federal Land Bank of Springfield v. Handschuh*, 125 Misc2d 686, 480 NYS2d 294 (1984); *Lipton* v. *Specter*, 96 AD2d 549, 465 NYS2d 59 (2d Dept. 1983), citing *Jamaica Sav. Bank v. Cohan*, 38 AD2d 841, 330 NYS2d 119 (2d Dept. 1972)

(5) *Vardy Holding Co. v. Metric Resales Inc.*, 131 AD2d 564, 516 NYS2d 490 (2d Dept. 1987); *Li v. Astoria Fed. Sav. & Loan Ass'n*, 81 AD2d 857, 438 NYS2d 865 (2d Dept. 1981); *Daiwa Bank Trust Co. v. Pierri, NYLJ*, Oct. 18, 1989, at 26, col. 6 (Sup.Ct. Queens Co., Hentel, J.).

(6) For a discussion of measuring the legal fee, see 2 *Bergman on New York Mortgagae Foreclosures*, §26.03, and for the standards for counsel in applying, see 2 *Bergman on New York Mortgage Foreclosures*, §26.06 (Matthew Bender & Co. Inc., rev. 1995).

(7) *Equitable Lumber Corp. v. IPA Land Dev. Corp.*, 38 NY2d 516, 381 NYS2d 459, 344 NE2d 391 (1976); *Federal Land Bank of Springfield, Massachusetts v. Ambrosano*, 89 AD2d 730, 453 NYS2d 857 (3d Dept. 1982).

(8) *First Nat'l Bank of East Islip v. Brower*, 2 NY2d 471, 398 NYS2d 875, 368 NE2d 1240 (1977); *Industrial Equip. Credit Corp. v. Green*, 92 AD2d 838, 460 NYS2d 337 (1st Dept. 1983), aff'd, 62 NY2d 903, 478 NYS2d 861, 467 NE2d 525 (1984); *Beacon Fed. Sav. & Loan Ass'n v. Marks*, 97 AD2d 451, 467 NYS2d 662 (2d Dept. 1983); *Federal Land Bank of Springfield, Massachusetts v. Ambrosano*, 89 AD2d 730, 453 NYS2d 857 (3d Dept. 1982); *Mead v. First Trust & Deposit Co.*, 60 AD2d 71, 400 NYS2d 936 (4th Dept. 1977); *Inter-City Investor Corp. v. Kessler*, 56 AD2d 645, 391 NYS2d 894 (2d Dept. 1977); *Avco Financial Services v. Bentley*, 116 Misc2d 34, 455 NYS2d 62 (1982); *Marine Midland Bank v. Roberts*, 102 Misc2d 721, 283 NYS2d 603 (1967).

(9) For more discussion of nuance and case law on the subject of counsel fees in the mortgage foreclosure case see 2 *Bergman on New York Mortgage Foreclosures*, §26.01 and §26.02 (Matthew Bender & Co. Inc., rev. 1995).

(10) For a further review of drafting the legal fee provision, with examples of clauses which do and do not serve the purpose, see 2 *Bergman on New York Mortgage Foreclosures*, §26.05 (Matthew Bender & Co. Inc., rev. 1995).

(11) *Sibley Mort. Corp. v. Sobotka*, 155 Misc2d 616, 589 NYS2d 279 (1992).