

You Can Claim Legal Fees, Correct?

What You Want Isn't Necessarily What You Will Get

BY BRUCE J. BERGMAN

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If New York is any example, there is a burgeoning problem regarding a lender's ability to recoup legal fees in the foreclosure case - and it is well worthy of remedial action.



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The underlying issue is the meaning of the widely employed standard paragraph 7 in the Fannie Mae/Freddie Mac Uniform Instrument [Lender's Right To Protect Its Rights In The Property; Mortgage Insurance]. The clause is glaringly less than ideal and some courts are arriving increasingly at that conclusion.

While this may seem to be a discussion of some technical nicety, it is indeed practical and translates into meaningful numbers.

A brief overview of general legal fee concepts will serve to help readers appreciate the importance of this discussion. Recognize that the impact is greater in judicial foreclosure states and of more significance where legal fee precepts are not controlled by statutes.

Although, of course, there are nuances and complications, the subject most often is really rather simple.

Getting what you pay for

If a lender or servicer can recapture legal fees through the mortgage foreclosure case, then to some extent - or completely - it is reimbursed and it need not pay counsel for the foreclosure.

Stated alternatively, the lender gets back what it has already paid its attorneys, or what it will be called upon to remit at the conclusion of the case.

Howsoever it is phrased, it is certainly pleasing for a lender or servicer not to incur legal expense in a foreclosure action, whether or not this

was a very large sum or a more modest amount.

Where statutes do not control the

granting of legal fees to a foreclosing plaintiff, case law typically provides that where the parties agree to contract

to reimburse a lender, the language is to be enforced. A mortgage is a contract and, therefore, an appropriately

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worded clause in the mortgage (it may
be insufficient if it appears only in the
note) will generally be the basis of an
award of legal fees.

In many judicial foreclosure states,
that award comes at the stage when
the judgment of foreclosure and sale
is sought.

Staking your claim

Even if it can be approached at
some other plateau in the foreclosure
case, counsel applying for fees must
demonstrate to the court that the
predicate of the appropriate language
appears in the mortgage.

Usually there then must be a pre-
sentation of the amount of time ex-
pended for services, the reasonable-
ness of the time, as well as the
reasonableness of the charges for
that time invested.

The court is then empowered to in-
clude in the judgment of foreclosure
and sale an assessment of the value

meruit basis, that is, what the legal
effort was worth.

Although sometimes that amount is
less than counsel has sought, and less
than servicer and counsel believe it is
worth, it can also be precisely what has
been requested. Whatever the sum is,
the potential that this will be welcome to
servicer and counsel is certainly there.

Changes in judgment

To be sure, the value of insertion
of legal fees in the judgment varies
over time.

Prior to 1987, when there tended to
be more generous equity in real estate,
selling the property at the foreclosure
sale for the full upset price occurred
more often than not. Since the upset
price typically contained the legal fees
(as awarded in the judgment), it meant
automatically that the lender was reim-
bursed for that expense.

With the downturn in the real es-
tate market, however, foreclosure
sale purchasers became less frequent
and when they did bid, it was often at
a reduced price. In those latter in-
stances, inclusion of a legal fee
amount in the judgment lost meaning
because there was nobody to pay the
amount computed.

Of course, this has been changing
and will change still more as the market
recovers. Thus, legal fees will once
again become increasingly important.

The worst problem the lender or
servicer should encounter, then, is a
judge who is less generous than
lenders or servicers would prefer in
evaluating the worth of the legal ser-
vices. But that is not the only
predicament.

Interpreting 'paragraph 7'

Recalling that there must be a
clause in the mortgage sufficient to
support the award, turn to the om-
nipresent standard paragraph 7 in the
Fannie Mae/Freddie Mac form which,
as far as is relevant here, reads as fol-
lows:

"If I do not keep my promises and
agreements made in this Security In-
strument, or someone, including me,
begins a legal proceeding that may
significantly affect Lender's rights in
the Property (such as a legal pro-
ceeding in bankruptcy, in probate,
for condemnation or to enforce laws
or regulations), Lender may do and
pay for whatever is necessary to pro-
tect the value of the Property and
Lender's rights in the Property.
Lender's actions may include appear-
ing in court, paying reasonable attor-
neys' fees and entering on the Prop-
erty to make repairs. Lender must
give 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."

If the noted language is broken
down into its elements, it can be ar-
gued that it says and means that if
the borrower fails to keep any agree-
ment (such as the obligation to pay),
then the lender can do whatever is
necessary to protect its rights in the
property, including expending legal

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The court (is) empowered to include in the judgment of foreclosure and sale an assessment of the value of the legal work (based on) what it was worth.

fees in a foreclosure. That is the view lenders and servicers would espouse.

An opposing view

A coherent argument can also be made, even if we disagree with it, that all this language does not apply specifically to a mortgage foreclosure brought by the lender. This counter position is further buttressed by other clauses in the mortgage which do specifically refer to mortgage foreclosure, and yet do not in those areas talk about recompense for legal fees.

Judges have taken this precise position before and continue on occasion to do so. They are saying that the clause at issue refers to actions

other than the lender's own foreclosure. Whether this is genuinely a trend, how widely its mischief will spread may be open to conjecture. Whatever its extent, it does no good deed for lenders and servicers.

Adding a clause

Rhetorically it could be asked, how difficult is it to prepare a simple clause providing that in the event a lender or servicer begins a mortgage foreclosure action it is entitled to be repaid reasonable legal fees expended in prosecuting the action?

The ready answer is "not very difficult." Why the language in the Fannie Mae/Freddie Mac form is so obscure, unclear or ambiguous is most perplexing indeed. If the intention was for lenders to recover legal expense (which we think, by the way, it was), then the draftsmanship should have been much better. It certainly *could* have been.

Assuming Fannie Mae/Freddie Mac don't become independently excited by this article, in the end this problem is solved with a simple clause inserted in a rider appended to the mortgage.

Lenders or servicers who may originate mortgages should consider attending to this as soon as possible. It will consume but a moment's time. This may not be of critical importance this very day, but it will become more meaningful in the months and years to come.

It is certainly worth thinking about.

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