

IN THE
SUPREME COURT OF APPEALS OF
WEST VIRGINIA

RECORD NO. 12-0522

(Kanawha County Circuit Court No. 10-C-592)

HARTFORD FIRE INSURANCE COMPANY,

Defendant Below/Petitioner,

v.

JERRY LEE RHODES

and

BONNIE M. COCHRAN,

Plaintiffs Below/Respondents.

PETITIONER'S BRIEF

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TABLE OF CONTENTS

| | <u>Page</u> |
|---|-------------|
| TABLE OF AUTHORITIES | iv |
| ASSIGNMENTS OF ERROR..... | 1 |
| STATEMENT OF THE CASE..... | 2 |
| SUMMARY OF ARGUMENT | 5 |
| STATEMENT REGARDING ORAL ARGUMENT AND DECISION | 7 |
| ARGUMENT | 8 |
| I. Standard of Review..... | 8 |
| II. Statutory and Regulatory Background..... | 9 |
| <u>Assignment of Error No. 1</u> | 11 |
| III. The Bond is Subject to the General Rule Set Forth in W. Va. Code § 45-1-3. | 11 |
| IV. The Exception Set Forth in <u>Myers</u> Does Not Apply. | 12 |
| V. The Rules of Contract Construction Cited by Plaintiffs Are Irrelevant to this Appeal..... | 17 |
| VI. The Kanawha County Circuit Court’s Order in <u>Stayer</u> Supports Hartford’s Position Here, and Hartford is Not Estopped from Relying on its § 45-1-3 Protections Because of an Argument it Advanced and Lost in Another Case. | 18 |
| VII. The Commissioner of Banking Had No Authority to Require a Bond that Ignores a Mortgage Broker Bond Surety’s Rights Under W. Va. Code § 45-1-3. | 22 |
| <u>Assignment of Error No. 2</u> | 24 |
| VIII. Public Policy Considerations Weigh in Favor of Ensuring that a Surety is Entitled to an Opportunity to Defend Itself on the Merits. | 25 |

| | | |
|-----|--|----|
| IX. | Commonly Accepted Principles of Surety Law Do Not Permit a Plaintiff to Enforce a Default Judgment Awarded Against a Principal Where the Surety Was Not Given Notice and Opportunity to Defend. | 28 |
| | <u>Assignment of Error No. 3</u> | 30 |
| X. | Plaintiffs Have Received One Full Recovery for the Indivisible Injuries Allegedly Caused by Equity South and its Joint Tortfeasors | 30 |
| XI. | Hartford is Entitled to a Credit Against the Judgment in the Full Amount of the August 4, 2010 Settlement..... | 32 |
| | CONCLUSION..... | 38 |
| | CERTIFICATE OF SERVICE | 40 |
| | EXHIBIT A: <u>Stayer v. Litton Loan Servicing, et al.</u> , No. 08-C-3157 (Kanawha Co. Cir. Ct. Aug. 16, 2010) | |

TABLE OF AUTHORITIES

| | <u>Page(s)</u> |
|--|-------------------|
| <u>Cases:</u> | |
| <u>Aetna Cas. & Sur. Co. v. Fed. Ins. Co. of New York,</u> 148 W.Va. 160, 133 S.E.2d 770 (1963)..... | 8 |
| <u>Axess Int’l v. Intercargo Ins. Co.,</u> 183 F.3d 935 (9th Cir. 1999) | 29 |
| <u>Baldau v. Jonkers,</u> No. 35650, 2011 W. Va. LEXIS 13 (W.Va. Mar. 10, 2011) | 8 |
| <u>Bd. of Educ. of McDowell County v. Zando, Martin & Milstead, Inc.,</u> 182 W.Va. 597, 390 S.E.2d 796 (1990)..... | 7, 32, 33, 34, 35 |
| <u>Bldg. & Loan Ass’n v. Sohn,</u> 54 W.Va. 101, 46 S.E. 222 (1903)..... | 24 |
| <u>Bloss v. Plymale,</u> 3 W.Va. 393 (1869) | 34 |
| <u>Boley v. Miller,</u> 187 W.Va. 242, 418 S.E.2d 352 (1992)..... | 23 |
| <u>Brewer v. Appalachian Constructors, Inc.,</u> 135 W.Va. 739, 65 S.E.2d 87 (1951)..... | 32 |
| <u>Chewning v. Tomlinson,</u> 105 W.Va. 76, 141 S.E. 532 (1928)..... | 36 |
| <u>City of Mullens v. Davidson,</u> 133 W.Va. 557, 57 S.E.2d 1 (1949)..... | 18 |
| <u>Commercial Bank v. St. Paul Fire & Marine Ins. Co.,</u> 175 W.Va. 588, 336 S.E.2d 552 (1985)..... | 16 |
| <u>Cottrill v. Ranson,</u> 200 W.Va. 691, 490 S.E.2d 778 (1997)..... | 8, 9 |
| <u>Frederick Mgmt. Co. v. City Nat’l Bank,</u> No. 35438, 2010 W. Va. LEXIS 144 (W.Va. Nov. 23, 2010)..... | 8 |

| | |
|--|---------------|
| <u>Gen. Elec. Co. v. Nat'l Labor Relations Bd.</u> , 414 F.2d 918 (4th Cir. 1969) | 17 |
| <u>Hannah v. Heeter</u> , 213 W.Va. 704, 584 S.E.2d 560 (2003) | 20 |
| <u>Hardin v. The New York Cent. R.R. Co.</u> , 145 W.Va. 676, 116 S.E.2d 697 (1960) | 34, 36 |
| <u>Hartford Fire Ins. Co. v. Curtis</u> , Record No. 12-0037 (Sup. Ct. Appeals. W.Va.) | 7 |
| <u>Keatley v. Mercer County Bd. of Educ.</u> , 200 W.Va. 487, 490 S.E.2d 306 (1997) | 24 |
| <u>Lawson v. County Comm'n</u> , 199 W.Va. 77, 483 S.E.2d 77 (1996) | 24 |
| <u>Lovas v. Consolidation Coal Co.</u> , 222 W.Va. 91, 662 S.E.2d 645 (2008) | 23 |
| <u>New River & Pocahontas Consol. Coal Co. v. Eary</u> , 115 W.Va. 46, 174 S.E. 573 (1934) | 34, 36 |
| <u>Old Republic Sur. Co. v. Bonham State Bank</u> , 172 S.W.3d 210 (Tex. App.-Texarkana 2005) | 13 |
| <u>Pegram v. Herdrich</u> , 530 U.S. 211 (2000) | 21 |
| <u>Pennington v. Bluefield Orthopedics, P.C.</u> , 187 W. Va. 344, 419 S.E.2d 8 (1992) | 32 |
| <u>Pico v. Webster</u> , 14 Cal. 202, 204 (Cal. 1859) | 15 |
| <u>Potesta v. United States Fid. & Guar. Co.</u> , 202 W.Va. 308, 504 S.E.2d 135 (1998) | 17 |
| <u>Rashid v. The United States Fid. & Guar. Co.</u> , No. 2:91-0141, 1992 U.S. Dist. LEXIS 22914 (S.D.W. Va. Sept. 28, 1992) | 6, 13, 14, 15 |
| <u>Respass v. Workers' Comp. Div.</u> , 212 W.Va. 86, 569 S.E.2d 162 (2002) | 23 |

| | |
|--|---------------|
| <u>Rhodes v. Nationstar Mortgage, LLC,</u> No. 08-C-69 (Putnam Co. Cir. Ct.)..... | 2 |
| <u>Robinson v. Cabell Huntington Hosp., Inc.,</u> 201 W.Va. 455, 498 S.E.2d 27 (1997)..... | 16 |
| <u>Rollyson v. Jordan,</u> 205 W.Va. 368, 518 S.E.2d 372 (1999)..... | 26 |
| <u>Rowe v. W. Va. Dept. of Corr.,</u> 170 W.Va. 230, 292 S.E.2d 650 (1982)..... | 23 |
| <u>State v. Abbott,</u> 63 W.Va. 189, 61 S.E. 369 (1907)..... | 15, 28 |
| <u>State v. Duggan,</u> 102 W.Va. 312, 135 S.E. 270 (1926)..... | 11, 12, 15 |
| <u>State v. Epperly,</u> 135 W.Va. 877, 65 S.E.2d 488 (1951)..... | 17 |
| <u>State v. Myers,</u> 74 W.Va. 488, 82 S.E. 270 (1914)..... | 6, 12, 13, 14 |
| <u>State v. Williams,</u> 196 W.Va. 639, 474 S.E.2d 569 (1996)..... | 24 |
| <u>Stayer v. Litton Loan Servicing, et al.,</u> No. 08-C-3157 (Kanawha Co. Cir. Ct. Aug. 16, 2010)..... | 18, 19 |
| <u>Tennant v. Craig,</u> 156 W.Va. 632, 195 S.E.2d 727 (1973)..... | 34, 36, 37 |
| <u>The Hardwood Group v. LaRocco,</u> 219 W.Va. 56, 631 S.E.2d 614 (2006)..... | 28, 29 |
| <u>United Hosp. Ctr. v. Richardson,</u> 757 F.2d 1445 (4th Cir. 1985)..... | 24 |
| <u>W. Va. Dep't. of Transp., Div. of Highways v. Robertson,</u> 217 W.Va. 497, 618 S.E.2d 506 (2005)..... | 20, 21 |
| <u>Wellington Power Corp. v. CNA Sur. Corp.,</u> 217 W.Va. 33, 614 S.E.2d 680 (2005)..... | 15, 17 |

| | |
|---|----|
| <u>Winnings v. Wilpen Coal Co.</u> , 134 W. Va. 387, 59 S.E.2d 655 (1950)..... | 30 |
|---|----|

Statutes:

| | |
|---|-------------------|
| Tex. Transp. Code § 503.033..... | 13 |
| W.Va. Code § 31-17-2..... | 9 |
| W.Va. Code § 31-17-4..... | 9, 10, 22, 23, 24 |
| W.Va. Code § 31-17-6..... | 9 |
| W.Va. Code § 31-17-12..... | 9 |
| W.Va. Code § 44-10-14..... | 36 |
| W.Va. Code § 45-1-3..... | passim |
| W.Va. Code § 55-7-12..... | 36 |
| W.Va. Code § 55-7-13..... | 33 |
| W.Va. Code, 1913, sec. 28, ch. 32, serial section 1144..... | 13 |

Rules of Court

| | |
|---|----|
| Rule 8(e)(2), West Virginia Rules of Civil Procedure..... | 21 |
|---|----|

Miscellaneous:

| | |
|---|----|
| 4B MICHIE’S JURISPRUDENCE <u>Contracts</u> § 40 (Repl. Vo. 1986)..... | 26 |
| 74 AM. JUR. 2D <u>Suretyship</u> § 153 (1974)..... | 29 |
| RESTATEMENT (THIRD), <u>Suretyship & Guaranty</u> , § 67(3) (1995)..... | 28 |

ASSIGNMENTS OF ERROR

1. The trial court erred in disregarding West Virginia Code § 45-1-3 and holding that a surety on a statutory mortgage broker bond issued in the form and in the language established by the Commissioner of Banking is automatically responsible for paying any judgment rendered against its principal.

2. The trial court erred in holding that a default judgment against a principal on a mortgage broker bond can be enforced against the surety where the surety does not receive notice of the claim against its principal until after judgment is rendered.

3. The trial court erred in holding that a surety and its principal are not entitled to a setoff or credit against a judgment rendered against the principal despite the fact that the plaintiffs have already received one full recovery for their alleged injury.

STATEMENT OF THE CASE

This appeal arises from a summary judgment ruling against a surety on a statutory mortgage broker bond. Equity South Mortgage, LLC (“Equity South”) was a mortgage broker licensed and operating in West Virginia. The Defendant Below/Petitioner, Hartford Fire Insurance Company (“Hartford”), was the surety on a mortgage broker bond in the amount of \$50,000 issued in strict accordance with Chapter 31, Article 17 of the West Virginia Code (the “bond”) naming Equity South as its principal and the State of West Virginia as its obligee. (App. 15-16). The bond was issued in the form promulgated and in the language prescribed by the West Virginia Commissioner of Banking.

On March 3, 2008, Plaintiffs/Respondents Jerry Lee Rhodes, the sole owner of the real property at issue, and Bonnie M. Cochran, Mr. Rhodes’s former live-in girlfriend,¹ filed suit in the Circuit Court of Putnam County, West Virginia against Equity South, Nationstar Mortgage LLC (“Nationstar”), Christopher Smith and John Doe Holder, initiating that case styled Rhodes, et al. v. Nationstar Mortgage, LLC, et al., No. 08-C-69 (the “Putnam County case”), and alleging that Equity South, among others, made certain misrepresentations which caused Plaintiffs to take two home improvement loans on unfavorable terms in 2003 and 2004. (App. 111-120). Nationstar is the successor in interest to Centex Home Equity Co., the company which actually made the loans to Plaintiffs. (App. 112). The defendant Equity South was identified as the mortgage broker who put the loan together in which plaintiffs were the borrowers and Nationstar was the lender. (App. 112-113). The defendant Christopher Smith was identified as the appraiser of the property to be used as collateral for the loan. (App. 112-113). John Doe Holder was the holder of the mortgage note. (App. 112). Hartford was not named as a defendant and

¹ Plaintiff Jerry Lee Rhodes still owns and resides in the home in Putnam County. (App. 234). Plaintiff Bonnie M. Cochran moved out of the home in 2006 when her relationship with Mr. Rhodes ended. (App. 148-149). Ms. Cochran does not hold an interest in the property at issue and never has.

was not informed at that time of the existence of the lawsuit or that a potential claim against its principal even existed.

Equity South failed to file a response to Plaintiffs' Complaint in the Putnam County case, as it was then defunct. On October 14, 2008, Plaintiffs obtained a default judgment against Equity South in the amount of \$56,300 plus post-judgment interest (the "Equity South Judgment"). (App. 291-292). Plaintiffs' claims against the other defendants in the Putnam County case, including the originating lender Nationstar, appraiser Christopher Smith, and John Doe Holder (later replaced with The Bank of New York Mellon (the "Bank of New York")), remained pending for resolution. (App. 292).

Four months after securing the default judgment without Hartford's knowledge, Plaintiffs finally gave the first notice of their claim to Hartford on February 5, 2009. (App. 302). Hartford responded by letter dated February 19, 2009, requesting documentation of the claim and indicating its intent to investigate. (App. 303). On or about March 29, 2010, the Complaint in the instant case was filed in the Circuit Court of Kanawha County, West Virginia. (App. 2-6). Plaintiffs again alleged that Equity South made certain misrepresentations and took certain actions which caused Plaintiffs to enter into a home improvement loan and subsequently refinance the property on unfavorable terms. (App. 2-6). By virtue of the Equity South Judgment, Plaintiffs alleged that they were entitled to payment in the full amount of the bond. (App. 5-6). Hartford filed a timely Answer to the Complaint on May 4, 2010. (App. 7-16).

No further action was taken in the instant case for over a year. In the meantime, Plaintiffs pursued settlement with the remaining defendants in the Putnam County case. On August 4, 2010, Plaintiffs entered into a formal settlement agreement with Nationstar and the Bank of New York, two of the remaining defendants in the Putnam County case. (App. 64-70).

Hartford was not notified of the settlement discussions and was not aware of the settlement until after it was finalized. Under the terms of the settlement, the remaining defendants agreed to and did (1) void the unpaid amount of the home improvement loan which is the subject of this case, (2) release the Deed of Trust on the real property owned by Plaintiff Rhodes, and (3) cure all negative credit reporting against Plaintiffs relating to their default under the loan. (App. 65). The result of the settlement is that Plaintiff Jerry Lee Rhodes now owns the property free and clear of any mortgage, and neither Plaintiff has any obligation to repay the money loaned to them or any adverse credit effects from the loan or subsequent refinance.

On December 19, 2011, Plaintiffs filed a Motion for Summary Judgment and Memorandum in Support asking the trial court to hold Hartford liable for the entirety of the Equity South Judgment without permitting Hartford an opportunity to present defenses or challenge the sum of damages claimed by Plaintiffs. (App. 30-34; App. 35-47). Hartford filed its Memorandum in Opposition to Plaintiffs' Motion for Summary Judgment on January 13, 2012, and Plaintiffs filed their Reply Brief on March 2, 2012. (App. 48-70; App. 73-77). Plaintiffs and Hartford argued the Motion for Summary Judgment before the trial court on March 7, 2012. (App. 78-90). The trial court held the Motion for Summary Judgment in abeyance and ordered the parties to submit Proposed Findings of Fact and Conclusions of Law, which they did in a timely fashion. (App. 91-106). Hartford's Proposed Findings of Fact and Conclusions of Law were supplemented with an affidavit submitted by its lead counsel, Archibald Wallace, III (App. 107-110), and exhibits detailing the history of the Putnam County case, the settlement, and the competing claims for the bond proceeds, among other things. (App. 111-321).

On March 27, 2012, the trial court entered a final order granting Plaintiffs' Motion for Summary Judgment and entering judgment against Hartford in the amount of \$50,000, the penal

sum of the bond. (App. 322-328). As a result, Hartford never had an opportunity to present any substantive or procedural defenses to Plaintiffs' allegations. A further effect of the trial court's ruling is that Plaintiffs have essentially been awarded a windfall: the loan and deed of trust against Plaintiff Rhodes' property have been stricken, and Plaintiffs' credit has been repaired; yet they seek an additional \$50,000 for unspecified, unproven, fictional damages. Hartford's Notice of Appeal was timely filed on April 23, 2012. (App. 1).

SUMMARY OF ARGUMENT

In this appeal, Hartford seeks vacation of the final judgment against it, reversal of the trial court's decision to award summary judgment in Plaintiffs' favor, and remand to the trial court to permit Hartford to assert any and all defenses available to it as provided by West Virginia Code § 45-1-3. In the alternative, Hartford seeks a setoff against the judgment entered against it in such amount as will reflect the settlement entered into by Plaintiffs in the Putnam County case. The Court must decide whether the obligation to pay under the mortgage broker bond issued by Hartford, as surety, was triggered when Plaintiffs obtained a default judgment against Hartford's principal, Equity South, in a separate action in which Hartford was never given notice. Should the Court find that Hartford is bound by the Equity South judgment, it must also decide whether Hartford is entitled to a credit for the favorable settlement obtained by Plaintiffs from Equity South's joint tortfeasors.

The effect of the trial court's ruling is that the statutory mortgage broker bond required for all mortgage brokers is a "judgment bond" and concomitantly, that any surety providing such a bond is not entitled to notice of a lawsuit against its principal or to assert any defenses which would have been otherwise available to it or its principal. In so ruling, the trial court has eviscerated West Virginia Code § 45-1-3. The trial court's ruling is erroneous because the bond

does not fall as a “judgment bond” under the narrow exception to § 45-1-3 set forth in State v. Myers, 74 W.Va. 488, 491, 82 S.E. 270, 271-72 (1914), which applies only where the surety “expressly agrees to pay a judgment recovered against its principal.” Rashid v. The United States Fid. & Guar. Co., No. 2:91-0141, 1992 U.S. Dist. LEXIS 22914, *15 (S.D. W.Va. Sept. 28, 1992).

The bond does not contain an agreement to pay any judgment recovered against Equity South, and the statute requiring the Bond does not require such an agreement. But even if such an agreement could be implied in the Bond, the West Virginia Division of Banking lacked the authority to require a mortgage broker bond which permits a plaintiff to subject a surety to execution on a default judgment obtained against the principal. No such authorization appears in the West Virginia Code, and the Division of Banking may not exercise powers not expressly delegated to it under long-standing principles of West Virginia law.

Because it contains no automatic forfeiture provision appears in it – and one cannot be implied using inapplicable rules of construction – the bond is in the nature of a performance bond and Hartford is entitled to assert all the defenses that Equity South could have raised, or that might otherwise be available to Hartford as a surety. A decision in Hartford’s favor would best further the statutory scheme surrounding surety bonds in that it would preserve the expectations of sureties and their principals while disfavoring windfalls. It would also be consistent with fundamental principles of surety law which recognize a surety’s right to notice and an opportunity to be heard when its principal is accused of wrongdoing. This Court should also preserve the principle of fundamental fairness which militates against finding a party liable without an opportunity to be heard.

Finally, in the alternative, Hartford maintains that it should receive credit for the settlement reached by Plaintiffs with Nationstar and the Bank of New York, Equity South's joint tortfeasors in the Putnam County case. The record reflects that Plaintiffs have received one full recovery for the alleged misrepresentations and other tortious conduct of the defendants in the Putnam County case. To permit Plaintiffs to recover further money damages from Hartford would create a windfall, thereby conflicting with this Court's decision in Bd. of Educ. of McDowell County v. Zando, Martin & Milstead, Inc. (hereinafter "Zando"), 182 W.Va. 597, 390 S.E.2d 796 (1990), which established a *pro tanto* credit for pretrial settlements in favor of non-settling parties. Hartford's inchoate right of contribution against Nationstar and the Bank of New York has also been destroyed, leaving Hartford with no opportunity to offset its loss if the judgment against it is upheld.

STATEMENT REGARDING ORAL ARGUMENT AND DECISION

Hartford respectfully submits that this appeal should be orally argued before the Court. None of the criteria under Rule 18(a) of the West Virginia Rules of Appellate Procedure is met in this matter. The parties have not waived oral argument and this appeal is not frivolous. The dispositive issues in this case have not been authoritatively decided by this Court; in fact, along with the currently pending case Hartford Fire Ins. Co. v. Curtis, Record No. 12-0037,² this case appears to be one of first impression in West Virginia. The decisional process would be significantly aided by oral argument because the issues to be decided rest on fundamental questions of statutory interpretation, regulatory authority and surety law.

² Curtis has been fully briefed and is currently awaiting scheduling of oral argument or the issuance of a memorandum decision. Hartford, who is also the Petitioner in Curtis, has also requested oral argument in that case, and does not object to the consolidation of the two cases insofar as the arguments and law in relation to Assignments of Error No. 1 and 2 are substantially identical. The parties in Curtis are represented by the same counsel as in this matter.

Hartford requests that oral argument be heard pursuant to Rule 20 of the West Virginia Rules of Appellate Procedure. No appellate court sitting in West Virginia has ever ruled on whether a mortgage lender or broker bond is a judgment bond, or whether the surety on these bonds is entitled to the protections afforded to sureties in West Virginia Code § 45-1-3. Nor has any appellate court in West Virginia ruled on whether a surety is entitled to a settlement credit on a judgment obtained against its principal. With numerous plaintiffs now pursuing default judgments against defunct mortgage lenders and brokers after the collapse of the mortgage market, this Court has an opportunity to define the rights of sureties and consumers in cases pending in circuit courts across the state. This Court should not reach a decision on these important issues without the benefit of the maximum time of oral argument permitted by the Rules.

ARGUMENT

I. Standard of Review

A circuit court's decision to grant summary judgment is reviewed *de novo*, and this Court applies the "same standard for summary judgment that is to be followed by the circuit court." Cottrill v. Ranson, 200 W.Va. 691, 695, 490 S.E.2d 778, 782 (1997). It has "long held that 'a motion for summary judgment should be granted only when it is clear that there is no genuine issue of fact to be tried and inquiry concerning the facts is not desirable to clarify the application of the law.'" Baldau v. Jonkers, 725 S.E.2d 170, 178 n.11 (W.Va. 2011) (quoting Syl. pt. 3, Aetna Cas. & Sur. Co. v. Fed. Ins. Co. of New York, 148 W.Va. 160, 133 S.E.2d 770 (1963)). "[T]he circuit court's function at the summary judgment stage is not to weigh the evidence and determine the truth of the matter, but is to determine whether there is a genuine issue for trial." Frederick Mgmt. Co. v. City Nat'l Bank, 723 S.E.2d 277, 285 (W.Va. 2010). This Court will

“reverse a circuit court’s award of summary judgment if there is a genuine issue of material fact to be resolved or if, as a matter of law, the moving party is not entitled to the judgment.”

Cottrill, 200 W.Va. at 695, 490 S.E.2d at 782.

II. Statutory and Regulatory Background

Chapter 31, Article 17 of the West Virginia Code, known as the West Virginia Residential Mortgage Lender, Broker and Servicer Act (the “Act”), governs entities which originate and service residential loans. To do business in West Virginia, a mortgage broker is required to maintain a license administered by the West Virginia Commissioner of Banking (the “Commissioner”). W.Va. Code § 31-17-2(a). A broker applying for a license must comply with the applicable requirements of West Virginia Code § 31-17-4, including subsection (f), which states in relevant part:

At the time of making application for a broker’s license, the applicant therefor shall...

(3) File with the commissioner a bond in favor of the state for the benefit of consumers or for a claim by the commissioner for an unpaid civil administrative penalty or an unpaid examination invoice in the amount of \$50,000 for licensees with West Virginia loan originations of \$0 to \$3 million ... in a form and with conditions as the commissioner may prescribe and executed by a surety company authorized to do business in this state[.]

The West Virginia Code contains several provisions specifically governing mortgage broker bonds but does not expressly provide for any required language.³ Nor does the Code set

³ Following is a comprehensive list of the statutory provisions dealing with mortgage broker bonds in West Virginia. Subsection (g) of West Virginia Code § 31-17-4 provides that the aggregate liability of a surety on a bond issued pursuant to subsection (f) cannot exceed the face amount of the bond. Subsection (i) gives the Commissioner the discretion to reduce or waive the bond amount for nonprofit entities. Subsection (k) gives priority to consumer restitution claims against such bonds over claims submitted by the Commissioner for a civil administrative penalty or an unpaid examination invoice. West Virginia Code § 31-17-6 requires a broker to keep the bond in full force and effect, and § 31-17-12(a)(4) permits the Commissioner to revoke or suspend a broker’s license should it fail to do so. No other provisions of the Code contain requirements relating to mortgage broker bonds.

forth the appropriate parties or the conditions which must be satisfied to maintain an action against the bond. Significantly, the Code does not specify or imply that a mortgage broker bond is a payment, forfeiture or judgment bond.

Pursuant to the statutory authority granted by West Virginia Code § 31-17-4(e)(3), the Commissioner wrote a bond form which must be used by mortgage brokers and their sureties. The Bond here was written on the Commissioner's mandatory form. The pertinent language in the Bond reads:

NOW, THEREFORE, if the said principal EQUITY SOUTH MORTGAGE, LLC shall conform to and abide by the provisions of said Act and of all rules and orders lawfully made or issued by the Commissioner of Banking thereunder, and shall pay to the State and shall pay to any such person or persons properly designated by the State any and all moneys that may become due or owing to the State or to such person or persons from said obligor in a suit brought by the Commissioner on their behalf under and by virtue of the provisions of said Act, then this obligation will be void, otherwise it shall remain in full force and effect. If any person shall be aggrieved by the misconduct of the principal, he may upon recovering judgement against such principal issue execution of such judgement and maintain an action upon the bond of the principal in any court having jurisdiction of the amount claimed, provided the Commissioner of Banking assents thereto.

(App. 15).⁴

Chapter 45 of the West Virginia Code, entitled "Suretyship and Guaranty," contains general provisions applying to all surety bonds. Most relevant to this appeal is West Virginia Code § 45-1-3, which states in part:

no judgment, decree or recovery rendered, entered, or had in any suit, action, prosecution or proceeding, to which the surety ... was not a party regularly served with process, shall be in any wise binding on such surety ... and, notwithstanding such decree, judgment or recovery, the surety ... shall be allowed to make any such defense in any action, suit or proceeding instituted against him, as could have been made in the suit in which such decree, judgment or recovery was had.

⁴ The fully executed bond was not made part of the record, but the parties agree that the unsigned document at App. 15 is a full and accurate representation of the operative language of the bond.

There is no statutory language or case law suggesting that the general surety provisions in Chapter 45 of the Code are not applicable to bonds issued pursuant to the Act.

Assignment of Error No. 1:

The trial court erred in disregarding West Virginia Code § 45-1-3 and holding that a surety on a statutory mortgage broker bond issued in the form and in the language established by the Commissioner of Banking is automatically responsible for paying any judgment rendered against its principal.⁵

III. The Bond is Subject to the General Rule Set Forth in W. Va. Code § 45-1-3.

The plain language of West Virginia Code § 45-1-3 is directly applicable to the facts of this case and must be considered to determine the rights of the parties to the Bond. It is uncontested that Hartford, a surety, was “not a party regularly served with process” at the time Plaintiffs obtained a default judgment against Equity South, Hartford’s principal. Hartford was unaware, until after the Equity South Judgment had been awarded, that any claim had been initiated against Equity South or that the Putnam County case had been filed. Nothing in the Complaint or Plaintiffs’ subsequent pleadings contradicts this fact. Under the plain language of West Virginia Code § 45-1-3, Hartford is not bound by the Equity South Judgment. Notwithstanding the Equity South Judgment, it should be allowed to make any defense which would have been available to Equity South, or to Hartford otherwise, had the judgment not been entered. See State v. Duggan, 102 W.Va. 312, 315-16, 135 S.E. 270, 271 (1926) (where the surety was not made a party in the suit against its principal, the precursor to West Virginia Code § 45-1-3 permitted it to interpose a defense which the principal failed to assert). Summary

⁵ Hartford’s arguments relating to this Assignment of Error were presented to the trial court in its Memorandum in Opposition to Plaintiffs’ Motion for Summary Judgment Regarding Hartford Fire Insurance Company Bond, (App. 51-60), its Proposed Findings of Fact and Conclusions of Law, (App. 97-101), and the arguments made by its counsel during oral argument on Plaintiffs’ Motion for Summary Judgment. (App. 81-84).

judgment was inappropriate here and Plaintiffs' case against Hartford should be tried on the merits.

IV. The Exception Set Forth in Myers Does Not Apply.

Hartford argued orally and in its brief opposing summary judgment that West Virginia Code § 45-1-3 entitles it to present its defenses notwithstanding the Equity South Judgment. (App. 51-60, 97-101). The trial court declined to follow West Virginia Code § 45-1-3, invoking an exception which has no application to the bond. It ruled that a judgment creditor has a right to immediately collect against a mortgage broker bond regardless of how the judgment was obtained or what defenses might have been available. In doing so, the trial court ignored bond language giving an aggrieved person who obtains a judgment against the principal the right only to “maintain an action upon the bond of the principal.” (App. 142). The trial court found that the bond was a “judgment bond” because “the only condition that must be met by the plaintiffs is a judgment against the principal,” without analyzing the rights Plaintiffs enjoy under the bond language by virtue of obtaining the judgment. (App. 325-326). A review of Myers, 74 W.Va. 488, 82 S.E. 270, the case relied on by the trial court in holding that § 45-1-3 is not applicable to mortgage broker bonds, shows that this Court intended for the exception to be narrow. Courts should only apply the Myers exception where the surety *explicitly* grants the right to recover against the bond immediately upon a judgment against the principal.

In Myers, the court considered a “retail liquor dealer’s license bond” which was “conditioned as required by Sec. 28, Ch. 32, serial section 1144, Code 1913.” Myers, 74 W.Va. at 488, 82 S.E. at 271. The specific language of the Myers bond is not included in the opinion; however, at the time Myers was decided, the statute mandating a liquor dealer’s license bond required compliance with the following conditions:

No county or license court nor town council shall authorize the issuing of any license to sell spirituous liquors ... until the applicant shall have given bond with good security ... in the penalty of at least [\$3,500] ... and with the further condition, that he will pay all such damages and costs as may be recovered against him by any person under any of the provisions of chapter thirty-two of the code of West Virginia, as amended. And such applicant *and his securities* in said bond *shall be liable*, in a suit or suits thereon, *for the fine and costs which may be recovered against him* for any offence under this chapter which is a violation of any of the conditions of said bond, *as well as for the damages* hereinbefore provided for, until the penalty of such bond is exhausted.

W.Va. Code, 1913, sec. 28, ch. 32, serial section 1144 (emphasis added). The verb phrase “shall be liable,” coupled with the modifier “for the fine and costs which may be recovered against [the principal],” demonstrates that a surety issuing a bond of the type discussed in Myers clearly relinquishes the right to defend its statutory right to defend on the merits granted by § 45-1-3.⁶ This Court held that inasmuch as the sureties in Myers had expressly contracted away their rights under the precursor to § 45-1-3, they were liable as a matter of law for a judgment against their principals. Myers, 74 W.Va. at 493, 82 S.E. at 272; see also Rashid, 1992 U.S. Dist. LEXIS 22914 at *15 (“In refusing to strictly construe the statute, the court in Myers concluded that the legislature had not intended to impair the right to contract”). The deciding factor in Myers was that the surety “expressly stipulated” that paying such a judgment or fine “shall be the condition of his bond; it is the very thing which he has agreed to pay.” Myers, 74 W.Va. at 492, 82 S.E. at 272.⁷ Of particular importance to the Court was the need to preserve the “express undertaking of

⁶ The precursor to West Virginia Code § 45-1-3 was, at the time Myers was decided, a portion of former Code Ch. 37, Acts 1907. See Myers, 74 W.Va. at 491, 82 S.E. at 271. The relevant language of the statute is not materially different today.

⁷ Similarly, the Texas Court of Appeals decided Old Republic Sur. Co. v. Bonham State Bank, 172 S.W.3d 210 (Tex. App.-Texarkana 2005) -- upon which Plaintiffs relied heavily in their memorandum in support of summary judgment -- based on statutory language incorporated into the bond which provided that “[a] person may recover against a surety bond ... if the person obtains ... a judgment assessing damages and reasonable attorney’s fees based on an act or omission on which the bond is conditioned.” See id. at 212, 214-15; Tex. Transp. Code § 503.033(d). No such statutory directive exists in West Virginia as to mortgage broker bonds.

the surety.” Myers, 74 W.Va. at 491, 82 S.E. at 271. Thus, the Myers exception only applies where the surety expressly agrees to pay or to become liable for any judgment rendered against its principal. It is in only in such an instance that a surety can be said to have waived or contracted away its § 45-1-3 rights.

The Bond must be evaluated according to its plain language and the statute calling for its issuance. See Rashid, 1992 U.S. Dist. LEXIS 22914 at *17-18 n.6 (“the deciding factor in Myers is an analysis of the surety’s contractual obligation under the bond”). The clear language of the bond establishes that Hartford never agreed to pay unquestioningly any judgment rendered against its principal, and that Hartford is entitled to the protection provided by § 45-1-3. The obligation bonded is the principal’s compliance with state law, rules and orders relating to mortgage brokers, and the principal’s payment of any moneys due to the State or persons designated by the State pursuant to a lawsuit brought by the Commissioner of Banking.⁸ According to the explicit language of the bond, the surety has no obligation unless the principal fails to comply with state law as it applies to mortgage brokers. Because the bonded obligation is Equity South’s proper performance of its duties under the Act, the bond is in the nature of a performance bond: the principal must perform its work in accordance with state law.

Hartford did not make any agreement or pledge in the bond to become summarily liable for any judgment rendered against its principal. That would have significantly expanded its

⁸ The precise language of this Bond provision is contained in § II above but is reprinted here for easy reference:

NOW, THEREFORE, if the said principal EQUITY SOUTH MORTGAGE, LLC shall conform to and abide by the provisions of said Act and of all rules and orders lawfully made or issued by the Commissioner of Banking thereunder, and shall pay to the State and shall pay to any such person or persons properly designated by the State any and all moneys that may become due or owing to the State or to such person or persons from said obligor in a suit brought by the Commissioner on their behalf under and by virtue of the provisions of said Act, then this obligation will be void, otherwise it shall remain in full force and effect.

obligation. See State v. Abbott, 63 W.Va. 189, 194, 61 S.E. 369, 371 (1907) (“As the sureties did not stipulate that they would abide by the judgment against the principal, or permit him to conduct the defense, and be themselves responsible for the result of it, the fact that the principal has unsuccessfully defended, has no effect on their rights”) (quoting Pico v. Webster, 14 Cal. 202, 204 (1859)). In contrast to Myers, no such agreement appears in the bond issued by Hartford or the statute requiring issuance of the bond, and one cannot be created by implication.

[W]here the surety is not a party as contemplated by the statute and there is *no contractual agreement to pay a judgment*, the statute allows the surety of a principal who fails to present his own defenses to “interpose the defenses its principal might have interposed in the suit in which the decree or recovery was had.”

Rashid, 1992 U.S. Dist. LEXIS 22914 at *15 (quoting Duggan, 102 W.Va. at 315, 135 S.E. at 271 (1926)) (emphasis added).

In its March 26, 2012 Order, the trial court confused Plaintiffs’ *condition* for recovery with the *remedy* provided to them. As third-party beneficiaries of the bond not in privity with the surety, Plaintiffs are limited to those rights of recovery specifically afforded to them by the bond language. That they satisfied the requirement contained in the bond is not enough to trigger automatic forfeiture. The bond does not say that Hartford is obligated to pay the judgment against its principal. It merely gives the right to “maintain an action” against Hartford. There is a wide difference between the right to maintain an action and the right to summary judgment which destroys all defenses in that action. The right to recover against the surety in an “action” is not guaranteed because a surety defendant is entitled to present its defenses at trial. See Wellington Power Corp. v. CNA Sur. Corp., 217 W.Va. 33, 40, 614 S.E.2d 680, 687 (2005) (“a surety may set up in defense to an *action* against him any matter or any act of the creditor that operates as a discharge of the principal from liability”) (emphasis added).

The right to pursue an action directly against a surety is in addition to, but not dependent upon, the aggrieved person's right to issue execution of a valid judgment obtained against the principal. In this regard, the trial court seems to have conflated the general concepts applicable to recovery against an insurance carrier with those pertaining to a surety. A plaintiff in a typical insurance case must usually obtain a judgment against the insured before he or she can bring an action directly against the insurer. See Robinson v. Cabell Huntington Hosp., Inc., 201 W.Va. 455, 459-60, 498 S.E.2d 27, 31-32 (1997) ("As a general rule, in the absence of policy or statutory provisions to the contrary, one who suffers injury which comes within the provisions of a liability insurance policy is not in privity of contract with the insurance company, and cannot reach the proceeds of the policy for the payment of his claim by an action directly against the insurance company"). Having obtained a judgment, the plaintiff may garnish the insurance policy, and the insurer's defenses to the garnishment are very limited because West Virginia Code § 45-1-3 does not apply to insurance policies. Commercial Bank v. St. Paul Fire & Marine Ins. Co., 175 W.Va. 588, 596-597, 336 S.E.2d 552, 559-60 (1985).

By contrast, a plaintiff with rights against a principal guaranteed by a surety has two options: a direct action against both, or an action against one or the other followed by a subsequent action against the other, if there has not been one full recovery. Recognizing this, the legislature has seen fit to provide sureties with protections under § 45-1-3, including the right to defend an action on the merits. The Bond language in this case is consistent and harmonious with that right.

In awarding summary judgment to Plaintiffs, the trial court failed to consider whether Hartford had contracted away its § 45-1-3 rights, evidently agreeing with Plaintiffs' argument that no such rights exist unless reaffirmed or incorporated in the Bond itself. (App. 43). There is

no need for a reaffirmation of statutory rights to appear in the bond because § 45-1-3 adequately sets forth the rights of a surety whose principal has suffered a judgment without the surety's knowledge. See, e.g., Gen. Elec. Co. v. Nat'l Labor Relations Bd., 414 F.2d 918, 924 (4th Cir. 1969) (mere fact that an entity executed a contract which did not include a guarantee of its statutory rights did not constitute an effective waiver of those rights); Potesta v. United States Fid. & Guar. Co., 202 W.Va. 308, 315, 504 S.E.2d 135, 142 (1998) ("A waiver of legal rights will not be implied except upon clear and unmistakable proof of an intention to waive such rights"). The statutory rights guaranteed by § 45-1-3 apply to all surety bonds unless those rights are contracted away. The plain, unambiguous language of the Bond does not demonstrate any intent on the part of Hartford to waive its statutory rights. It stipulates that a judgment gives an aggrieved person the right only to "maintain an action upon the bond." Without evidence of Hartford's intent to waive or contract away its rights, it was error for the trial court to ignore the clear provisions of the statute and deprive Hartford of its right to defend itself on the merits.

V. The Rules of Contract Construction Cited by Plaintiffs Are Irrelevant to this Appeal.

In its final order, the trial court explicitly relied on Plaintiffs' argument that the language in the bond is to be construed against Hartford. (App. 325). Hartford's statutory rights cannot be forfeited by selective application of rules of construction. A rule of construction can only be applied where the language of a statute or bond is doubtful or ambiguous. See State v. Epperly, 135 W.Va. 877, 881-82, 65 S.E.2d 488, 491 (1951). "[A] valid written instrument which expresses the intent of the parties in plain and unambiguous language is not subject to judicial construction or interpretation but will be applied and enforced according to such intent." Wellington Power Corp., 217 W.Va. at 37, 614 S.E.2d at 684. The language of the Bond is clear and subject to only one interpretation. There is nothing ambiguous about bond language giving

an aggrieved person the right to “maintain an action” upon the occurrence of conditions precedent.

Even if the Bond’s language was ambiguous, the rule cited by the trial court – that surety bonds are to be construed against a compensated surety where the surety scripts the bond⁹ – is inapplicable. There is no evidence to suggest that Hartford had anything to do with scripting the bond. In fact, the bond is in the standard form set by the Commissioner of Banking. Plaintiffs cannot benefit from a rule of construction premised on circumstances which clearly are not present in this case. There are no grounds to construe the bond’s clear and unambiguous language against Hartford.

VI. The Kanawha County Circuit Court’s Order in Stayer Supports Hartford’s Position Here, and Hartford is not Estopped from Relying on its § 45-1-3 Protections Because of an Argument it Advanced and Lost in Another Case.

In reaching its decision to grant partial summary judgment, the trial court placed great weight on a perceived inconsistency between the argument advanced by Hartford in this case and a position it took in Stayer v. Litton Loan Servicing, et al., No. 08-C-3157 (Kanawha Co. Cir. Ct. Aug. 16, 2010), another case decided by the Kanawha County Circuit Court.¹⁰ Stayer involved a mortgage broker bond with substantially identical language to the bond in this case. (Exhibit A, 1). The plaintiff brought a lawsuit directly against a mortgage broker bond without first proceeding against the principal, which had filed for bankruptcy in Maryland. (Exhibit A, 1-2). Hartford, the surety on the mortgage broker bond, moved to dismiss the Complaint on the grounds that the bond language required the plaintiff to obtain a judgment against the principal

⁹ In its final order, the trial court gave Plaintiffs the benefit of the rule stated in City of Mullens v. Davidson, 133 W.Va. 557, 566, 57 S.E.2d 1, 7 (1949): “As a bond executed by a surety for compensation is usually expressed in terms prescribed by the surety, it will for that reason be strictly construed in favor of the obligee.” (App. 325).

¹⁰ While referenced during the hearing on Plaintiffs’ Motion for Summary Judgment, the Stayer order relied on by the trial court was never made part of the record below. It is attached hereto as **Exhibit A**.

before it could seek recovery against the bond. (Exhibit A, 2). The circuit court disagreed and denied Hartford's motion to dismiss, stating that the legislative intent in requiring a mortgage broker bond was to provide a remedy to consumers aggrieved by insolvent brokers. (Exhibit A, 3). The Stayer case is not harmful to Hartford's arguments herein for two reasons.

First, the circuit court in Stayer actually assumed the validity of the argument being advanced by Hartford in this matter: that a surety is always entitled to assert the defenses its principal could have asserted. Paragraph 14 of the Order in Stayer – an Order prepared by the same plaintiff's counsel as in this case – states:

The Court FINDS and CONCLUDES that Plaintiff should not be required to sit idle and await the conclusion of the [principal's] bankruptcy, or travel to Maryland to obtain an order from the bankruptcy court permitting the Plaintiff to pursue the claim against [the principal] notwithstanding the automatic stay with the understanding that judgment would be executed against the bond. After this delay and needless process, *Hartford would then be permitted to assert all defenses [the principal] could have asserted.*

(Exhibit A, 5-6) (emphasis added). The Stayer court denied the motion to dismiss, rejecting Hartford's proposed two-tier approach to recovery against mortgage lender bonds and mortgage broker bonds, where judgment against the principal would be a precondition to filing suit against the bond. Placing emphasis on the legislature's intent to provide a remedial source for consumers and the need to conserve judicial resources, it instead favored a single-tier approach: the consumer, in one action, can proceed (1) only against the surety, (2) only against the principal, or (3) against both simultaneously. (Exhibit A, 6). All three of these options permit a plaintiff to try his claims in one proceeding, but as the Stayer court clearly recognized, West Virginia Code § 45-1-3 provides protection to the surety if the plaintiff chooses to sue only the principal. The decision in Stayer was not appealed because under the framework recognized by

the circuit court, Hartford would have an opportunity to defend itself on the merits in future cases.¹¹

At the urging of Plaintiffs' counsel, the trial court in this case went one step further than Stayer and approved a zero-tier approach, holding that where the principal is insolvent or unresponsive (a frequent occurrence in these cases), a plaintiff can obtain a default judgment and immediately execute on it against the surety without being held to his burden of proof. This Court should definitively close the loophole opened by the trial court to ensure that Plaintiffs cannot enjoy a windfall recovery against a mortgage broker bond without being bothered to present evidence in support of their claims. See Hannah v. Heeter, 213 W.Va. 704, 715 n.10, 584 S.E.2d 560, 571 n.10 (2003) (acknowledging a "defendant's interest in not providing the plaintiff with a windfall recovery").

Secondly, Hartford cannot be estopped from arguing that it is entitled to notice and to assert its principal's defenses. While the trial court did not explicitly invoke estoppel, it implied in the final order that Hartford was somehow prevented from taking the position it took in this case due to its prior arguments in Stayer:

Even though Hartford argues now that the plaintiffs were required to provide notice and an opportunity to defend the underlying case against Equity, the court concludes this is inconsistent with Hartford's argument in Stayer v. Litton Loan Servicing. In Stayer, Hartford argued that the plaintiff had no standing to sue on the bond until he first obtained a judgment against the principal.

(App. 325-326) (citation omitted).

Hartford will discuss the estoppel issue here in an abundance of caution, since the Court has the discretion to address judicial estoppel *sua sponte*. See W. Va. Dep't. of Transp., Div. of Highways v. Robertson, 217 W.Va. 497, 503-04, 618 S.E.2d 506, 512-13 (2005).

¹¹ Stayer has since been resolved by the parties out of court.

“[J]udicial estoppel is a common law principle which precludes a party from asserting a position in a legal proceeding inconsistent with a position taken by that party in the same or a prior litigation.” Robertson, 217 W.Va. at 504, 618 S.E.2d at 513 (citation omitted). “Under the doctrine, a party is ‘generally prevented ... from *prevailing* in one phase of a case on an argument and then relying on a contradictory argument to prevail in another phase.’” Id. (quoting Pegram v. Herdrich, 530 U.S. 211, 227 n.8 (2000)) (emphasis added). Estoppel is “an extraordinary remedy that should be invoked only when a party’s assertion of a contrary position will result in a miscarriage of justice and only in those circumstances where invocation of the doctrine will serve its stated purpose.” Robertson, 217 W.Va. at 504, 618 S.E.2d at 513 (citation omitted). In Robertson, this Court established four threshold criteria to determine when the doctrine of judicial estoppel can be invoked.

[J]udicial estoppel bars a party from re-litigating an issue when: (1) the party assumed a position on the issue that is clearly inconsistent with a position taken in a previous case, or with a position taken earlier in the same case; (2) the positions were taken in proceedings involving the same adverse party; (3) the party taking the inconsistent positions received some benefit from his/her original position; and (4) the original position misled the adverse party so that allowing the estopped party to change his/her position would injuriously affect the adverse party and the integrity of the judicial process.

Id. at 506, 618 S.E.2d at 515.

Reasonable persons can disagree as to whether the position taken by Hartford in this matter is “clearly inconsistent” with the arguments it made in Stayer.¹² However, the second, third and fourth prongs of the Robertson analysis are obviously not met here. While they are represented by the same counsel, Plaintiffs are not related to or in privity with the plaintiff in Stayer. As to the third prong, Hartford did not receive any benefit from its arguments on its

¹² Even if these legal arguments were mutually inconsistent, Hartford is entitled to present competing legal positions regardless of consistency, even if they were in the same case. Rule 8(e)(2), West Virginia Rules of Civil Procedure.

motion to dismiss in Stayer because it lost that motion. Finally, there is no indication whatsoever that the arguments made by Hartford in Stayer misled Plaintiffs such that they were injuriously affected.

In sum, there is no reason to hold Hartford's previous unsuccessful legal arguments against it here. To the extent that the trial court intended to bar Hartford from asserting inconsistent legal positions between this case and Stayer, it operated under an impermissibly broad application of this Court's well-established rules of estoppel.

VII. The Commissioner of Banking Had No Authority to Require a Bond that Ignores a Mortgage Broker Bond Surety's Rights Under W. Va. Code § 45-1-3.

As argued above, the bond language does not permit a plaintiff to obtain a default judgment against a mortgage broker bond and immediately execute on it against the surety where the surety had no notice of the proceedings against its principal. But even if this Court were to agree with the trial court that the bond is a judgment bond such that it permits a "zero-tier" approach to recovery, it should hold that the bond language required by the Commissioner conflicts with the West Virginia Code and is therefore null and void. In the absence of authority to create a judgment bond, the bond should be void insofar as it conflicts with W. Va. Code § 45-1-3 by robbing Hartford of its right to defend itself on the merits.

West Virginia Code § 31-17-4(f)(3) requires a mortgage broker to maintain a bond "in a form and with conditions as the commissioner may prescribe and executed by a surety company authorized to do business in this state." This statutory language seems to grant wide latitude to the Commissioner in determining the appropriate parties to the Bond and the conditions under which the bond can be sued upon. However, the Commissioner cannot create conditions which conflict with clear statutory language. "There is no question that when the rules of an agency

come into conflict with a statute that the statute must control[.]” Respass v. Workers’ Comp. Div., 212 W.Va. 86, 102, 569 S.E.2d 162, 178 (2002). “It is fundamental law that the Legislature may delegate to an administrative agency the power to make rules and regulations to implement the statute under which the agency functions. In exercising that power, however, an administrative agency may not issue a regulation which is inconsistent with ... its statutory authority.” Lovas v. Consolidation Coal Co., 222 W.Va. 91, 96, 662 S.E.2d 645, 650 (2008) (quoting Syl. pt. 3, Rowe v. W. Va. Dept. of Corr., 170 W.Va. 230, 292 S.E.2d 650 (1982)); see also Boley v. Miller, 187 W.Va. 242, 246, 418 S.E.2d 352, 356 (1992) (agency’s statutory interpretation does not apply where it is “unduly restricted and in conflict with the legislative intent”).

If the Commissioner’s mandatory bond form truly does create a judgment bond as the trial court ruled, it is in direct conflict with W.Va. Code § 45-1-3. There is no evidence to suggest that the Legislature, in enacting West Virginia Code § 31-17-4(f)(3), intended to give the Commissioner the authority to formulate and require a surety bond that contradicts the general suretyship provisions in Chapter 45 and eviscerates the surety’s right to rely on the defenses its principal could have raised. Had the Legislature intended to require a judgment bond despite § 45-1-3, it could have easily done so. That it did not suggests that the Legislature intended to preserve the rights guaranteed to all sureties elsewhere in the Code when delegating the authority to the Commissioner to create the language to be used in mortgage broker bonds.

Because the Legislature did not specifically require a judgment bond or exempt mortgage broker bonds from the application of W.Va. Code § 45-1-3, West Virginia law requires the statutes to be given equal effect. This Court has held for over 100 years that statutes dealing

with the same subject matter must be read together and should be given equal effect where possible.

[W]here it is possible to do so, it is the duty of the courts, in the construction of statutes, to harmonize and reconcile laws, and to adopt that construction of a statutory provision which harmonizes and reconciles it with other statutory provisions to give force and effect to each, if possible.

State v. Williams, 196 W.Va. 639, 641, 474 S.E.2d 569, 571 (1996).¹³

West Virginia Code §§ 31-17-4(f)(3) and 45-1-3 can be interpreted in such a way as to give equal effect to each. Simply put, the Commissioner can require a mortgage broker bond with conditions that do not infringe on a surety's statutory right to assert the defenses of its principal. A mortgage broker bond purporting to contain provisions that exceed the Commissioner's authority by taking away these rights is void as to those provisions. This interpretation best harmonizes two potentially conflicting statutes and upholds the Legislature's intent. Accordingly, even if the Bond is intended to be a judgment bond, as the trial court ruled, it is void for lack of authority.

Assignment of Error No. 2:

The trial court erred in holding that a default judgment against a principal on a mortgage broker bond can be enforced against the surety where the surety does not receive notice of a claim against its principal until after judgment is rendered.¹⁴

¹³ See also Keatley v. Mercer County Bd. of Educ., 200 W.Va. 487, 495 n.15, 490 S.E.2d 306, 314 n.15 (1997) (quoting Williams); Syl. Pt. 5, Lawson v. County Comm'n, 199 W.Va. 77, 483 S.E.2d 77 (1996) ("where two statutes are in apparent conflict, courts must, if reasonably possible, construe such statutes as to give effect to each"); United Hosp. Ctr. v. Richardson, 757 F.2d 1445, 1451 (4th Cir. 1985) ("Should there be some inconsistency between the two statutes ... courts, in construing the statutes, so far as it is possible, should seek to steer a middle course that vitiates neither provision but implements to the fullest extent possible the directives of each") (citation omitted); Bldg. & Loan Ass'n v. Sohn, 54 W.Va. 101, 109-10, 46 S.E. 222, 225 (1903) ("Regard must be had to all the parts of a statute, and to the other concurrent legislation *in pari materia*; and the whole should, if possible, be made to harmonize; and if the sense be doubtful, such construction should be given, if it can be, as will not conflict with the general principles of law, which it may be assumed the legislature would not intend to disregard or change").

¹⁴ Hartford's arguments relating to this Assignment of Error were presented to the trial court in its Memorandum in Opposition to Plaintiffs' Motion for Summary Judgment Regarding Hartford Fire

VIII. Public Policy Considerations Weigh in Favor of Ensuring that a Surety is Entitled to an Opportunity to Defend Itself on the Merits.

In the proceedings below, Plaintiffs argued that the “statutory scheme” of the Act would be threatened by recognizing the rights of a surety on a mortgage broker bond under West Virginia Code § 45-1-3, and that the default judgment against Equity South should be just as binding on Hartford as though it were decided after a full trial on the merits. (App. 44).

Hartford argued in response that public policy considerations weighed in favor of giving sureties the right to notice and the opportunity to defend themselves on the merits. (App. 57-60). The trial court, relying on decisions from the United States Court of Appeals for the Ninth Circuit and an intermediate appellate court in Texas, agreed with Plaintiffs. (App. 326).

Notwithstanding the trial court’s decision, any threat to the statutory scheme of mortgage broker bonds is posed by Plaintiffs, who despite their professed concerns over fairness stand to gain a windfall if the judgment in this case stands.

Nothing in the West Virginia Code suggests that there is something exceptional about mortgage broker bonds which takes them out of the ambit of § 45-1-3, or that a surety bond which is “for the benefit of consumers” is somehow exempted from the general surety provisions of the Code. The “statutory scheme” of Chapter, 31 Article 17 of the Code would not be defeated by applying the clear language of § 45-1-3 to a mortgage broker bond just as if it were any other type of bond, and there is no inconsistency between the Act and the general surety provisions in Chapter 45. If allowed to stand, the trial court’s interpretation of the bond provisions would nullify the general statutory scheme of surety bonds by disregarding § 45-1-3 in the absence of any directive or authority to do so. Such a result cannot be accomplished by

Insurance Company Bond, (App. 57-60), and the arguments made by its counsel during oral argument on Plaintiffs’ Motion for Summary Judgment. (App. 85-86).

appeal to public policy when the purported “policy” is directly at odds with a statute that has existed for over 100 years – a statute whose purpose has been to prevent fraud, collusion and prejudice against sureties, and to preserve the fundamental right to notice of judicial proceedings before judgment can be rendered.

A fundamental policy consideration *was* ignored by the trial court, but it does not involve vague notions of “statutory scheme.” An important policy of the State is to preserve the expectations of parties to a contract by giving full meaning to language which is plain and unambiguous.

Where parties contract lawfully and their contract is free from ambiguity or doubt, their agreement furnishes the law which governs them. It is the duty of the court to construe contracts as they are made by the parties thereto and to give full force and effect to the language used, when it is clear, plain, simple and unambiguous.

Rollyson v. Jordan, 205 W.Va. 368, 376, 518 S.E.2d 372, 380 (1999) (quoting 4B MJ Contracts § 40, at 56 (Repl. Vo. 1986)). A surety issuing a mortgage broker bond in West Virginia expects that it will be permitted to assert defenses if a judgment is obtained against the principal without the surety’s knowledge, because it has made no explicit agreement to the contrary and the West Virginia Code guarantees that right.

Despite claiming otherwise, Plaintiffs would not be “forced” to “litigate their claims twice” if their motion is denied. If they wanted to avoid repetitious litigation, they had the option of suing Hartford at the same time they sued its principal – just as every other beneficiary of every other surety bond is required to do in West Virginia, and just as their counsel has done in other cases across the state. In truth, Plaintiffs have not tried their case even once. Equity South did not answer the Complaint in the Putnam County case and Plaintiffs took a default judgment against it without being required to introduce any proof of their allegations. They did

not submit an affidavit supporting their claim for damages or any other evidence suggesting that they sustained any injury whatsoever. By moving for and achieving summary judgment against Hartford, they have been awarded a windfall without having to introduce any proof at all, after intentionally keeping Hartford in the dark about their claim until the Equity South Judgment had been entered.

If summary judgment is upheld here, it is easy to imagine defunct mortgage lenders and brokers being targeted, with plaintiffs and their attorneys knowing full well that no defense will be attempted. Then, after the inevitable default judgment, the surety on the bond could be made summarily liable without ever having notice of the claim or an opportunity to defend on the merits until it was too late. The effect such a practice would have on the mortgage industry is obvious and significant: when faced with near-certain forfeiture every time a principal goes out of business, sureties would likely cease to issue mortgage lender and broker bonds. Lenders and brokers would pull out of the West Virginia market and it would become far more difficult for West Virginians to find affordable loans. The effect on the judicial system would be just as erosive, perpetuating a sham where liability is premised on a procedural shell game rather than the redress of wrongs.

It is precisely this sort of result that West Virginia Code § 45-1-3 is meant to avoid. Without an explicit, clear promise in the Bond to become liable for or to automatically pay any judgment against the principal, a surety should not be held to have waived its rights under § 45-1-3. Hartford has a clear statutory right to have its defenses heard on the merits and to hold Plaintiffs to their burden of proof. This Court should uphold the expectations of the parties to the bond and ensure that surety contracts are to be interpreted by their clear, unambiguous language in West Virginia.

IX. Commonly Accepted Principles of Surety Law Do Not Permit a Plaintiff to Enforce a Default Judgment Awarded Against a Principal Where the Surety Was Not Given Notice and Opportunity to Defend.

Where, as here, the bond is conditioned for performance of a duty, this Court applies the majority rule that a default judgment against a principal is only *prima facie* evidence against a surety and is subject to rebuttal. See Abbott, 63 W.Va. at 192-93, 61 S.E. at 370-71 (differentiating between a bond providing that “a principal will pay a certain sum of money or satisfy a judgment,” and a bond where the surety “merely stipulate[s] that the principal will perform his duties”). The Third Restatement of Suretyship and Guaranty goes one step further and provides that a default judgment against a principal is only evidence of its rendition and creates no presumption. It states:

When, in an action by the obligee against the principal obligor to enforce the underlying obligation, a judgment in favor of the obligee is obtained by default, confession, stipulation, or the like, the judgment against the principal obligor is evidence only of its rendition in a subsequent action of the obligee against the secondary obligor to enforce the secondary obligation.

RESTATEMENT (THIRD), Suretyship & Guaranty, § 67(3) (1995). The justification for applying a less oppressive rule to a surety whose principal has suffered a default judgment is provided in Comment (c):

the probative significance of a judgment obtained by confession, default, or the like is much less than that of a judgment after trial on the merits. Moreover, the arguments of policy and efficiency against duplication of trials have little weight where there has not been a determination made by a fact finder after consideration of evidence introduced by both sides to the litigation.

Id., Comment (c). Indeed, “default judgments have been a disfavored mechanism for case resolution” in West Virginia because of this Court’s “stated policy of preferring that cases be resolved on their merits.” The Hardwood Group v. LaRocco, 219 W.Va. 56, 66, 631 S.E.2d 614,

624 (2006) (Albright, J., concurring); see also, e.g., The Hardwood Group, 219 W.Va. at 62, 631 S.E.2d at 620 (acknowledging that the presence of a material issue of fact or a meritorious defense is one of the factors favoring the vacation of a default judgment). These concepts are particularly applicable in this case, where Plaintiffs have not been put to their burden of proof, and an adverse decision in this appeal would force them to litigate their claims only once.

The trial court cited Axess Int'l v. Intercargo Ins. Co., 183 F.3d 935, 940 (9th Cir. 1999) for the proposition that “a default judgment is just as binding upon a surety issuing a judgment bond as it is upon a surety where judgment is rendered after a trial.” In that case, the Ninth Circuit Court of Appeals found guidance from a treatise stating that a default judgment against a principal is enforceable against the surety “[w]here the very condition of the bond is the performance of a judgment against the principal, or that the surety will pay for all damages that may be awarded in an action brought against the principal.” Id. (citing 74 AM. JUR. 2D Suretyship § 153 (1974)). The bond in Axess stated that “the condition of this obligation is that the penalty amount of this bond [\$50,000] shall be available to *pay any judgment for damages* against the Principal...” Axess Int'l, 183 F.3d at 940 (emphasis in original). Because the bond was issued “specifically to pay any judgment for damages,” it was a judgment bond and the judgment against the principal was enforceable against the surety. Id. In other words, even if this Court were to follow the decision in Axess, the analysis is the same as it is when determining whether the Myers exception applies: does the Bond specifically provide that the surety will be liable for any judgment attained against its principal?

There is no specific agreement in the mortgage broker bond at issue in this case which would compel the same result as that reached in Axess. The obligation identified by the bond is not the payment of a judgment but the principal’s lawful performance of its activities as a

mortgage broker. The Bond cannot be classified as a “judgment bond” by implication, as the trial court ruled, because only a clear election to waive a statutory right can eliminate the right. See Winnings v. Wilpen Coal Co., 134 W. Va. 387, 390-91, 59 S.E.2d 655, 658 (1950) (property right cannot be relinquished “unless it clearly appears, by express words or by necessary implication,” that the right has been released or waived). Hartford is entitled to an opportunity to defend pursuant to the West Virginia Code, and it was error for the trial court to borrow inapposite case law from the Ninth Circuit when the statutes of this state guarantee a surety’s rights.

Assignment of Error No. 3:

The trial court erred in holding that a surety and its principal are not entitled to a setoff or credit against a judgment rendered against the principal despite the fact that the plaintiffs have already received one full recovery for their alleged injury.¹⁵

X. Plaintiffs Have Received One Full Recovery for the Indivisible Injuries Allegedly Caused by Equity South and its Joint Tortfeasors.

The record is clear that Plaintiffs have fully recovered for the alleged injuries which form the basis of the Putnam County case and the instant proceedings. Paragraph 1 of the Complaint in the Putnam County case stated, in part, “[t]he defendant lenders in this case joined with a participating broker¹⁶ and appraiser to induce the Plaintiffs into home loans that are not in their best interests.” (App. 111). Plaintiffs went on to allege that they “have been, through the routine business operation of these lenders/brokers, successively flipped into higher loans through (1) solicitation (2) bogus appraisal, and (3) a refinancing of inflated principal.” (App. 112). Equity

¹⁵ Hartford’s arguments relating to this Assignment of Error were presented to the trial court in its Memorandum in Opposition to Plaintiffs’ Motion for Summary Judgment Regarding Hartford Fire Insurance Company Bond, (App. 60-61), its Proposed Findings of Fact and Conclusions of Law, (App. 101-102), and the arguments made by its counsel during oral argument on Plaintiffs’ Motion for Summary Judgment. (App. 84-85).

¹⁶ I.e., Equity South.

South, along with Nationstar and Bank of New York, were named as codefendants in Count II – Unconscionability and Count III – Fraud. (App. 116-118). As a result of Equity South's failure to respond to the Putnam County litigation, it suffered a default judgment in the amount of \$56,300 which Hartford, as Equity South's surety, has now been called on to pay. (App. 291-292).

The August 4, 2010 Release and Settlement Agreement evidences the relief obtained by Plaintiffs from Nationstar and Bank of New York in exchange for their agreement to dismiss the Putnam County case as against those codefendants. (App. 64-70). By virtue of the settlement, Nationstar and Bank of New York (1) voided the loan and released Plaintiffs from making any further payments, (2) released the deed of trust on the property, and (3) deleted the trade line for the Plaintiffs' account for the purposes of reporting to credit bureaus. (App. 65). In other words, Plaintiff Rhodes now owns the property free and clear with no obligation to repay the loans and neither he nor Plaintiff Cochran will suffer any negative credit effects from the transaction.

The financial benefit enjoyed by Plaintiffs as a result of the settlement is significant. As reflected in the HUD-1 Settlement Statement for the 2004 loan, Plaintiffs had a pre-existing mortgage of \$24,272.60 paid off in full, received cash from the lender in the amount of \$21,817.12, and wound up with no outstanding debt or lien on the property. (App. 232). In sum, Plaintiffs have received \$46,089.72, plus the forgiveness of overdue payments and late fees. Yet, by virtue of the trial court's award of summary judgment, Plaintiffs now stand to recover an additional \$50,000 from Hartford for damages which have never been specified, substantiated, particularized, or proven. While Hartford denies that the trial court's entry of summary judgment against it was proper for the reasons stated above, at the very least Hartford is entitled to a credit against the judgment in the full amount of the August 4, 2010 settlement.

XI. Hartford is Entitled to a Credit Against the Judgment in the Full Amount of the August 4, 2010 Settlement.

“A familiar principle of law, requiring no citation of authorities, is that a plaintiff can have only one recovery for an injury.” Brewer v. Appalachian Constructors, Inc., 135 W.Va. 739, 747, 65 S.E.2d 87, 93 (1951). It is well established in West Virginia that a nonsettling defendant receives a “*pro tanto*, or dollar-for-dollar credit for partial settlements against any verdict ultimately rendered for the plaintiff.” Bd. of Educ. of McDowell County v. Zando, Martin & Milstead, Inc., 182 W. Va. 597, 606, 390 S.E.2d 796, 805 (1990) (hereinafter “Zando”). “[T]he office of compensatory damages is to make the plaintiff whole, but certainly not more than whole.” Id. at 608, 390 S.E.2d at 807. This doctrine applies even where the settling entities causing the loss were not parties to the instant action. Pennington v. Bluefield Orthopedics, P.C., 187 W. Va. 344, 350, 419 S.E.2d 8, 14 (1992) (applying credit in favor of doctor for plaintiff’s settlement with an independent tortfeasor prior to institution of a malpractice action).

Plaintiffs are entitled to only one satisfaction for their alleged injury. Because their injury is indivisible, Hartford, as a non-settling defendant, is entitled to a set-off for all sums paid in good faith by any parties who allegedly shares liability for the injury. See syl. pt. 7, Zando, supra. All compensation received by Plaintiffs from Nationstar and the Bank of New York was for the same injury for which Plaintiffs seek recovery from Hartford in this case: an unfavorable home loan resulting from unconscionable inducement and fraud. With that loan no longer in existence, Plaintiffs have realized a significant benefit for which Hartford should receive credit.

While the trial court acknowledged that Zando is controlling precedent on the issue of setoff, it took an unreasonably narrow view of this Court’s decision and failed to consider its rationale in recognizing a setoff. It held, “under Zando, the right to setoff only applies to

verdicts. Specifically, Zando provides that a setoff may only be performed after a verdict is returned and *before* a judgment is entered.” (App. 327) (emphasis in original). It is true that Zando dealt with the common circumstance of a non-settling defendant proceeding to trial after its codefendants elected to enter into pretrial settlements, but the rationale underlying Zando is just as applicable to the procedural history of the instant case.

In Zando, the Board of Education sued an architectural/engineering firm, a soil testing company, and a general contractor for negligence and breach of contract relating to defective construction work on a school in McDowell County. Zando, 182 W.Va. at 601-02, 390 S.E.2d at 800-01. Prior to trial, the Board settled its claim against the general contractor for \$600,000. Id. at 602, 390 S.E.2d at 801. During trial, the Board released the soil testing company in exchange for \$30,000. Id. At verdict, the only remaining defendant was the architectural firm. Id. The jury returned a verdict of \$1,000,000 in compensatory damages, and found the general contractor 75% at fault, the architectural firm 15% at fault, the Board 5% at fault, “others” 5% at fault, and the soil testing company not at fault. Id. at 602, 390 S.E.2d at 801. The circuit court refused to grant a credit to the architectural firm for the previous settlements and awarded the Board a final judgment of \$1,000,000. Id.

The Zando Court reversed the circuit court’s ruling and held that the architectural firm was entitled to a dollar-for-dollar credit in the amount of the settlements reached by the Board with the contractor and the soil testing company. Id. at 610, 390 S.E.2d at 809. In arriving at its decision, the Court discussed the termination of a defendant’s right of contribution when a joint wrongdoer settles with the plaintiff. Id. at 604, 390 S.E.2d at 803. Ordinarily, recognized the Court, a defendant has an “inchoate right of contribution,”¹⁷ which allows it to join a joint

¹⁷ The right is referred to as “inchoate” to distinguish it from the statutory right to contribution which arises from a joint judgment, as provided by W.Va. Code § 55-7-13.

tortfeasor in advance of judgment based on a cause of action for contribution. Zando, 182 W.Va. at 602, 390 S.E.2d at 801. “[J]oinder of contribution claims serves to ensure that those who have contributed to the plaintiff’s damages share in that responsibility.” Id. at 603, 390 S.E.2d at 802. As noted by the Court, however, an independent line of cases established “a practice of allowing the defendant against whom a verdict is rendered to reduce the damages to reflect any partial settlement the plaintiff has obtained from a joint tortfeasor.” Id. (citing Syl. pts. 1 & 2, Tennant v. Craig, 156 W.Va. 632, 195 S.E.2d 727 (1973); syl. pt. 2, Hardin v. The New York Cent. R.R. Co., 145 W.Va. 676, 116 S.E.2d 697 (1960) (“Where a payment is made, and release obtained, by one joint tort-feasor, the other joint tort-feasors shall be given credit for the amount of such payment in the satisfaction of the wrong”); syl. pt. 5, New River & Pocahontas Consol. Coal Co. v. Eary, 115 W.Va. 46, 174 S.E. 573 (1934) (“Partial satisfaction of the injured person by one joint tortfeasor is a satisfaction, *pro tanto*, as to all. To hold otherwise would entitle the injured party to multiple satisfaction—a surfeit not permitted by law”) (citing Bloss v. Plymale, 3 W.Va. 393, 409 (1869))).

The Court reconciled the right of inchoate contribution with the settlement credit afforded to non-settling defendants by holding that the right of contribution is extinguished as to any codefendant who settles with the plaintiff prior to the entry of judgment. See Zando, 182 W.Va. at 604, 390 S.E.2d at 803. This rule “furthers the strong public policy favoring out-of-court resolutions of disputes,” by ensuring the finality of the settlement and preventing a settling defendant from being subjected to additional liability determined in another suit in which he may not be a party. Id. at 604-05, 390 S.E.2d at 803-04. In return for the loss of the inchoate right of contribution, the non-settling defendant gets the benefit of a *pro tanto* settlement credit. “From a practical standpoint, the reduction of the verdict to reflect partial settlements counterbalances the

loss of the right of contribution, since the remaining defendants, who would otherwise have been entitled to such right, obtain the benefit of the settlement.” Zando, 182 W.Va. at 605, 390 S.E.2d at 804. “At the same time, the use of the verdict credit ensures against double recovery by the plaintiff.” Id. Based on these policy and practical concerns, the Court enunciated the following general rule: “We, therefore, conclude that a party in a civil action who has made a good faith settlement with the plaintiff prior to a judicial determination of liability is relieved from any liability for contribution.” Id. at 606, 390 S.E.2d at 805.

Under this well-established rule, Hartford is not entitled to any contribution from Nationstar or the Bank of New York because they have entered into full and final settlements of the indivisible loss allegedly caused by Equity South and the other defendants in the Putnam County case. Because this right has been taken away, it necessarily follows that Hartford is entitled to a credit for the benefit received by Plaintiffs as a result of that settlement. Plaintiffs would stand to recover a windfall double recovery if no credit is given. To permit them to do so would compromise the general principles set forth in Zando.

Contrary to the trial court’s creation of a bright-line rule applying a credit only where a jury verdict has been rendered and not yet reduced to judgment, the predecessors to Zando do not limit setoff credits to cases involving only a jury verdict. An early decision involving judgments against multiple defendants stated the following:

While a plaintiff in such case may proceed severally to final judgments, that prerogative does not imply the right to recover multiple remuneration. His damages are entire and single no matter the number who occasioned them. He is privileged to elect which judgment he will collect. The law must consider the judgment so elected as the full measure of his damages. Payment of that judgment in full will be held to make complete reparation for his wrong. When the wrong is repaired, the right of action is gone. Such payment therefore operates as a satisfaction of the other judgments, except as to costs[.]

Chewning v. Tomlinson, 105 W.Va. 76, 78-79, 141 S.E. 532, 533 (1928) (emphasis added).¹⁸ In Hardin, the Court applied the same concept to settlements. After citing the above language, it stated,

If a compromise settlement is made by one joint tort-feasor and a release obtained thereby, although it does not release other joint tort-feasors as to the entire claim for damages, it is well settled that such payment by one joint tort-feasor is a satisfaction *pro tanto*, as to all. *Pro tanto* means “for so much”. Therefore, where a partial payment is made by one joint tort-feasor, other joint tort-feasors shall be given credit for that much thereof in the satisfaction of the wrong.

Hardin, 145 W.Va. at 681, 116 S.E.2d at 701 (citations omitted). These decisions do not contain any limiting language which suggests that the setoff credit should be applied only to jury verdicts. Rather, the focus is on the prevention of multiple recoveries, and, particularly in Zando, striking a balance between a non-settling defendant’s right to contribution and the encouragement of out-of-court settlements.

Finally, in Tennant, this Court recognized the existence of a credit in a case where no jury verdict had been rendered. There, the plaintiffs were occupants of a vehicle involved in a three-car accident in which they were first struck head-on by a driver named Spitznogle, then rear-ended by a driver named Craig. Id. at 633-34, 195 S.E.2d at 729. The plaintiffs, who were infants, received court approval for a settlement under W.Va. Code § 44-10-14 with Spitznogle. Id. at 634, 195 S.E.2d at 729. They then sued Craig for their injuries. Id. The circuit court

¹⁸ Importantly, the Chewning Court also held that W.Va. Code § 55-7-12, then codified at section 7, Chapter 136, is not to be interpreted literally such that a plaintiff can enjoy more than one full recovery. Chewning, 105 W.Va. at 79-81, 141 S.E. at 533-34; see also New River, 115 W.Va. at 50, 174 S.E. at 575. The language of W.Va. Code § 55-7-12, which has not changed since Chewning was decided, states:

A release to, or an accord and satisfaction with, one or more joint trespassers, or tort-feasors, shall not inure to the benefit of another such trespasser, or tort-feasor, and shall be no bar to an action or suit against such other joint trespasser, or tort-feasor, for the same cause of action to which the release or accord and satisfaction relates.

dismissed the case on the grounds that the plaintiffs could not separate their injuries from the rear-end collision from those arising from the head-on collision, for which they had already received compensation. Tennant, 156 W.Va. at 635, 195 S.E.2d at 729-30. The case was appealed to this Court on numerous issues. Analyzing the effect of the settlement involving the head-on collision on the proceedings against the rear-ending vehicle, this Court noted, “the plaintiffs are entitled to only one satisfaction for the injuries suffered as a result of the accident,” and that the previous settlement was “a part of that satisfaction.” Id. at 636, 195 S.E.2d at 730.

After examining the decisions in Brewer, Hardin, and Eary, among others, the Court ruled:

while the plaintiffs are entitled to only one satisfaction for the injuries suffered by their minors, the payment received pursuant to the compromise settlement is satisfaction *pro tanto* but not necessarily full satisfaction. This settlement with and release of Spitznogle does not act as a bar to an action against Craig.

Tennant, 156 W.Va. at 637, 195 S.E.2d at 730. Continuing, the Court stated,

The burden, however, will be on the plaintiffs to prove that the concurrent negligence of defendant Craig and of Spitznogle, as a joint tort-feasor, was the proximate cause of the injuries and that the plaintiffs are entitled to damages in excess of the amounts paid as a result of the compromise and settlement with Spitznogle.

Id. at 639, 195 S.E.2d at 732 (emphasis added). The circuit court’s decision was reversed and the case was remanded for further proceedings. Id. at 640, 195 S.E.2d at 732.

It can be presumed from this language and the prior authorities that the credit for the Spitznogle settlement would have been applied had the plaintiffs gone on to prevail on summary judgment. There was no suggestion that the *pro tanto* satisfaction should only be recognized if the case proceeded to a jury verdict, and at that point in the case, no trial had occurred.

Here, the trial court’s final order does not consider the fact that Hartford has no right of contribution from Equity South’s joint tortfeasors as a result of Plaintiffs’ settlement with

Nationstar and the Bank of New York. Nor does it even mention the possibility that permitting Plaintiffs to recover the full bond amount from Hartford would reward them with a windfall double recovery. Instead, it constricts Zando to a narrow application that is wholly unjustified by either the rationale advanced in that case or the prior opinions relied on by this Court in deciding it. It was error for the trial court to refuse to apply a credit for the prior settlement, and its decision should be reversed.

Finally, it is anticipated that Plaintiffs will cite the trial court's finding of fact that "the amount of the settlement was influenced, at least in part, by the existence of the default judgment" as support for its argument that no credit should be applied to any judgment against Hartford. (App. 324). Even if true,¹⁹ this is irrelevant. Under Zando, the reasons for recognizing a settlement credit are to prevent a plaintiff from enjoying a double recovery and to maintain fairness in light of a non-settling defendant's loss of its inchoate right of contribution. Both of these protections will be ignored in this case if Plaintiffs are allowed to escape their loan through the settlement with the lender and then enjoy a \$50,000 windfall for unspecified, unproven damages. Hartford should not be required to make the Plaintiffs more than whole.

CONCLUSION

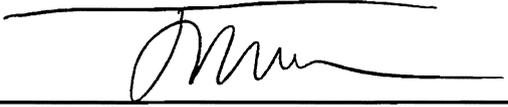
For the foregoing reasons, the trial court's award of summary judgment should be reversed and the proceedings remanded to the Kanawha County Circuit Court for trial on the merits. In the alternative, Hartford should be awarded an offset against the judgment rendered against it in the amount of the settlement between Plaintiffs, Nationstar Mortgage, LLC, and The Bank of New York Mellon.

¹⁹ There is no evidentiary support in the record for this finding of fact. The Release and Settlement Agreement signed by Plaintiffs makes no mention of it. (App. 322-28). The only basis the trial court had to make this finding was an assertion made by Plaintiffs' counsel during the hearing on the Motion for Summary Judgment. (App. 86).

Respectfully submitted,

HARTFORD FIRE INSURANCE COMPANY

By Counsel

A handwritten signature in black ink, appearing to read 'T Moran', is written over a horizontal line.

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IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

HARTFORD FIRE INSURANCE COMPANY,

Defendant Below/Petitioner,

v.

Record No. 12-0522

JERRY LEE RHODES and
BONNIE M. COCHRAN,

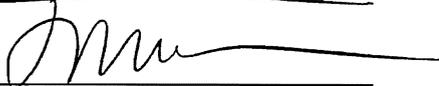
Plaintiffs Above/Respondents.

CERTIFICATE OF SERVICE

I, Thomas J. Moran, counsel for the Petitioner, Hartford Fire Insurance Company, do hereby certify that I have served a true and exact copy of the foregoing **PETITIONER'S BRIEF and the APPENDIX** upon counsel for the Respondents via U.S. Mail, this 27th day of July, 2012, as follows:

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