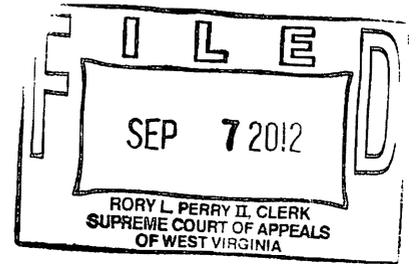


**IN THE
SUPREME COURT OF APPEALS OF
WEST VIRGINIA**



NO. 12-0522

**JERRY LEE RHODES AND
BONNIE M. COCHRAN,**

Respondents/Plaintiffs,

v.

HARTFORD FIRE INSURANCE COMPANY,

Petitioner/Defendant.

RESPONDENTS' BRIEF

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RESPONSE TO ASSIGNMENTS OF ERROR

Response to Assignment of Error No. 1:

The trial court properly applied W.Va. Code 45-1-3 and the general rules of construction when it concluded that the mortgage broker bond issued by the defendant, Hartford, was a judgment bond.

Response to Assignment of Error No. 2:

The trial court was right in concluding that the plaintiffs had satisfied the condition of the bond by obtaining a default judgment against the mortgage broker and, therefore, that the plaintiffs were entitled to judgment against the defendant, Hartford.

Response to Assignment of Error No. 3:

The trial court properly refused to grant a setoff for a settlement reached over a year after the default judgment was entered, particularly in light of the fact that no determination was ever made of the total amount of damages necessary to fully compensate the plaintiffs.

STATEMENT OF THE CASE

This is an appeal of a summary judgment entered against the defendant, Hartford Fire Insurance Company ("Hartford"), on a bond issued to a mortgage broker pursuant to W.Va. Code 31-17-4.

The Legislature enacted Chapter 31, Article 17 of the West Virginia Code as part of an overall effort to regulate mortgage lending and brokering. All businesses desiring to engage in mortgage brokering in the State of West Virginia are required to obtain a bond "for the benefit of consumers." The bond must be "in a form and with conditions as the commissioner [of banking] may prescribe." These bonding requirements are codified in West Virginia Code 31-17-4.

At all relevant times, Equity South Mortgage, LLC ("Equity") was a mortgage broker doing business in West Virginia. App3. The defendant, Hartford, issued a mortgage broker bond to Equity in the principal amount of \$50,000. The bond provided that if Equity engaged in misconduct violating Chapter 31, Article 17, then, upon recovering a judgment against Equity, anyone aggrieved by the misconduct could "maintain an action upon the bond...in any court having jurisdiction of the amount claimed." App15. The relevant text reads:

THE CONDITION OF THE ABOVE OBLIGATION IS SUCH THAT, WHEREAS, the above bound principal [Equity], in pursuance of the provisions of Article 17, Chapter 31, of the Code of West Virginia, as amended, (hereinafter the "Act") has obtained, or is about to obtain, from the Commissioner of Banking of the State of West Virginia, a license to conduct a Mortgage Lender business.

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 be come due or owing to the State or to such person or persons from said obligor in a suit brought by the Commission on their behalf under and by virtue of the provisions of said Act, then this obligation shall 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 [sic] against such principal issue execution of such judgement [sic] 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.* (emphasis added)

The plaintiffs, Jerry Lee Rhodes and Bonnie Cochran, reside in Putnam County, West Virginia. In 2003, the plaintiffs responded to a solicitation by Equity for a home improvement loan. Even though the home in question had no market value, Equity nevertheless obtained an inflated appraisal of the home's value so that a home improvement loan could be written. Furthermore, Equity misrepresented that the plaintiff, Bonnie Cochran, was a joint owner of the home so that her income could be used to justify the loan. App2-3.

In 2004, the plaintiffs' payments became difficult. Equity again solicited the plaintiffs for a loan, using the same predatory lending tactics as before. Equity also failed to make timely and accurate broker disclosures, charged an illegal broker's fee, and committed other violations of West Virginia's consumer laws. App4. All of this

conduct, as alleged, constituted violations of Chapter 31, Article 17 of the West Virginia Code.

The plaintiffs brought suit in Putnam County against Equity, among others, alleging fraud, statutory violations, and other claims arising out of this predatory lending scheme. Equity failed to answer the plaintiffs' complaint. Accordingly, the plaintiffs filed a motion for default judgment. On October 14, 2008, the trial court entered judgment against Equity in the amount of \$56,300. App5, 291.

Thereafter, the plaintiffs notified Hartford of the judgment and demanded payment under Equity's mortgage broker bond. Hartford refused. App5. In March, 2010, the plaintiffs brought suit against Hartford directly, seeking to recover the full \$50,000 available under the mortgage broker bond. On November 19, 2011, the plaintiffs filed a motion for summary judgment upon the bond. App30. The trial court entered an order on March 26, 2012 granting summary judgment in the plaintiffs' favor in the face amount of the bond, i.e., \$50,000, together with pre and postjudgment interest. App322. The trial court found that the bond was, in fact, a judgment bond, and that by obtaining the default judgment against Equity the plaintiffs had satisfied the condition of the bond:

5. Under the plain language of the bond, the only condition that must be met by the plaintiffs is a judgment against the principal, Equity, involving conduct violating the provisions of Article 17, Chapter 31 of the West Virginia Code.

* * * * *

7. From all of the foregoing the court concludes that the bond issued by the defendant, Hartford, is clearly a

judgment bond.

8. Under West Virginia law, a surety on a judgment bond is conclusively obligated to pay any judgment rendered against the principal *State vs. Myers*, 74 W.Va. 488, 82 S.E. 270 (1914).

9. The law does not distinguish between a default judgment and a judgment on the merits when determining a surety's payment obligations under a judgment bond.

10. A default judgment is just as binding upon a surety issuing a judgment bond as it is upon a surety where judgment arises from an adjudication on the merits.

App325-26 (3/27/12 Order Granting Plaintiffs' Motion for Summary Judgment, at 5, 7-10).

Hartford now appeals the trial court's summary judgment ruling. For the reasons set forth herein, the trial court's ruling was correct in all respects and, therefore, should be affirmed.

SUMMARY OF ARGUMENT

According to Hartford, it is not bound by the judgment against Equity and, therefore, "should be allowed to make any defense which would have been available to Equity, or to Hartford otherwise, had the judgment not been entered." PETITIONER'S BRIEF, AT 11. Hartford cites W.Va. Code 45-1-3, a general statute governing sureties. However, W.Va. Code 45-1-3 is inapplicable because the bond Hartford issued *is a judgment bond*.

Nearly 100 years ago, this court decided *State vs. Myers*, 74 W.Va. 488, 82 S.E.2d 270 (1914). *Myers* is controlling here. Like the present case, *Myers* involved a bond that was issued as part of a regulatory scheme enacted by the Legislature (i.e., the licensing and sale of liquor). *Myers* specifically held that judgment bonds fall outside of the scope of W.Va. Code 45-1-3. A judgment bond is one where the surety contracts to pay any judgment rendered against the principal. Thus, where a judgment bond is involved "the judgment against the principal...is conclusive evidence of the surety's liability." 74 W.Va. at 488, 82 S.E.2d at 272.

The trial court, examining the language of the bond issued by the defendant, Hartford, concluded that it, too, was a judgment bond. Therefore, under *Myers*, the judgment obtained by the plaintiffs against Equity was sufficient to trigger Hartford's obligation under the bond.

At various points throughout its brief, Hartford complains that it has been deprived of a "right" to notice and a defense. See, e.g., RESPONDENT'S BRIEF, AT 16-17, 23-24. In reality, Hartford is attempting to enforce a right which does not exist

under the West Virginia Code or under the language of the bond itself. Instead, Hartford is asking this court to rewrite its bond—and, in so doing, to upset the regulatory scheme codified in Chapter 31, Article 17.

Even if the court concludes that the plaintiffs are entitled to judgment upon the bond, Hartford nevertheless insists that it should receive a setoff for a settlement reached with the lender and the note holder. First and foremost, the default judgment against Equity does not represent full compensation for the plaintiffs' injuries, damages and losses. Without a determination of the total amount of damages necessary to fully compensate the plaintiffs, setoff is improper. Furthermore, the law only authorizes a setoff to be performed *after* a verdict has been returned and *before* a judgment has been entered. There is no law supporting the remedy Hartford seeks here—i.e., an amended judgment.

STATEMENT REGARDING ORAL ARGUMENT AND DECISION

This case presents a straightforward application of settled law. Hartford suggests in its brief that “[n]o appellate court sitting in West Virginia” has addressed the issue it seeks to raise herein. PETITIONER’S BRIEF, AT 8. However, these issues were addressed in *State vs. Myers*, 74 W.Va. 488, 82 S.E.2d 270 (1914) where this court expressly held that judgment bonds fall outside of the protection of W.Va. Code 45-1-3 because, by their very nature, they require no showing other than a judgment duly rendered against the principal.

Myers clearly applies and clearly is controlling. Three judges, sitting in three different judicial circuits, have all reached the exact same result citing *Myers*.¹ Accordingly, unless the court desires argument, it is respectfully submitted that oral argument is unnecessary and that the case should be disposed of by memorandum opinion.

¹ The other two cases are *Morgan vs. Hartford Fire Ins. Co.*, Civil Action No. 07-C-763DS (Mercer Cty 4/3/12), decided by Judge Swope, and *Curtis vs. HSBC Mortgage Services, Inc.*, Civil Action No. 08-C-157 (Jackson Cty. 7/13/11), decided by Judge Beane. *Curtis* is presently before this court.

ARGUMENT

Response to Assignment of Error No. 1:

The trial court properly applied W.Va. Code 45-1-3 and the general rules of construction when it concluded that the mortgage broker bond issued by the defendant, Hartford, was a judgment bond.

Hartford begins by citing W.Va. Code 45-1-3, which is a general statute governing sureties, guarantors, indorsers and others who may be secondarily liable for a debt. W.Va. Code 45-1-3 gives certain procedural protections, including the right to be served with process, answer and defend. Hartford argues that the judgment entered against it violated W.Va. Code 45-1-3 because it was deprived of these protections. Hartford acknowledges *Myers*, but says it is a “narrow” exception to this statutory provision. PETITIONER’S BRIEF, AT 12. In fact, Hartford appears to argue that W.Va. Code 45-1-3 confers specific rights upon sureties and, for the plaintiffs to prevail, they bear the burden of proving that Hartford actually “waived or contracted away its [statutory] rights.” ID., AT 14.

But none of this finds legal support. Instead, as *Myers* recognizes, there are simply two different species of bonds.

First, there are *performance* bonds. Through a performance bond, a surety actually guarantees the performance of an underlying contract. See, e.g., *Gateway Communications, Inc. vs. John R. Hess, Inc.*, 208 W.Va. 505, 541 S.E.2d 461 (2000)(“the purpose of a performance bond is to guarantee that the contractor will perform the construction contract”). For example, a surety may issue a bond to a contractor guaranteeing the timely completion of a highway construction project. If the

principal defaults (e.g., by failing to complete the project or by completing it in an unworkmanlike manner), the surety can complete the contract itself or pay damages up to the face amount of the bond. "If the surety does not do either of these things, the obligee can sue the surety on the bond." *Hanover Ins. Co. vs. Corpro Companies*, 312 F.Supp.2d 816, 822 (2004). In this setting, the surety is given a statutory right to appear and defend.

Second, there are *judgment* bonds. "A judgment bond is one in which the surety agrees to be liable for a judgment based on a specific violation covered by the bond." *Old Republic Surety Co. vs. Bonham State Bank*, 172 S.W.3d 210, 214 (Tex. Ct. App. 2005); see also 74 Am.Jur.2d, *Suretyship* §9. The surety's liability under a judgment bond is primary. For this reason, a judgment bond falls outside of W.Va. Code 45-1-3 and a surety writing a judgment bond is not entitled to any of its procedural protections. Instead, a judgment rendered against the principal is sufficient in and of itself to impose liability upon the surety.

Myers itself confirms this. In *Myers*, a retail liquor dealer obtained a bond to operate a liquor business. The bond was conditioned upon the dealer's compliance with state liquor laws, including laws prohibiting the sale of liquor to minors. The dealer did, in fact, make a sale to a minor, and, as a result, was subjected to a fine. Thereafter, the State of West Virginia attempted to collect the fine under the dealer's bond. The trial court treated the judgment against the dealer as conclusive proof of the surety's liability.

This court affirmed the trial court's ruling. The surety in *Myers* argued, as Hartford does now, that it was entitled to the procedural protections provided for under the predecessor to W.Va. Code 43-1-3.² But this argument was soundly rejected. Because the bond obligated the surety to pay any judgment rendered against the principal, proof of such a judgment--without anything more--was sufficient to recover upon bond:

The construction of the statute contended for by counsel for plaintiffs in error would produce great confusion in our present system of laws and would produce much useless and expensive litigation....Notwithstanding a surety had expressly undertaken to satisfy any judgment that may be rendered against his principal in any pending or contemplated suit or proceeding, he could, nevertheless, say that what he had agreed to do was not binding on him, and demand a retrial of the case against his principal, in an action against the surety on the bond. But the Legislature was not dealing with the subject of the right to contract, and therefore could not have intended such a result. *If a surety has obligated himself to pay a judgment or fine that may be imposed on his principal, why should not such judgment or fine determine his liability?* He has expressly stipulated that it shall be the condition of his bond; it is the very thing which he has agreed to pay. Our conclusion is that *in all such cases the surety is estopped, in the absence of fraud or collusion, to controvert the judgment recovered against his principal*, notwithstanding chapter 37, Acts 1907. It was not the purpose of said act to destroy the evidential character of a judgment against the principal alone, in a subsequent action against the surety on his bond to collect the judgment, wherein payment of such

² As Hartford notes, the statutory language of the predecessor to W.Va. Code 43-1-3 is materially the same.

judgment was a condition of the bond. 74 W.Va. at 488, 82 S.E.2d at 272 (emphasis added).

The rule from *Myers* can, therefore, be summarized as follows: W. Va. Code §45-1-3 **does not** apply to judgment bonds. This is so because the surety has contractually agreed to be bound by any judgment which may be rendered against the principal. Therefore, any such judgment is binding against the surety unless it can be proven that the judgment was obtained through fraud or collusion. *See also, Rashid v. United States Fid. & Guar. Co.* 1992 W.L. 565341, *5 (S.D.W.Va. 1992) (“[T]he court in *Myers* concluded that the legislature had not intended to impair the right to contract. Consequently, prior law holding that a judgment against a principal is conclusively binding against the surety when payment of the judgment is a condition of the bond remained unchanged by the statute.”).

The question, then, is not whether Hartford “waived or contracted away its [statutory] rights.” PETITIONER’S BRIEF, AT 12. The question is: Does the plain language of the bond provide that Hartford will pay any judgment rendered against its principal, Equity, for conduct which violates Chapter 31, Article 17 of the West Virginia Code? *See, e.g., Gateway Communications, Inc. vs. John R. Hess, Inc.*, 208 W.Va. 505, 541 S.E.2d 461 (2000) (“The liability of a surety...arises out of positive contract, and the contract...generally measures the extent of [the surety’s] liability”); Syl. Pt. 1, *Soliva vs. Shand, Morahan & Co.*, 176 W.Va. 430, 345 S.E.2d 33 (1986) (“[I]anguage in an insurance policy should be given its plain, ordinary meaning”).

In this regard, Hartford highlights the language differences between the bond in *Myers* and its own bond. But these differences are not substantive and they do not have any effect on the outcome.

As Hartford observes, *Myers* does not provide us with the actual text of the bond. However, we may gain insight from the language of the code provision requiring liquor dealers to obtain a bond. The key language, found in Code 1913 c. 32, §28, reads as follows:

And such applicant and his securities in said bond *shall be liable, in a suit or suits thereon, for the fines and costs which may be recovered against him* for any offense under this chapter which is a violation of any of the conditions of said bond, as well as for the damage as hereinbefore provided for, until the penalty of such bond is exhausted.

Interestingly, this language does not say that the bond is a “judgment” bond. For that matter, the word “judgment” does not appear at all. Instead, the code says simply that the surety “shall be liable...in a suit” for any fines or costs recovered against the principal. We may safely assume that the bond contained this language, or that the language was read into the bond as a matter of law. *State Road Comm’n vs. Curry*, 155 W.Va. 819, 824, 187 S.E.2d 632 (1972)(“a bond executed pursuant to a statutory requirement must be construed and applied in conformity with...the statutory language which prescribes terms and conditions of the bond so formulated and executed, whether the statutory language is or is not expressly and precisely stated in the bond”). In either event, *Myers* had no difficulty whatsoever concluding that the surety was liable for the judgment against the dealer, and that proof of the judgment was conclusive of the surety’s liability.

The language in Hartford's bond is even clearer. Importantly, the bond here specifically includes the word "judgment." In fact, the whole purpose of the language defining Hartford's obligation is to explain what happens *after a judgment against the principal has been obtained* (i.e., "upon recovering judgment against such principal"). The bond makes it clear that a judgment holder has two options for enforcing a judgment. First, he may seek recovery from Equity directly by "issu[ing] execution of such judgment." Second, he may seek recovery from Hartford directly by "maintain[ing] an action upon the bond."

Hartford interprets this language to mean that the plaintiffs can sue upon the bond, but that Hartford, nevertheless, can still raise any and all defenses it might possess. PETITIONER'S BRIEF, AT 15-16. This is nonsensical. To begin with, it simply ignores the context. The bond clearly contemplates a judgment against the principal, i.e., Equity. It then explains a judgment holder's enforcement rights. The judgment may be enforced against Equity by means of execution. Alternatively, it may be enforced against Hartford by means of "an action upon the bond." Hartford's interpretation would render the language meaningless by informing the judgment holder of a self-evident fact--i.e., that to recover upon the bond he must sue upon the bond. Under West Virginia law, a contract, including a bond or an insurance policy, should not be interpreted so as to create an absurdity. See, e.g., *Glen Falls Ins. Co. vs. Smith*, 217 W.Va. 213, 221, 617 S.E.2d 760, 768 (2005)("[a] contract of insurance should never be interpreted to create an absurd result, but should instead receive a reasonable interpretation").

Furthermore, Hartford itself recognizes that the bond is a judgment bond. In fact, Hartford has taken this very position in prior litigation. In *Stayer vs. Litton Loan Servicing*, No. 08-C-3157 (Kanawha Cty 8/16/10),³ the plaintiffs sued a mortgage broker for predatory lending practices. The broker was insolvent and was actively involved in federal bankruptcy proceedings. The plaintiffs, therefore, proceeded against Hartford as the surety which issued the broker's statutory bond. Hartford argued that a judgment against the principal was a condition precedent to recovery under the bond. As the trial court concluded, Hartford's argument here that it was entitled to notice and an opportunity to defend was "inconsistent with Hartford's argument in *Stayer*...that the plaintiff had no standing to sue on the bond until he first obtained a judgment against the principal." App326.⁴

Finally, Hartford's strained interpretation of its bonding obligation would have the effect of upsetting the statutory scheme.

Judgment bonds are purchased for the protection of those aggrieved by the principal's wrongdoing, particularly where the bond is statutorily required. In this case, we are dealing with Chapter 31, Article 17 of the West Virginia Code, which requires any mortgage broker doing business in West Virginia to obtain a bond for the protection of the public, including those who may be victimized by predatory and other illegal lending practices. To allow Hartford to avoid its obligations under the bond by arguing that it is not bound by the judgment entered against its principal, Equity, would

³ Hartford attached a copy of the *Stayer* opinion to its initial brief. The plaintiffs have no objection in light of the fact that *Stayer* was expressly referenced during oral argument of the summary judgment motion, App.81, and in the court's summary judgment order.

⁴ Hartford's specific arguments regarding the trial court's treatment of *Stayer* are dealt with at pp. 18-22.

defeat the entire statutory scheme. Indeed, victims of Equity's illegal conduct would be forced to litigate their claims *twice*—once against Equity (a defunct party which refused to even appear in the underlying case) and then again against the surety who, for valuable consideration, agreed to be bound by any judgment entered against Equity.

Hartford is certainly not prejudiced by having to honor the express terms of its bond and satisfy the judgment entered against its principal, Equity. Hartford has the ability and the right to pursue Equity for reimbursement of any payment it makes to the plaintiffs. West Virginia consumers, like the plaintiffs here, should not be required to bear the expense of pursuing a broker who may be out of business or without assets to satisfy a judgment where the Legislature saw fit to require a judgment bond for that very purpose. Hartford voluntarily agreed, for good and valuable consideration, to serve as Equity's surety and to pay *any* judgment rendered against Equity arising out of Equity's mortgage brokering business in the event Equity failed to do so. The judgment entered against Hartford is, therefore, consistent with the statutory purpose to insure that victims of illegal lending practices can be fully and expeditiously compensated through the proceeds of a judgment bond.

Thus, giving the language of the bond its plain, ordinary meaning, it is clear that the trial court reached the right conclusion: Hartford's bond is a judgment bond which falls outside of W.Va. Code 45-1-3.

Even if Hartford's bond is ambiguous, the rules of construction require a liberal interpretation of the bond's language. West Virginia strictly construes obligations

under a bond against the surety. *Elkins Manor Associates v. Eleanor Concrete Works, Inc.*, 183 W.Va. 501, 508, 396 S.E.2d 463, 470 (1990) (where “the surety is a corporation and supplies bonds for a consideration, the courts will construe the obligations of the bond most strongly against the surety.”); *City of Mullens v. Davidson*, 133 W.Va. 557, 566, 57 S.E.2d 1, 7 (1949) (“[A]s 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.”).

Hartford does not dispute these authorities, but argues that they are inapplicable because Hartford did not write the bond. Instead, the bond was written by the commissioner of banking. As Hartford puts it, the plaintiffs “cannot benefit from a rule of construction premised on circumstances which even they acknowledge are not present.” PETITIONER’S BRIEF, AT 18.

However, even in cases involving statutory bonds this court has applied the same rule of strict construction. For example, in *Cecil I. Walker Machinery Co. vs. Stauben, Inc.*, 159 W.Va. 563, 230 S.E.2d 818 (1976), a suit was brought against a contractor and its surety relating to a highway construction project. The nature and scope of the surety’s obligation under the bond were specifically set forth in W.Va. Code 17-4-20.⁵ Nevertheless, this court repeated the familiar rule that “courts will construe the obligation of [a] bond most strongly against the surety.” Moreover, the court noted: “Generally speaking, the courts have endeavored to extend the protection

⁵ W.Va. Code 17-4-20 provides, in relevant part, that in the event of a breach of the conditions of the bond the surety was obligated to “pay in full to the persons entitled thereto for all material, gas, oil, repairs, supplies, equipment, rental charges for equipment and charges for the use of equipment, and labor used by him in and about the performance of [the] contract.”

afforded by the statutory bond *as far as reason and logic will permit.*" 159 W.Va. at 568, 230 S.E.2d at 820 (emphasis added); see also *Hicks vs. Randich*, 106 W.Va. 109, 144 S.E. 887 (1928).

Furthermore, because the bonding obligation arises out of a statute, it is also necessary for the court to consider the legislative intent. "When the bond is given to meet statutory requirements, the question of construction is not merely a question of the intention of the parties, but becomes a question of what the statute requires, for the terms of the statute are ordinarily read into and form part of the statutory bond." 11 *Couch on Insurance*, 3d ed. §165:36. As noted previously, the intent of the Legislature in enacting Chapter 31, Article 17 of the West Virginia Code was to protect West Virginians who might suffer harm at the hands of unscrupulous brokers. The mortgage broker bond is an integral part of the Legislature's remedial scheme. Its purpose is to provide a quick, efficient, and inexpensive remedy in the event that the broker is incapable of paying a judgment rendered against it. Needless to say, it would defeat this remedial goal to require predatory lending victims to try their case *twice* simply to be compensated *once*. If, indeed, there is any ambiguity in Hartford's bond, then it must be resolved in the plaintiffs' favor to insure that the Legislature's remedial goal is fully effected. Accordingly, this court should affirm the trial court's ruling that Hartford's bond is a judgment bond and that the procedural protections provided for under W.Va. Code 45-1-3 are inapplicable.

Hartford devotes nearly four pages of its brief to the *Stayer* opinion, which was cited previously and which the trial court considered in its summary judgment ruling.

Hartford makes two arguments regarding *Stayer*. First, it says that *Stayer* actually supports the position it advances here. Second, it argues that the trial court improperly applied principles of judicial estoppel in its treatment of *Stayer*. Neither of these arguments is persuasive.

To begin with, Hartford suggests that the trial court “placed great weight” on *Stayer*. PETITIONER’S BRIEF, AT 18. However, in reality the trial court only addressed *Stayer* in two sentences. App325-26. Therefore, Hartford’s inconsistency in its position was merely one fact, among others, that the trial court considered in granting summary judgment.

Citing paragraph 14 of the *Stayer* order, Hartford says that “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.” PETITIONER’S BRIEF, AT 19. But this is a misunderstanding of the court’s ruling and rationale.

The mortgage broker in *Stayer* was a party to bankruptcy proceedings. It was impractical, if not impossible, for plaintiff to obtain a judgment against the broker. Therefore, the plaintiff proceeded directly against Hartford. The trial court concluded that it was unnecessary for the plaintiff to await the outcome of the bankruptcy or ask the bankruptcy court to lift the stay. It then noted: “After this delay and needless process, Hartford would then be permitted to assert all defenses [the broker] could

have asserted.”⁶ Thus, Hartford says, the trial court accepted the proposition that the surety is entitled in all cases to appear and defend.

But this goes far beyond the trial court’s ruling. Hartford’s bond was a judgment bond, and the trial court carved out an exception to the judgment requirement. The ongoing bankruptcy effectively prevented the plaintiff from suing the broker. Accordingly, the trial court found that the plaintiff could proceed directly against Hartford under those circumstances. However, *because there was no judgment against the broker* Hartford would have the right to appear and assert any defenses it might have.

Hartford next argues that the trial court improperly invoked the doctrine of judicial estoppel by “imply[ing]...that Hartford was somehow prevented from taking the position it took in this case due to its prior arguments in *Stayer*.” PETITIONER’S BRIEF, AT 19. The simple answer is that the trial court *did not* invoke judicial estoppel. The trial court was not preventing Hartford from advancing two inconsistent positions. Rather, it was simply recognizing the fact that Hartford was being disingenuous--taking inconsistent positions regarding the exact same bond in two different legal proceedings. Hartford’s acknowledgment in prior litigation that a judgment was a condition precedent was a fact that the court considered, along with the language of the bond, the statutory intent, etc. In fact, it is clear from the summary judgment order that the court *first* determined from the plain, ordinary language of the bond that it was a judgment bond. This conclusion was reinforced by the fact that Hartford itself had

⁶Reference is made to paragraph 14 of the *Stayer* opinion which is attached as an exhibit to Hartford’s brief.

acknowledged as much in the context of the *Stayer* case. Thus, Hartford's judicial estoppel arguments are simply misplaced.

Finally, Hartford suggests that the banking commissioner had no authority to require a judgment bond: "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." PETITIONER'S BRIEF, AT 23.

In making this argument, however, Hartford is engaging in misdirection. Hartford begins by repeating its false premise that W.Va. Code 45-1-3 somehow confers substantive rights which cannot be taken away. As we have seen, W.Va. Code 43-1-3 simply recognizes that sureties have certain procedural rights in the context of *performance* bonds. Where, however, a *judgment* bond is involved, these procedural rights do not come into play because the surety is simply being asked to do what it contracted to do--i.e., pay the judgment.

Therefore, the question is not whether the commissioner exceeded her authority by requiring a bond that conflicts with W.Va. Code 43-1-3. The question is simply one of statutory construction: Does W.Va. Code 31-17-4 give the commissioner authority to require a judgment bond? The answer, clearly, is yes because the Legislature gave the commissioner the fullest possible grant of authority. Under W.Va. Code 31-17-4(e)(3), the bond must be "in a form and with conditions *as the commissioner may prescribe.*" Clearly, then, the Legislature concluded that the commissioner, with her specialized knowledge and experience, was in the best position to dictate the appropriate terms and conditions of the bond.

For all of these reasons, the trial court correctly applied West Virginia law in determining that the surety bond issued by Hartford pursuant to W.Va. Code 31-17-4(f)(3) was a judgment bond.

Response to Assignment of Error No. 2:

The trial court was right in concluding that the plaintiffs had satisfied the condition of the bond by obtaining a default judgment against the mortgage broker and, therefore, that the plaintiffs were entitled to judgment against the defendant, Hartford

Hartford begins this assignment of error by repackaging its earlier argument that the trial court's ruling conflicts with W.Va. Code 45-1-3.

To begin with, Hartford says that public policy favors notice and an opportunity to be heard. The trial court's ruling would "nullify" this policy and West Virginia's "general statutory scheme of surety bonds." PETITIONER'S BRIEF, AT 25. In fact, Hartford argues that the trial court's ruling "is directly at odds with a statute that has existed 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." ID., AT 26.

As noted already, Hartford's entire argument rests on a false premise. W.Va. Code 45-1-3 does not provide sureties with procedural rights which can only be overcome by proving a knowing and intelligent waiver. *Myers* makes this perfectly clear. In the case of performance bonds, the protections codified in W.Va. Code 45-1-3 are available to sureties. In the case of judgment bonds, they are not. If there is any public policy that the court should seek to enforce here, it is simply the public policy

that contracts freely made by competent parties are “sacred” and should be fully enforced. See, e.g., *Wellington Power Co. vs. CNA Surety Corp.*, 217 W.Va. 33, 38, 614 S.E.2d 680 (2005)(recognizing a strong public policy in this state requiring “that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts, when entered into freely and voluntarily, shall be held sacred, and shall be enforced by courts of justice”). *Myers* tells us that, where judgment bonds are concerned, the judgment is “the very thing which [the surety] has agreed to pay.” Accordingly, the trial court’s order granting summary judgment and requiring the defendant, Hartford, to pay the judgment rendered against Equity was in all respects proper.

It should be noted at this point that Hartford’s worries of “fraud, collusion and prejudice against sureties” are simply unfounded. Even though sureties who write judgment bonds do not have the right to be served, appear and defend, as provided for under W.Va. Code 45-1-3, *Myers* nevertheless provides that a judgment is only conclusive against the surety “in the absence of fraud or collusion.” 74 W.Va. 488, 82 S.E.2d at 272. Therefore, even in a case arising out of a judgment bond, the surety is still free to challenge the underlying judgment as being the product of fraud or collusion. Here, of course, there are no facts supporting fraud or collusion and, indeed, Hartford has never made such an allegation.

Hartford also attacks the plaintiffs’ argument that they should not be forced to litigate their claims twice. “In truth,” says Hartford, “the [plaintiffs] have not tried their case even once.” PETITIONER’S BRIEF AT 26. This is not at all true. The plaintiffs

sued multiple parties in the underlying case, including the lender, the servicer, and the holder of the note. The case was litigated against the remaining parties, all of whom were served, appeared and eventually settled with the plaintiffs. Moreover, even though the claims against the broker, Equity, were not tried on the merits, there were nevertheless default judgment proceedings. Therefore, the plaintiffs engaged in substantial litigation before seeking recovery from Hartford.

Hartford next raises the specter of plaintiffs and attorneys who intentionally “target” defunct mortgage companies, obtain default judgments, and then seek to recover those judgments under the applicable mortgage lender bonds. PETITIONER’S BRIEF, AT 27. Of course, this is not a legal argument, but simply a scare tactic intended to bully the court into ruling in Hartford’s favor. It has no factual basis whatsoever.⁷ It is also offensive that Hartford would attack the integrity of the West Virginia bar by suggesting that lawyers would engage in unethical conduct in pursuing their claims.

In the next part of its brief, Hartford argues that it should not be bound by the judgment against Equity because it was a default judgment.

Hartford cites only a handful of authorities including *State vs. Abbott*, 63 W.Va. 189, 61 S.E. 369 (1907) and the Restatement (Third) of Suretyship. In the end, Hartford acknowledges that these authorities apply to bonds which are “conditioned for

⁷ In fact, Hartford refused to disclose how many mortgage lender and/or broker bonds it has issued or the premiums it has earned. Therefore, it is impossible to say exactly how many bonds Hartford issued to fly-by-night mortgage lenders or brokers and how many premium dollars it earned by doing so.

performance of a duty"--i.e., performance bonds. PETITIONER'S BRIEF, AT 28. But here, as the trial court found, we are dealing with a judgment bond.

Where a judgment bond is involved, a default judgment is just as binding upon a surety as a judgment arising from an adjudication on the merits. *Axess Intern., Ltd. v. Intercargo Ins. Co.* 183 F.3d 935 (9th Cir. 1999); *Southern Ins. Co. v. ADESA Austin*, 239 S.W.3d 423, 427 (Tex. App. 2007) ("When a surety has contracted to be bound by a particular judgment that may be rendered against the principal, the judgment is conclusive against the surety even if the surety was not a party to the suit where the judgment was obtained. Also, a surety on a judgment bond is bound by a default judgment against the principal even if the surety did not have notice of the prior suit against the principal. A default judgment against the principal is conclusive of the surety's liability, unless there is evidence of fraud, collusion, or that the default judgment altered the terms of the bond.") (internal citations omitted); *Old Republic Sur. Co. vs. Bonham State Bank*, 172 S.W.3d 210, 214 (Tex. App. 2005)("[I]f the bond is a judgment bond, . . . a surety is bound by the default judgment against the principal even if the surety did not have notice of the prior suit against the principal absent proof of collusion or fraud."); *First Mobile Home Corp. v. Little*, 298 So.2d 676, 682-83 (Miss. 1974) ("[A] default judgment against a principal is conclusive against his surety, unless it is shown that the default judgment was obtained through consent of the debtor, or collusion so as to be a fraud upon the rights of the surety."). Thus, the fact that the underlying judgment arose from the default of Equity has no impact on Hartford's obligations under the bond it issued.

Hartford's complaint that it was deprived of notice and an opportunity to be heard is adequately answered by *Myers* and, of course, by the language of the bond itself, which does not require that any notice be given to Hartford. The reality is that Hartford agreed to answer for any judgment entered against Equity. Therefore, by paying the proceeds of its bond Hartford is, in fact, doing nothing more than it contractually agreed to do. Hartford (and, for that matter, any other surety writing mortgage broker bonds) is free to raise any issues of fraud or collusion which might be warranted by the facts. Nevertheless, the fact that the underlying judgment was entered by default has no effect whatsoever on Hartford's bonding obligation. Accordingly, the trial court did not err when it entered judgment against Hartford on the basis of the underlying default judgment.

Response to Assignment of Error No. 3:

The trial court properly refused to grant a setoff for a settlement reached over a year after the default judgment was entered, particularly in light of the fact that no determination was ever made of the total amount of damages necessary to fully compensate the plaintiffs.

In its final assignment of error, Hartford claims that it is entitled to a set off for a settlement reached by the plaintiffs with the lender and the note holder. This settlement was consummated in August, 2010--over a year after the default judgment was entered against the defendant, Equity.

According to Hartford, the plaintiffs "are entitled to only one satisfaction for their alleged injury." PETITIONER'S BRIEF, AT 32. Because the plaintiffs have "fully

recovered” their damages, ID., AT 30, Equity (and, of course, Hartford as its surety) must receive a setoff for this settlement. Otherwise, says Hartford, the plaintiffs will receive an unfair “windfall.” ID., AT 38.

Hartford’s argument is flawed at multiple points.

First, the plaintiffs most assuredly did not “fully recover” their damages through the default judgment they obtained against the defendant, Equity. In fact, the default judgment represented *only a portion of the plaintiff’s liquidated damages*.⁸ The remaining liquidated damages, together with unliquidated damages for annoyance, aggravation, inconvenience, damage to credit, etc., were not included as part of the default judgment and, therefore, remain uncompensated.

Second, for this reason the default judgment cannot serve as a basis for a setoff. The setoff rule works hand-in-glove with the “one satisfaction” rule. An injured plaintiff is entitled to recover “no more than full compensation for his loss.” *Burgess vs. Porterfield*, 196 W.Va. 178, 183, 469 S.E.2d 114 (1996). Therefore, where a determination has been made of the amount of damages necessary to fully compensate the plaintiff, any settlements received should be set off against that amount. Because there has never been a determination of the total amount of damages due to the plaintiffs here, setoff is inappropriate.

Third, setoff is only available for settlements previously received in the past—not for future settlements. The trial court rightly concluded that “a setoff may only be performed after a verdict is returned and before a judgment is entered.” App327 .

⁸Specifically, the figure of \$56,300 represented the principal amount of the plaintiffs’ note and certain statutory penalties. App286-87.

Thus, only settlement amounts received before judgment was entered against Equity may be considered for setoff purposes.

These same principles are restated in *Board of Education of McDowell County vs. Zando, Martin & Milstead, Inc.*, 182 W.Va. 597, 390 S.E.2d 796 (1990). Hartford cites *Zando* and acknowledges that it is controlling. PETITIONER'S BRIEF, AT 32. Nevertheless, Hartford overlooks *Zando's* the key points.

We begin with an overview of the facts. The plaintiff was a school board that contracted with the defendant, Zando, to design and oversee construction of a new school building. The building was completed, but soon began developing cracks that led to a structural failure. The plaintiffs sued Zando who, in turn, filed a third party complaint against two of the contractors. Eventually, settlements were reached with the contractors. The case then proceeded to trial against the defendant, Zando, alone. The jury awarded \$1,000,000 in compensatory damages. Through its posttrial motions, Zando asked to have the jury's verdict reduced by the settlement amounts received by the plaintiff.

Justice Miller, writing for a unanimous court, began by "confirm[ing] our traditional practice of granting a nonsettling defendant a pro tanto, or dollar-for-dollar credit for partial settlements *against any verdict ultimately rendered for the plaintiff.*" 182 W.Va. at 606, 390 S.E.2d at 805 (emphasis added). He then summarized the law in syllabus point 7:

Defendants in a civil action *against whom a verdict is rendered* are entitled to have the verdict reduced by the amount of any good faith settlements *previously made with*

the plaintiff by to her jointly liable parties. Those defendants against whom the verdict is rendered are jointly and severally liable to the plaintiff for payment of the remainder of the verdict. Where the relative fault of the nonsettling defendants has been determined, they may seek contribution among themselves after judgment if forced to pay more than their allocated share of the verdict. (Emphasis added).

Zando, then, makes it clear that the predicate for obtaining setoff is *a prior determination by the factfinder of the full amount of damages due*. Then, and only then, is a setoff proper. If, for example, the jury tells us that the plaintiff's total damages are \$1,000,000, then any settlements reached beforehand should be set off to prevent any windfall to the plaintiff. Conversely, if there is no verdict then no right to a setoff exists. In fact, attempting a setoff in the absence of a jury verdict would give the defendant an unfair and undeserved reduction in his proportionate share of the damages, and, at the same time, would leave the plaintiff undercompensated for his injuries.

Frankly, the situation here is no different from a case where all of the defendants settle separately before trial. Is D2 entitled to a set off for the amount of D1's settlement? Of course not. Why? Because there has been no determination of the plaintiff's total damages. Without knowing the full amount of damages the plaintiff is entitled to recover, there is no reason for performing a setoff and no legal basis for doing so.

Zando also confirms that the right to a setoff applies only to *prior* settlements. In fact, *Zando* contemplates a simple, three-step process. First, the fact finder

determines the total amount of damages. Second, the court makes a reduction for any prior settlements. Third, the court proceeds to enter judgment for the reduced amount. There is simply *no law* authorizing a court to amend an existing judgment to account for settlements received after the fact.

Hartford cites a handful of older cases in an effort to convince the court that a setoff would somehow be appropriate here. But these cases simply do not support Hartford's argument.

To begin with, Hartford cites *Chewning vs. Tomlinson*, 105 W.Va. 76, 141 S.E. 532 (1928). *Chewning* is a factually complex case involving a judgment entered by a justice of the peace, an appeal by only one of the two defendants, and a new judgment entered by the circuit court. Even a cursory reading of *Chewning* reveals that it has nothing to do with the issue presented. For that matter, *Chewning* is not an offset case at all. It is, instead, a satisfaction of judgment case. Hartford selectively quotes from *Chewning*, but the fact remains that *Chewning* says nothing altering our well-settled law in *Zando*.⁹

Hartford also cites *Hardin vs. New York Central RR Co.*, 145 W.Va. 676, 116 S.E.2d 697 (1960). However, *Hardin*, like *Zando*, was a case tried to verdict. *Hardin* confirms what *Zando* itself says: that nonsettling defendants are entitled to a post

⁹The ruling in *Chewning* has been explained as follows: "Whether one of several joint tortfeasors has obtained in [the Supreme Court] a writ of error to a joint judgment rendered in a trial court, resulting in a diminished judgment against the plaintiff in error, the payment of the judgment has diminished on the writ of error is an election on the part of the judgment creditor, and operates as a satisfaction of the judgment in the trial court." *State ex rel. Bumgarner vs. Sims*, 139 W.Va. 92, 79 S.E.2d 277, 292 (1953).

It is also worth mentioning that both of the judgments in *Chewning* were the result of a trial on the merits and, therefore, represented a finding of the total amount of damages due and owing. Even if the court would find *Chewning* to be applicable in the context of setoffs, it is nevertheless consistent with *Zando*.

verdict offset for any settlements. The issue in *Hardin* was how the court should handle the offset as a matter of procedure--by presenting evidence of the settlement for the jury to consider, or by addressing the issue post verdict. *Hardin*, then, is in full agreement with *Zando*.

Finally, Hartford cites *Tennant vs. Craig*, 156 W.Va. 632, 195 S.E.2d 727 (1973). Hartford argues that *Tennant* is broader than *Zando*, but again there is nothing even remotely suggesting that a setoff can be performed without a determination of the total damages suffered by the plaintiff. In fact, the very language quoted by Hartford in its brief makes this clear: "The burden, however, will be on the plaintiffs to prove...that [they] are entitled to damages in excess of the amounts paid as a result of the compromise and settlement." 156 W.Va. at 639, 195 S.E.2d at 732. Thus, *Tennant* clearly recognizes that a determination of damages must precede any right to a set off.

CONCLUSION

The trial court was right in concluding, under *Myers*, that the mortgage broker bond issued by Hartford was a judgment bond. Accordingly, the procedural protections of W.Va. Code 45-1-3 were not triggered. The condition of the bond was fully satisfied when judgment was entered against the principal, Equity. Hartford was contractually obligated to answer for that judgment. This construction of the bond is consistent with *Myers*, with the language of the bond itself, and with the Legislature's intent to provide victims of predatory lending a speedy, full and adequate remedy in the event a broker was unable to pay a judgment rendered against it. Finally, under settled law, Hartford

is not entitled to any setoff for the settlement reached by the plaintiffs with any of the remaining defendants.

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CERTIFICATE OF SERVICE

Service of the foregoing **RESPONDENTS' BRIEF** was had upon said defendant by forwarding a true and correct copy thereof by United States Mail, postage prepaid, to its counsel of record, Archibald Wallace III, at his last known address 7100 Forest Avenue, Suite 302, Richmond, VA 23226, this 5th day of September, 2012.

A handwritten signature in black ink, appearing to be 'AW III', written over a horizontal line.

Counsel for Plaintiffs