DOCTRINE OF MERGER MAY IMPEDE A LENDER'S RIGHT TO COLLECT POST JUDGMENT COLLECTION EXPENSES

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On January 19, 2006, the Third Circuit highlighted the New Jersey Merger Doctrine holding that a lender's rights to post-judgment attorneys' fees and expenses as provided for in "loan documents" are extinguished upon their merger into the final judgment of foreclosure. The Court also noted a potential exception to this rule, finding that when language does clearly evidence intent to preserve the effectiveness of the attorneys' fees and expenses provision in the mortgage, the provision survives post-judgment.

In A&P Diversified, the borrower defaulted on a loan from Fleet Bank, which consequently instituted foreclosure proceedings. The borrower petitioned for Chapter 11 bankruptcy, but the Court issued an automatic bankruptcy stay to complete the foreclosure. Fleet's foreclosure judgment included $7,500 in counsel fees as permitted by the New Jersey Court Rules. Subsequently, the trustee for the borrower filed a motion in Bankruptcy Court where Fleet cross-moved for attorneys' fees pursuant to section 506(b). The Court denied the trustee's motion and awarded Fleet over $330,000 in attorneys' fees and expenses. The District Court affirmed this Order and the trustee appealed to the Third Circuit.

At question were the loan documents issued by the lender which include a provision stating that the borrower would pay reasonable fees, costs, and expenses of the lender's attorneys incurred in the collection of the debt or enforcement of the loan agreement. The Court stated that upon final judgment, the mortgage agreement and all of its terms, including the covenant requiring the borrower to pay legal fees, merges into the final judgment under the merger doctrine.

The Third Circuit held that the lender's rights under the contract were extinguished when the contract merged with the judgment. The Court recognized the exception to this rule if the mortgage clearly evidences intent to preserve the effectiveness of a mortgage provision post-judgment.

In this case, the Court found that Fleet Bank, the lender, did not clearly evidence the requisite intent and, therefore, limited the lender's recover of attorney's fees and costs to the amount authorized by Fleet's foreclosure judgment pursuant to the New Jersey Court Rules.

In light of the foregoing, Lenders should review their loan documentation to determine whether there is adequate language therein evidencing the intent to preserve the right to collect post-judgment fees and expenses.

Please contact us should you require any additional information or assistant in reviewing your loan documentation