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JUDGE: M. A. Mahoney

PARTIES: Catherine D. Slick, Norwest Mortgage, Inc.

CHAPTER: 13

ATTORNEYS: S. Olen, S. L. Nicholas, D. J. Stewart, H. A. Callaway, III, W. C. Bitzer

DATE: 5/10/02

KEY WORDS:

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UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF ALABAMA

In Re

CATHERINE D. SLICK,  
Debtor.

Case No. 98-14378-MAM

CATHERINE D. SLICK,  
Plaintiff,

v.

Adv. No. 99-1136

NORWEST MORTGAGE, INC.,  
Defendant.

**ORDER AWARDING JUDGMENT TO PLAINTIFFS**

Steve Olen and Steven L. Nicholas, Mobile, AL, Attorneys for the Plaintiff Class  
Donald J. Stewart, Mobile, AL, Attorney for Plaintiff Class  
Henry A. Callaway, III and Windy C. Bitzer, Mobile, AL, Attorneys for the Defendants

This matter is before the Court on (1) defendant's motion for a judgment on partial findings pursuant to Fed. R. Bankr. P. 7054; (2) defendant's motion for a verdict at the close of the evidence; and (3) trial of the case. The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the Order of Reference of the District Court. This is a core proceeding pursuant to 28 U.S.C. § 157(b) and the Court has the authority to enter a final order.

**FACTS**

A.

Catherine Slick filed a chapter 13 bankruptcy case on December 3, 1998. She had a mortgage loan secured by her homestead. The mortgagee was Norwest Mortgage, Inc. Norwest was given notice of Ms. Slick's bankruptcy filing and it filed a proof of claim on December 18, 1998.

The proof of claim did not include any disclosure of any attorneys fee being paid to anyone to file the proof of claim. In fact, Barrett Burke Wilson Castle Daffin & Frappier LLP (“Barrett Burke”), a Texas law firm, prepared and filed the proof of claim. Barrett Burke charged Norwest \$125 for preparation of the proof of claim. Norwest paid Barrett Burke and then assessed or posted the fee to Slick’s account by adding the fee to the loan balance due Norwest from Slick.

Norwest filed an amended claim in November 1999. The proof of claim preparation fee was not disclosed on this claim form either. Norwest never sought court approval for the fee at any time.

#### B.

Norwest had followed several different procedures throughout the years for handling bankruptcy proofs of claim. Before 1994, Norwest prepared and filed all proofs of claim through use of its own nonlawyer personnel. Norwest charged no fee to debtors for this work.

In 1994 or 1995, Norwest hired Creditor’s Bankruptcy Service (“CBS”) to prepare and file its proofs of claim. This “outsourcing” of the claims preparation process freed Norwest from the expense of maintaining staff of its own to file the claims. Norwest then added the cost of the claim preparation to each debtor’s account. A CBS nonlawyer employee did the work in Norwest’s Charlotte, NC office. CBS put the proof of claim preparation fee on the proof of claim form, designating it as a “proof of claim filing fee.” CBS charged \$75 for each claim filed.

In 1996, Barrett Burke succeeded CBS as the outside firm filing proofs of claim for Norwest. In the beginning (until July 1997), Barrett Burke prepared the claims, but Norwest employees signed them. Norwest also was listed as the party filing the claims on the stationery used to mail claims to courts. Barrett Burke’s fee was posted to each debtor’s account when

paid. Continuing the CBS procedure, the proof of claim filing fee was disclosed on the form. In July 1997, Barrett Burke's nonattorney employees started signing the claims and did so until June 1998 when Barrett Burke hired an attorney, Debra Clark, to take over the review and signing of all proofs of claim. Barrett Burke initially charged \$100 per claim. That fee rose to \$125.

The same procedures were followed in the Des Moines, Iowa and Maryland service centers with different law firms doing the work. The only difference was that the Iowa and Maryland service centers never had an attorney working on claims. Only nonlawyer employees of the outside firms prepared the claims. However, just as in the Charlotte service center, in the Des Moines and Maryland service centers, the fee was also disclosed on the claim form and the fee charged by the outside firm was added to each debtor's account.

By April 1998, Norwest had consolidated its claims filing procedures and Barrett Burke was doing all of Norwest's claim filing. The Maryland and Iowa service centers had phased out their bankruptcy departments and the work was consolidated in Charlotte.

### C.

As stated above, the proof of claim preparation fee was disclosed on the proof of claim form commencing in 1994 when the fee was first incurred due to Norwest's outsourcing. However, in September 1997, Norwest informed Barrett Burke to discontinue disclosing the fee due to "pending litigation, industry litigation and opinions of in-house counsel." (Deposition of Jill Helmers, pp. 42-43.) The change in policy occurred because of the allegations in a class action suit commenced against Norwest Mortgage. *See Majchrowski v. Norwest Mortgage*, 6 F. Supp. 2d 946 (N.D. Ill. 1998). The suit alleged that Norwest included improper inspection

and attorneys fees in its proofs of claim and asserted that these charges violated the RICO Act, committed unfair and deceptive practices and breached the Norwest mortgage agreements.

The nondisclosure of the claim preparation fees did not mean that they were no longer charged. The fees were still posted to debtors' accounts. However, no debtor knew the fee was being assessed against him or her—at least not from any filings with the bankruptcy court. The fee was not even added to the loan balance shown in the proofs of claim filed.

D.

Since 1994, Barrett Burke's fee has always been a flat rate fee for each claim prepared and filed of either \$75, \$100, or \$125. (It was unclear to the Court what the fee was in the beginning and when it rose.) In 1999, Barrett Burke filed 7,811 claims for Norwest and was paid \$976,375. The Barrett Burke attorney who worked at Norwest's Charlotte office reviewed and signed each claim after nonattorney employees of Barrett Burke prepared the claims. If she worked fifty 40-hour weeks, she spent about 15 minutes on each claim. She testified that she spent 25-40 minutes on each claim—2 to almost 3 times the 15-minute average. Her supervising attorney testified that she believed Barrett Burke's on-site attorney spent one to one-and one-half hours on each proof of claim.

E.

Recently Norwest began to send all of its Fannie Mae and VA loans to two law firms other than the Barrett Burke firm. Fannie Mae and VA loans are about 25% of Norwest's portfolio. The firms are approved by Fannie Mae as required by Fannie Mae procedures. The firms charge up to \$800 for services in each bankruptcy case. The firms break their fees into two parts. They charge \$450 for work within 90 days after the bankruptcy filing, which work includes filing a proof of claim. A large portion of the time expended is spent on loss mitigation

efforts.<sup>1</sup> After confirmation (about 90 days after filing of a case), if work is done, a second bill is sent. No fees are shown on any proof claim filed by a Fannie Mae approved firm. They do not break out how much time is devoted to performing any particular task including preparation and filing of a proof of claim. The firms also do not differentiate between pre- and postconfirmation work.

F.

Barrett Burke sold its claims processing business to First American on approximately January 2, 2001. First American is not a law firm. First American operated exactly like Barrett Burke did. In fact, the Barrett Burke attorney who handled proofs of claim at the Norwest offices continued to do so (probably as a First American employee) until July 1, 2001 or so when First American's services were terminated.

G.

Norwest Mortgage merged with Wells Fargo in 1998. Its bankruptcy department is still located in the Charlotte, NC service center.

As of July 1, 2001, the proof of claim fee policy came full circle. After July 1, 2001, no fee was assessed to borrowers who filed bankruptcy for the filing of a proof of claim except Fannie Mae and VA loans. Norwest handles all non-Fannie Mae loans in-house. First American's services have been terminated.

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<sup>1</sup>A recent Wall Street Journal article described the loss mitigation program. "Pinched Homeowners are Finding Shelter in Modified Loans," Wall Street Journal, October 30, 2001, at A.1.

H.

From 1994 to July 2001 (and continuing for Fannie Mae and VA loans), the proof of claim filing fee was posted to a debtor's account and was collected from the debtor if the loan was paid in full.<sup>2</sup> This payment may have occurred through a bankruptcy case, through loan maturity and payment, through a redemption after foreclosure, or through a refinancing of the debt. If a foreclosure occurred, the fee was never collected from the debtor unless the debtor redeemed the property.

I.

The evidence shows that proofs of claim were filed by Norwest in 23,771 bankruptcy cases with no fee disclosure from September 1, 1997 through June 30, 2001. Other than those loans in which a foreclosure has occurred since the bankruptcy filing of a debtor, the proof of claim filing fee remains posted to the account or the fee has been paid as part of a redemption, refinance or other payment of the loan in full.

LAW

The plaintiffs have the burden of proving their case by a preponderance of the evidence. That burden has been met. The Court carefully considered the defendant's motion for a judgment on partial findings pursuant to Fed. R. Bankr. P. 7054 and the defendant's motion for a verdict at the close of the evidence. The plaintiffs met their burden at each stage of the trial and these motions are denied.

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<sup>2</sup>In the Fannie Mae and VA loan cases, the claim preparation charge is a part of the first \$450 billed to Norwest (Wells Fargo).

The Court has already entered numerous orders in this case and several similar cases. The Court, when appropriate, will refer to those rulings by reference rather than repeat them. All prior rulings in this case are incorporated by reference.

The remaining sections of the opinion will be broken into ten parts and the Court will discuss each issue in turn.

- A. Jurisdiction
- B. Class Certification
- C. Fee Disclosure in Chapter 13 Cases
- D. Cases in Which Fees were Disclosed
- E. Statute of Limitations
- F. Converted and Dismissed Cases
- G. Damages
- H. Sanctions
- I. Prejudgment Interest
- J. Attorneys Fees

A.

#### Jurisdiction

This Court issued a ruling on its jurisdiction to hear this type of case. *In re Noletto*, 244 B.R. 845 (Bankr. S.D. Ala. 2000). The Court incorporates that ruling by reference. The U.S. District Court for the Northern District of Alabama has recently issued a thoughtful opinion concluding that its bankruptcy court also has jurisdiction to consider a class action suit. *Bank United v. Manley (In re Manley)*, Case No. CV-00-N-2141-W, opinion dated November 29, 2001. This Court adopts its reasoning as well. This Court concludes that there is clearly no obstacle to this Court ruling on issues involving debtors in this district. The defendant does not dispute this exercise. It is debtors' cases beyond this district as to which a question has been raised. As to those cases, the District Court certainly has jurisdiction if this Court does not. If

this Court is held to be without jurisdiction over this case, the Court reports and recommends to the District Court that it adopt these findings and conclusions pursuant to Fed. R. Bankr. P. 9033.

The problem at issue in this case and several others pending in this Court and other courts needs to be addressed. Creditors should not be able to assess fees to the account of a person in bankruptcy without the person's knowledge. A bankruptcy case's purpose is to allow a debtor to get out of financial trouble. At discharge, a debtor ought to be able to expect he or she has brought his or her secured debts current and wiped out all unsecured debts not paid through a plan. Undisclosed fees prevent a debtor from paying the fees in his or her plan—an option that should not be lost simply because a creditor chooses to not list the fee and expects to collect it later. Also, secured creditors should not be able to add unapproved attorneys fees to a debtor's account during a bankruptcy when no other creditor can receive fees without approval.

B.

#### Class Certification

This Court has issued an opinion certifying a class in this case and a separate order defining the class. *In re Slick*, Order Granting Plaintiff's Motion to Alter, Amend or Vacate Summary Judgment Order and Denying Defendant's Motion to Alter or Amend, March 6, 2001 (Bankr. S.D. Ala. 2001); *In re Slick*, Order Defining Class to be Certified in Case, June 5, 2001 (Bankr. S.D. Ala. 2001). These opinions are incorporated by reference.

C.

#### Fee Disclosure in Chapter 13 Cases

The crux of the controversy in this case is whether Norwest can charge attorneys fees to debtors' accounts at any time during a bankruptcy case without disclosure of those fees to

anyone. The Court has already addressed this issue in an opinion in this case. *Supra*, *Slick* order of March 6, 2001, at 5. The evidence at trial did not alter this Court's view of the issue.

Norwest, since 1994, has outsourced its bankruptcy proofs of claim filing function. The outside firm—whether a law firm or not—charges a fee for the service of preparing and filing the claim. (In the case of the Fannie Mae Designated Counsel Program, the fee is an unspecified amount of the first installment fee charged to Norwest.) The fee is posted to each debtor's account. Any failure to pay the fee is not grounds for default, but Norwest attempts to collect the fee when a loan is paid off or a redemption after foreclosure occurs. The fee is not collected if a foreclosure occurs with no redemption.

Since September 1997, the fee has not been disclosed at all during a debtor's bankruptcy case. It is simply posted to the debtor's account and the debtor finds out about the fee (if ever) after his or her bankruptcy case is discharged or the case is dismissed or relief from the stay is granted to the creditor.

This Court has written an opinion that deals with the issue of nondisclosure and inadequate disclosure of fees. *In re Noletto*, Order Granting Defendant's Summary Judgment Motion, dated December 29, 2000 (Bankr. S.D. Ala. 2000). That opinion is incorporated by reference.

The U.S. Supreme Court case of *Rake v. Wade*, 508 U. S. 464, 113 S. Ct. 2187, 124 L. Ed. 2d 424 (1993) and the Eleventh Circuit case of *Telfair v. First Union Mortgage Corp.*, 216 F.3d 1333 (11th Cir. 2000) *cert. denied*, 531 U.S. 1073 (2001), *reh'g denied*, 121 S. Ct. 765 (2001), speak to this issue. This ruling is consistent with their holdings.

*Rake v. Wade* held that a chapter 13 debtor who chose to cure a default on his or her oversecured home mortgage through a plan had to pay postpetition interest on the arrearage

claim. The plan in question provided that the arrearage including interest and attorneys fees would be paid through the plan. The Supreme Court held that debtors could pay postpetition interest through the plan and be in compliance with 11 U.S.C. §§ 506(b) and 1322(b)(5). The Court commented, without disagreeing, that COLLIER ON BANKRUPTCY and the parties to the suit agreed that § 506(b) is applicable only to the effective date of the plan. 3 COLLIER ON BANKRUPTCY ¶ 506.05, pp. 506-43 and n.5c (15th ed. 1993); *Rake* at 508 U.S. 468. Thus, § 506(b) interest and fees should only be added to a claim if preconfirmation.

The *Telfair* case, *Telfair v. First Union Mortgage Corp.*, 216 F.3d 1333 (11th Cir. 2000) *cert. denied*, 531 U.S. 1073 (2001), *reh'g denied*, 121 S. Ct. 765 (2001), building upon this ruling, held that payment of postconfirmation attorneys fees from the debtor's regular monthly mortgage payments paid postconfirmation did not violate § 506(b) or § 362 of the Bankruptcy Code.

[A]fter confirmation, only the amount required for the plan payments remained property of the estate. *Telfair*'s regular loan payments, made outside of the plan, were therefore no longer property of the estate and First Union's application of a portion of those payments to attorneys fees pursuant to the Deed [of Trust] did not violate section 362.

*Id.* at 1340; and

[T]he Supreme Court has stated that interest accrues under section 506(b) "as part of the allowed claim from the petition date until the confirmation or effective date of the plan." *Rake v. Wade*, 508 U. S. 464, 471, 113 S. Ct. 2187, 2191, 124 L. Ed. 2d 424 (1993) . . . . This Court . . . can find no basis to distinguish *Rake*'s statement that section 506(b) "applies only from the date of filing through the confirmation date," 508 U.S. at 468, 113 S. Ct. at 2190, on the ground that it dealt with interest rather than attorney's fees.

*Id.* at 1328-29. No other circuit court has disagreed with *Telfair*. Indeed, it would be hard to do so since it is based on the U.S. Supreme Court case of *Rake v. Wade*.

*Telfair* reasons that postconfirmation fees are *not* part of the creditor's secured claim in a chapter 13 bankruptcy case, but preconfirmation fees are. The treatment of all preconfirmation fees, therefore, must be consistent with this premise.

Since the fees are to be treated as part of Norwest's secured claim, two things must happen. The proof of claim fee must be *disclosed* so that the debtor knows the fee is part of the secured claim. Second, the fee should be included in the arrearage claim portion of the debt so that debtor can pay the fee through his or her plan as allowed by 11 U.S.C. § 1322(b)(5)..

Norwest makes several new arguments at trial as to the propriety of its undisclosed attorneys fee charges:

1. The fees are not treated as "defaults" and therefore need not be cured under 11 U.S.C. § 1322(b)(5).
2. A long-term mortgage debt survives the discharge of the debtor in a chapter 13 case. It is consistent with this premise that a debtor may remain liable for some debts which cannot be or are not included in a creditor's proof of claim.

The first argument relates to § 1322(b)(5) of the Bankruptcy Code that states a chapter 13 plan shall

provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.

If failure to pay the attorneys fee is not a "default," according to Norwest, the sum should not be added to any arrearage claim to be paid in a plan. Norwest points to how its mortgage documents treat the proof of claim fee. (Def. Exh. No. 16; ¶ 6(B) and 9(a)). Only failure to pay monthly mortgage payments is an event of default, not failure to pay fees or expenses.

This theory will not save Norwest for several reasons. First, § 506(b) clearly includes attorneys fees as part of a creditor's secured claim as made clear in *Rake v. Wade, supra*, and

*Telfair, supra*. If the fee is not listed, the debtor has no way to know it exists. If the debtor does not know it exists, it cannot be a part of the secured claim. Since it should be included as part of the secured claim, it cannot be collected after discharge. Second, Norwest cannot decide for the debtor what arrearage or costs the debtor may pay in his or her plan and what arrearages he may not pay in his plan by picking and choosing which § 506(b) costs to disclose. Section 1322(b)(5) is a provision of the Bankruptcy Code which gives the *debtor* options for plan formulation, not the creditor. If the debtor does not know all of his debts, he cannot exercise his options most effectively for himself. A creditor should not be able to dictate to a debtor what option he selects by its nondisclosure. Norwest failed to disclose a \$75-125 fee. What if it was more?<sup>3</sup> One thousand dollars? Two thousand dollars? The debtor must be able to sort through his choices. Also, only “reasonable” attorneys fees are to be added to the debt. If the fees are not disclosed, no reasonableness determination can be made. As this case shows, fees have been \$75, \$100, \$125 and a part of a \$450 fee.

Norwest’s second argument is that since the mortgage debt rides through the plan and discharge, it does not matter if the fee is added to the arrearage. A portion of the debt will remain anyway and letting this fee ride through is consistent with that. This argument is also incorrect. As *Rake v. Wade* and *Telfair* stated, § 506(b) states that a secured claim includes all prepetition debt and all postpetition interest, fees, costs and charges to the effective date of the plan. The § 506(b) charges can be paid through the plan. The debtor has a choice to make--to pay the debt in the plan or to allow it to be added to the debt and paid after the bankruptcy case is

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<sup>3</sup>In the Fannie Mae cases, it may have been more—up to \$450 for unspecified services.

concluded. If a creditor fails to disclose those charges, they cannot be added later. Norwest has no choice in the matter. If the fee is not disclosed, it is discharged.

D.

Cases in Which Fees were Disclosed

In 1994 or 1995, Norwest commenced outsourcing of the proof of claim filing function. Initially Creditor's Bankruptcy Service filed the claims. CBS disclosed a \$75 charge for a "proof of claim filing fee" on the proofs of claim filed. The plaintiffs are not asserting that any relief is due them when there has been a disclosure in this case. ("Based on the undisputed evidence in this case, Defendant Norwest Mortgage . . . intentionally implemented a practice of assessing and collecting proof of claim fees from bankruptcy debtors with no **disclosure of the fees.**" (emphasis in original) (Plaintiff's trial brief, p. 1)). Therefore, the Court assumes for purposes of this ruling, without making additional findings, that CBS's disclosure was adequate. Since the disclosure was adequate, the debtors had an opportunity to challenge the fee in each of their cases. Therefore, debtors with CBS claims are not members of the class of debtors included in this case. This is also true of any debtors in whose chapter 13 cases the Barrett Burke fee or Fannie Mae/VA fees were disclosed.

E.

Statute of Limitations

On June 5, 2001, this Court certified a class that included all bankruptcy debtors who filed a chapter 13 petition on or after January 1, 1994, in which certain proofs of claim were filed. The Court indicated in the certification order that it would deal with what the appropriate limitations period was after trial of the case.

Norwest asserts that the debtors included in this class should be those who filed cases from and after July 9, 1997 or later because that date is two years prior to the filing of this class action suit. The Alabama statute applicable to this case sets a two-year limit. ALA. CODE § 6-2-38(j) and (e) (1975). Due process suits are limited by a two-year statute as well. ALA. CODE § 6-2-38(l) (1975). The plaintiffs assert that statutes of limitations do not control when the issue is injunctive relief. *Holmberg v. Armbrecht*, 327 U.S. 392 (1946). Also, equitable tolling should apply since the fees were undisclosed. *In re Bookout Holsteins, Inc.*, 100 B.R. 427 (Bankr. N.D. Ind. 1989). Finally, there is no statute of limitations for a violation of the stay. *E.g., In re Wills*, 226 B.R. 369 (Bankr. E.D. Va. 1998); *In re Germansen Decorating, Inc.*, 149 B.R. 517 (Bankr. N.D. Ill. 1992).

The Court concludes that the class of debtors should include all debtors who filed chapter 13 cases on or after January 1, 1994 if Norwest charged but did not disclose a proof of claim filing fee in the case. The Court agrees with the plaintiffs' arguments. The fact that the fees in this case were completely undisclosed makes an equitable tolling argument especially appropriate. *Erie Ins. Co. v. Romano (In re Romano)*, 262 B.R. 429, 432 (Bankr. N.D. Ohio 2001) ("Equitable tolling will apply when a plaintiff, through no fault of its own and despite the exercise of due diligence, cannot determine information essential to bringing a complaint in a timely manner."). Because the primary relief to be granted is injunctive, and because of equitable tolling, the period of limitations is longer—from January 1, 1994 to date. The Court is not agreeing with plaintiffs' position that the stay has been violated and, therefore, the fact that there is no limitations period for stay violations is not adopted.

F.

Converted and Dismissed and Closed Cases

Norwest asserts that debtors whose cases have been converted or dismissed should be excluded from the class as finally constituted. Norwest argues that converted or dismissed debtors will not pay any arrearages from property of the estate; and, in converted cases, the attorneys fee claim becomes part of the prepetition claim. 11 U.S.C. § 348(d). First, an undisclosed fee in a discharged chapter 7 case, if posted or collected after filing of the case, violates the chapter 7 debtor's discharge. The posting and collection of the fee is an action to collect a preconfirmation claim treated in the plan. The violation remains, even if the case is closed. Such violations can be handled without reopening each underlying case. *Singleton v. Wells Fargo Bank, N.A. (In re Singleton)*, 269 B.R. 270 (Bankr. D.R.I. 2001). As to dismissed cases, no discharge is entered so there can be no violation of it. However, each debtor still has a cause of action to avoid the fee because it was improperly charged during the bankruptcy case. This cause of action is not extinguished by dismissal of the case because § 349 of the Bankruptcy Code specifically addresses what occurs at dismissal and extinguishment of bankruptcy causes of action is not included. The case of *Menk v. Lapaglia (In re Menk)*, 241 B.R. 896, 906 (B.A.P. 9th Cir. 1999) specifically catalogues numerous actions that are not extinguished. Among these are issues of compensation. *Id.* at 906. That is precisely the issue in this case. What is the proper compensation to be allowed to Norwest, if any, for preparation of the bankruptcy proof of claim? This is an issue of bankruptcy law. It should not be dealt with in state court when a class of similar debtors is constituted in federal court. The issue is still a part of the bankruptcy case and federal court jurisdiction remains. The matter "arises under title 11." 28 U.S.C. § 1334(b). The question is the validity and reasonability of the fee under § 506(b), a

purely federal law question. Therefore, debtors in dismissed cases are included. There is also no need for these cases to be reopened. *Id.* at 906-07.

G.

#### Damages

The damages suffered by the plaintiffs are of two kinds. First, all of the debtors had a proof of claim filing fee posted to their accounts. Second, some of the debtors have actually paid the fee.<sup>4</sup> Those debtors that have had the fee posted to their accounts must have the fee expunged from their account records. Those who have paid the fee must have it returned.

Even if the bankruptcy case of a debtor has been dismissed or converted or relief from stay granted, the fee cannot remain on the account or be added after the bankruptcy is over. The fee was a bankruptcy attorneys fee. It should have been charged and disclosed during the bankruptcy case and the debtor given a right to contest the fee in bankruptcy court. Therefore none of the fees are collectible from a debtor. As *Telfair* stated, preconfirmation fees are part of the secured claim in the bankruptcy case and, therefore, this Court concludes that they are discharged if they are not claimed or adequately disclosed in the bankruptcy case.

The Court does not even need to reach the issue of the propriety or reasonability of a particular fee or type of fee. When an attorneys fee for filing a proof of claim is completely undisclosed, it simply cannot be charged.

As to the fees of Fannie Mae/VA counsel that are not broken down as to pre- and post confirmation charges, all charges must be presumed to be preconfirmation in the first billing because the Court was given no evidence (or very little) to the contrary. The evidence indicated

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<sup>4</sup>The exact number that have paid the fee is unknown at present.

that the first billing was made at about the time of confirmation. Therefore, when the Court speaks of how to treat fees in its order for judgment, the entire first bill of \$450 that was posted to debtors' accounts must be expunged and must be refunded, if paid by the debtor.

H.

#### Sanctions

Plaintiffs seek sanctions or exemplary damages for the actions of Norwest under § 105 of the Bankruptcy Code. Section 105 authorizes a court to

issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

Such damages are awarded when there has been an abuse of the bankruptcy process. *Karsch v. LaBarge (In re Clark)*, 223 F.3d 859 (8th Cir. 2000). Cases have awarded damages under § 105 for attorney misconduct. *In re Rimsat, Ltd.*, 212 F.3d 1039 (7th Cir. 2000). The case of *In re Tate*, 253 B.R. 653 (Bankr. W.D.N.C. 2000) used § 105 to award damages for money collected on improperly filed claims. Cases involving issues related to § 362 stay violations, such as *Jove Engineering, Inc. v. Internal Revenue Service (In re Jove Engineering, Inc.)*, 92 F.3d 1539 (11th Cir. 1996), and violations of § 524, the discharge injunction, such as *Bessette v. Avco Financial Services, Inc.*, 230 F.3d 439 (1st Cir. 2000), have invoked § 105 to award actual damages, attorneys fees, and punitive damages too.

As stated above, actual damages in the form of an injunction and the ancillary relief of repayment of any proof of claim filing fees collected are appropriate under § 105 in this case. Attorneys fees are also warranted.

The more difficult issue is whether punitive or exemplary damages should be assessed. Courts award exemplary damages if a creditor has willfully abused the bankruptcy process or court orders. *E.g., In re Lafferty*, 229 B.R. 707 (Bankr. N.D. Ohio 1998). There are factors to consider that weigh both ways.

Prior to September 1997, Norwest disclosed the proof of claim filing fees it charged to debtors on the debtors' proofs of claim. Only after a federal court suit raised a question about inspection and attorneys fees was that policy changed. Norwest's evidence was that it was trying to follow what its legal advisers thought was correct procedure in bankruptcy cases. There has been no evidence of any malicious intent; however, the decision not to disclose fees was certainly intentional or "willful."

The reason Norwest had this problem was its attempt to raise its own profits and avoid lawsuits. Norwest, to lower its costs, outsourced an activity it previously did in-house without attorneys. From 1994 to 2001, it paid nonattorney entities or attorneys to file the proofs of claim and put that cost on its borrowers. The decision was a business and bottom line driven decision. Norwest created this issue by its major policy shift—to outsource certain actions and lay that cost on borrowers. It benefitted financially from that action. Once a decision was made to charge debtors for a previously "free" service, Norwest knew it had two choices—to disclose that a fee was being charged or to not disclose it. At first it made a disclosure. Then, when it encountered a court challenge to the fees it charged, it changed its policy. It chose not to disclose the fees it charged anymore. Nondisclosure or "hiding" a fee always carries some risk, particularly when the "target" of the nondisclosure is unsophisticated.

The Court concludes that the nondisclosure should be sanctioned. Norwest gave debtors no notice at all of a fee added to their accounts. Over \$2,000,000 in fees have been assessed to

unknowing debtors.<sup>5</sup> Courts are concerned about fees, as the numerous decisions about fees at all court levels attest. *E.g.*, cases cited at BANKRUPTCY SERVICE, LAWYERS EDITION, § 16:636 Sua Sponte Power of the Court (Gavin L. Phillips & Michael J. Yaworsky, eds, West 2001). Treatises discuss judges' duties in regard to fees. *E.g.*, 2 CHAPTER 11 THEORY AND PRACTICE, § 12.01 at 12:3 (James F. Queenan, Jr., et al., eds. 1994) ("The bankruptcy judge has an independent duty to examine the property and reasonableness of fees, even if no party in interest objects."). Norwest decided to not disclose its fees in the face of this knowledge. The Court concludes that \$2,000,000 in punitive damages should be paid to the plaintiffs. This represents less than \$100 per debtor. This sum is large enough to send a message to Norwest and other lenders about the necessity of disclosing fees in bankruptcy cases.

The Court looked for cases upon which to base its award. There was only one similar case. In the *Conley v. Sears, Roebuck & Co.* case, 222 B.R. 181 (D. Mass. 1998), Sears agreed to pay 151% of 190,000 debtors' out of pocket losses or over \$165,000,000 and a finance charge waiver (18-21%) on all postpetition purchases. The actions of Sears were clear violations of the blackletter bankruptcy law. Sears' actions affected more debtors. Therefore, an exemplary award of approximately \$100 per debtor is appropriate in this case. This is considerably less than the 151% of charges and finance charge waiver paid in the *Sears* case.

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<sup>5</sup>This figure is arrived at by figuring that an average fee of \$100 was charged for the 23,771 claims filed.

I.

Prejudgment Interest

The plaintiffs have suggested several prejudgment interest rates that could be applied in this case. Plaintiffs conclude a rate of 6% is most appropriate since it is the rate used in Alabama, ALA. CODE § 8-8-2 (1975), and in Norwest's home state (before its merger with Wells Fargo), MINN. STAT. § 334.01. This Court has broad discretion in whether to award prejudgment interest. *In re Vic Bernacchi & Sons, Inc.*, 170 B.R. 647 (Bankr. N.D. Ind. 1994). The Court concludes prejudgment interest should be paid to every plaintiff who has paid some or all of the attorneys fee posted to his or her account. The debtor has been deprived of the use of that money since payment. Since this is a case based strictly on federal law and involves plaintiffs from every state, the most appropriate interest rate to use is 28 U.S.C. § 1961(a), the federal prejudgment interest statute.

J.

Attorneys Fees

The parties have agreed that attorneys fees will be determined at a later hearing.

CONCLUSION

Undisclosed proof of claim preparation attorneys fees cannot be posted to or collected from bankruptcy debtors. Such fees, if posted or collected, are improper under the Bankruptcy Code, particularly 11 U.S.C. § 506(b).

IT IS ORDERED:

1. The motions of Norwest Mortgage, Inc. for judgment on partial findings and for a judgment at the close of the evidence are DENIED.

2. Norwest Mortgage is enjoined from posting all undisclosed proof of claim preparation attorneys fees to the account of any mortgagors who filed chapter 13 bankruptcy cases from January 1, 1994 to the current date.

3. Norwest Mortgage shall expunge from the account of any mortgagor who filed chapter 13 on January 1, 1994 to date any undisclosed proof of claim preparation attorneys fee.

4. Norwest Mortgage is ordered to refund to the class all undisclosed proof of claim preparation attorneys fees collected from mortgagors who filed chapter 13 cases from January 1, 1994 to date together with prejudgment interest pursuant to 28 U.S.C. § 1961(a) for the period from the date of collection to the date of refund to the debtor.

5. The plaintiffs are awarded exemplary damages of \$2,000,000 for Norwest Mortgage's improper, undisclosed assessment of fees to debtors' accounts.

6. Norwest shall search its records for the names and last known addresses of all members of the class and provide that list to plaintiffs' counsel within ninety days of this order.

7. A hearing on attorneys fees to be awarded to plaintiffs' counsel shall be held on **October 22, 2002 at 1:00 p.m.** in Courtroom 2, U.S. Bankruptcy Court, 201 St. Louis Street, Mobile, AL 36602.

Dated: 5/10/02

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MARGARET A. MAHONEY  
CHIEF BANKRUPTCY JUDGE