[Hastings Business Law Journal](https://repository.uchastings.edu/hastings_business_law_journal)

Volume 8
Number 2 *Summer 2012*

Article 3

Summer 1-1-2012

MERS: The Unreported Effects of Lost Chain of Title on Real Property Owners

David E. Woolley

Lisa D. Herzog

MERS: The Unreported Effects of Lost Chain of Title on Real Property Owners

David E. Woolley and Lisa D. Herzog***

I. INTRODUCTION

Many problems with the Mortgage Electronic Registry System ("MERS") and the home loan securitization process have been reported in print media, in movies, on television and in academic journals. MERS now keeps electronic records on about half of the home mortgages in the United States.[1] Courts have ruled against MERS' standing to foreclose and have criticized the MERS model as being flawed, wholly inaccurate and not allowing homeowners to fight foreclosures because it shields the true owner of a mortgage in public records.[2] States Attorneys' General and

---

* David E. Woolley is the principal, owner and founder of both Harbinger Analytics Group and D. Woolley & Associates. Mr. Woolley is a California Licensed Land Surveyor and Certified Fraud Examiner with over twenty-four years of experience. At Harbinger Analytics, Mr. Woolley specializes in the investigation of commercial real property boundary disputes, land survey fraud, land title insurance fraud and their cumulative effects on mortgage loans. Mr. Woolley is also an experienced expert witness, testifying in California and federal courts in a variety of land title, boundary dispute, and other civil litigation matters.

At Harbinger Analytics, Mr. Woolley provides land title survey auditing and quality control programming, fraud investigation, and technical report production pertaining to land survey and land title fraud. Harbinger Analytics Group also provides litigation support services in the form of expert witness opinions regarding standard of care, professional negligence, negligent misrepresentation and breach of representations and warranties.

** Lisa D. Herzog is a California Licensed Attorney with over fourteen years of professional legal experience in the fields of business and real property litigation, employment litigation, discrimination litigation, and business transactions and agreements. Ms. Herzog is an adjunct professor for Pepperdine University Graziadio School of Business and Management in Malibu, California. She received a B.A. in Communcations and Psychology from Michigan State Unversity, a Masters in Labor and Industrial Relations from Michigan State University, and her J.D. from Pepperdine University School of Law.

Ms. Herzog also serves as a writer, researcher, and editor for Harbinger Analytics Group where she specializes in preparing papers for publication. She assists David Woolley in compiling client reports and findings.

1. Marian Wang, *Backgrounder: A Closer Look at MERS, the Industry's Controversial Mortgage Clearinghouse*, PROPUBLICA (March 7, 2011), http://www.propublica.org/blog/item/backgrounder-a-closer-look-at-mers-the-industrys-controversial-mortgage-cle.

2. See *In re Agard*, 444 B.R. 231 (Bankr. E.D.N.Y. 2011) (holding that MERS lacked the legal standing to transfer the ownership of mortgages on behalf of banks). In his opinion, Judge Robert E. Grossman stated "This court does not accept the argument that because MERS may be involved with

federal bank regulators[3] are investigating MERS practices including fraudulently robo-signing (by way of servicers) and backdating missing documents. A few County Registrars of Deeds are claiming that they are owed millions of dollars in lost revenue from mortgage assignment transfers that were not recorded because MERS was listed as the mortgagee in public land records.[4]

What none of these "experts," reporters, or courts are analyzing (in specific terms) is the destructive effect that the MERS system will have on 400 years of recorded property rights in the United States. Most articles mention the lost chain of title but stop short of explaining what this means, or how it will affect homeowners with or without mortgages in the MERS system. These problems deal with ramifications "on the ground" (literally) for determining (1) property boundaries (senior and junior property rights) and (2) proof of ownership in order to obtain title insurance and financing. Most individuals reasonably assume the limits of their title agree with those delineated by improvements (i.e., fences), however, this may not be true.

Because MERS is utilized for transferring title and these transfers are not publicly recorded (thereby imparting constructive notice), MERS does not comply with race (first in time) or (constructive or actual) notice[5] statutes and, therefore, senior/junior property rights cannot be determined when a discrepancy arises in property boundaries lines. Consider the following:

- What happens if the chain of title cannot be determined because there are no accurate and publicly recorded deeds/title documents showing chain of title to determine senior and junior rights designations for boundary determinations between neighbors?

- What happens when you destroy the adjoining property rights and records of homeowners who never defaulted on their mortgages

fifty percent of all residential mortgages in the country, that is reason enough for this court to turn a blind eye to the fact that this process does not comply with the law."

3. Including the Office of the Comptroller of Currency, the Federal Reserve, the Federal Deposit Insurance Corporation and the Federal Housing Finance Agency. Wang, *supra* note 1. *See also* Nick Timiraos, *Critical Signs in Foreclosure Talks*, WALL STREET J., Apr. 12, 2011 (giving status of settlement with states' attorneys general, and federal regulators and lenders).

4. *See* Austin Kilgore, *Recorder Wants to Close Account at Bank of America to Protest MERS*, NATIONAL MORTGAGE NEWS, (April 11, 2011), at 8, *available at* http://www.nationalmortgagenews.com/on_features/recorder-wants-to-close-bofa-account-1024417-1.html?site=default_tech (regarding Registrar of Deeds in South Essex District of Massachusetts). "MERS saved banks time and money by providing a private, electronic alternative to the public system used by local government recorders. By using the MERS registry, they largely avoided the recording fees." Wang, *supra* note 1.

5. For the purposes of this article, no distinction is made between race, notice, and race/notice. Race/notice is meant to encompass all designations.

are now forced to litigate boundary disputes and property rights?

- Why did the title insurance companies repeatedly refuse to underwrite foreclosures if land title was stable?[6]

These are the exact problems that MERS has created—the bigger problems that no one has explained—the elephant in the room. Thanks to MERS' failure to accurately complete and/or publically record property conveyances in the frenzy of banks securitizing home loans and in subsequent foreclosure actions,[7] neighbors to a foreclosed property (with a sequential conveyance[8]) as well as the foreclosed property itself will have unclear boundaries on the ground and clouded/unmarketable titles making it difficult, if not impossible, for these homeowners to sell their properties and for subsequent purchasers to obtain title insurance and financing on that property. We will not be able to determine senior (superior) and junior (inferior) property rights designations because no one will know which parcels were conveyed first in time and to whom.

The MERS system has created an environment in which tens of thousands of titles have been lost or diluted in a sea of MERS transactions and may take a hundred years to fix, while forcing innocent adjacent homeowners to litigate in order to reclaim their property rights. This article will: (1) summarize the history of how land was surveyed and divided in the Western United States, (2) explain how junior and senior property rights are determined in the face of a boundary dispute, (3) briefly discuss the robo-signer scandal, the problem with the MERS system and recent court cases involving MERS, (4) describe exactly how MERS has destroyed or severely diluted chains of title for boundary disputes between foreclosed properties' subsequent owners and all of their neighbors, (5)

6. At one point in October 2010, Old Republic was reportedly refusing to write title policies for some foreclosures altogether. Stephanie Armour, *Old Republic To Stop Writing Policies For Some Foreclosures*, USA TODAY, October 2, 2010, http://www.usatoday.com/money/economy/housing/2010-10-02-old-republic-foreclosures_N.htm.

7. "For banks, the local government recorders weren't speedy enough especially as the mortgage industry moved into the business of securitization, or bundling and selling mortgages." Wang, *supra* note 1.

8. A sequential conveyance occurs when:

> a portion of a tract of land is sold, two or more parcels are created, a new parcel and the remainder parent parcel. Because the new parcel must receive all of the land described, it is called the senior deed, and the remainder, at the time of conveyance, becomes the junior deed. Sequential conveyances are those written deeds in which junior and senior rights exist between two adjoining parcels. In general, sequential conveyances came into being because of a lapse of time between successive conveyance instruments.

BROWN, CURTIS M., WALTER G. ROBILLARD, DONALD A. WILSON, BROWN'S BOUNDARY CONTROL AND LEGAL PRINCIPLES § 11.2 (6th ed. 2009).

analyze the resulting difficulty these subsequent homeowners and their neighbors will experience when attempting to sell their properties (with clouded titles) when purchasers will not be able to obtain title insurance (without seller indemnity) and financing.

II. LAND DIVISION AND CHAIN OF TITLE IN THE UNITED STATES

A. A BRIEF HISTORY LESSON

The concept of land title is uniquely American. Historically, Native Americans had no concept of written title because they did not believe that any person could "own" land. European settlers changed this belief by imposing the concept of land ownership by individual people on the New World of America.[9] Today, the concept of *stable* individual "land ownership" separates America from most of the rest of the world. In the United States, the following key concepts are true: (1) real property law rights and defenses all tie to accurate and publically recorded chain of title and property ownership records at the county level, (2) accurate publically recorded chain of title documents are critical in determining land ownership (senior and junior property rights) avoiding the need for litigation, (3) there are no federal laws governing private property rights. Therefore, a federal system of title (electronic or otherwise) is not feasible, (4) the stability of the land title is paramount in preserving land ownership and maintaining civil harmony, and (5) real property is a secure and valuable investment.

In the Western States, land division began with the Louisiana Purchase of 1803. According to this statute and pursuant to the Land Act of 1805, land was to be surveyed west of the Mississippi River all the way to California (excluding Texas at that time).[10] Government Land Office ("GLO") surveyors, beginning in Ohio, were tasked with subdividing land into one square mile sections—each containing 640 acres.[11] Nevertheless, no two parcels are exactly the same when measured on the ground due to rough terrain, bad weather, and antiquated instruments and, sometimes, surveyors' failure to survey at all. These subdivided 640 acres varied from a few inches to several hundred feet. Like snowflakes, each 640-acre section was different and these discrepancies remain today.

As early as 1891, the California legislature recognized that land

9. BROWN, ROBILLARD, AND WILSON, *supra* note 8, at § 1.2.
10. *Id.* at § 6.
11. *Id.*

subdivided by way of a written description was prone to title defects, gaps, gores and overlaps which resulted in expensive litigation. At that time, California (and most other states) enacted laws that required a land surveyor to file a *public record* each time one of these property lines was established by a surveyor. These laws were intended to make the property line determinations available to the public, thus avoiding litigation to resolve disputes associated with unfiled records or unclear boundaries.

Modern day surveyors are still discovering discrepancies in the course of conducting boundary surveys; therefore, it is easy to see why material discrepancies in title still arise. The only way to resolve these boundary discrepancies, absent litigation, is by examination of the chain of title to determine senior and junior property rights and divide the land according to established legal principles.

B. The Surveyor's Role – Determining Senior and Junior Property Rights In Sequential Property Conveyances

As a practical matter, the law (and surveyors) deals with boundary discrepancies discovered by surveys, without the need for litigation, by examining the chain of title (found in publically recorded documents and grantor/grantee indexes) back to the original owner and grantor to determine senior and junior rights for sequential conveyances. The real property's history of conveyances from one owner to another is called a "chain of title." Chain of title is specifically defined as the "record of successive conveyances, or other forms of alienation, affecting a particular parcel of land, arranged consecutively, from the government or original source of title down to the present holder."[12]

Because only evidence of ownership is recorded in these public records, to prove ownership of a particular parcel, a property owner must show a continuous title record back to the first conveyance by the original owner/grantor that described the parcel. The compilation of all title ownership is known as the chain of title or chain of record.[13] When a portion of a tract of land is sold, two or more parcels are created including a "new parcel" and the "remainder" of the parent parcel.[14] A parcel is apportioned according to well-settled principles found in race/notice statutes. Because the "new parcel" must receive all the land described, it is called the "senior deed" (or "senior parcel", "senior rights") and at the time of conveyance the "remainder" becomes the "junior deed" (or "junior

12. BLACK'S LAW DICTIONARY 229 (6th ed. 1990).
13. BROWN, ROBILLARD, AND WILSON, *supra* note 8, at 457.
14. *Id*. at 301.

parcel," "junior rights").[15] "Sequential conveyances" are those written deeds in which junior and senior rights exist between adjoining parcels.[16] Stated another way, the first (in time) conveyance by deed is called the senior conveyance. The next (in time) conveyance by deed is called the junior conveyance. Four well established principles in law and in surveying that determine senior and junior property rights are stated as follows:

(1) "As between private parties in a land dispute, a senior right is superior to a junior right;"[17]

(2) "As between private parties, a junior grant, in conflict with a senior grant, yields to the senior grant;"[18]

(3) A grantor cannot convey what he does not own;[19] and

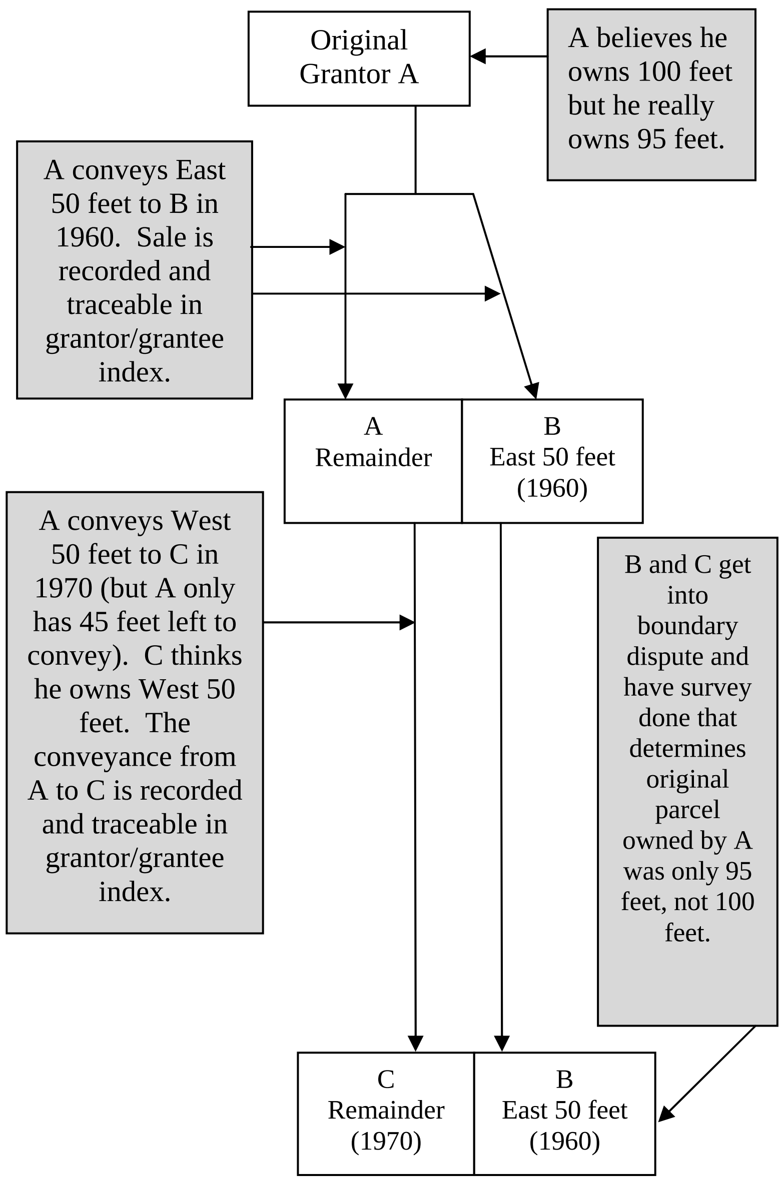
(4) Between equal equities, the first in order of time shall prevail.[20]

These principals establish the rights of the parties when excesses or, more importantly, when deficiencies in the amount of land conveyed to two parties occurs. The surveyor (and the courts) study the chain of title from recorded public deeds/title documents to determine senior and junior rights designations based on the portion of the parcel that was conveyed first in time (pursuant to race/notice statutes) by the original grantor. Based on existing case law and statutory authority, this boundary determination is made clearly and accurately without the need for litigation as to the location of the property lines.

Diagram A on the following page shows the importance of a clear chain of title.

15. BROWN, ROBILLARD, AND WILSON, *supra* note 8, at 301.
16. *Id.*
17. *Id*. at 297.
18. *Id*. at 303.
19. Caselli v. Messina, 567 N.Y.S.2d 972, 973-74 (App. Div. 1990).
20. *Maxims of Equity*, WIKIPEDIA, http://en.wikipedia.org/wiki/Maxims_of_equity (last updated Dec. 5, 2011) (citing Richard Edwards, Nigel Stockwell (Pearson Education, 2005) *Trusts and Equity*, pg. 34).

Diagram A
Normal Conveyance (Non-MERS)



1. B and C now have a problem. How is A's original parcel divided?

2. The division between B and C is determined by examining the chain of title (found in the publicly recorded documents and the grantor/grantee indexes) back the original grantor A.

3. B acquired the East 50 feet from A in 1960 leaving A with 45 feet.

4. C acquired the West 50 feet from A in 1970, however, A only had 45 feet left to convey.

5. Because B acquired his 50 feet first in time (superior) he keeps 50 feet and C keeps the remaining 45 feet (junior).

6. C's deed is reformed to reflect 45 feet and this document is recorded.

This basic example shows the importance of a clear chain of title in determining property rights in sequential conveyances, particularly when dealing with a previously flawed survey or an ambiguous conveyance. In the event that the chain of title cannot be recovered, owners will be forced to litigate boundaries because they will not be able to determine the senior rights—the exact problem created by MERS. See Diagram B below.

III. ROBO-SIGNER MORTGAGE FRAUD

One year ago, the American public was unfamiliar with the term "robo-signer" describing loan processors and attorneys signing as many as 10,000 foreclosure documents a month (like robots) without reviewing the documents' contents.[21] Many lenders, including Fannie Mae and Freddie Mac, turned to law firms ("foreclosure mills") that specialized in quick processing of thousands of foreclosures for banks.[22] A foreclosure mill is created in the following scenario:

A loan is securitized through MERS (wherein MERS is presumably the mortgagee holding land title and is also named as the nominee by the promissory note holder). At this point, the promissory note and the mortgage are separated. The promissory note is then pooled with other

21. Ariana Eunjung Cha & Brady Dennis, *Under Piles of Paperwork, a Foreclosure System in Chaos*, WASHINGTON POST, Sept. 23, 2010, http/www.washingtonpost.com/wp-dyn/content/article/2010/09/22/AR2010092206146.html.

22. Stephanie Armour & Thomas Frank, *Ex-worker: Florida Law Firm Ran "Foreclosure Mill"*, USA TODAY, Oct. 18, 2010, http://www.usatoday.com/money/economy/housing/2010-10-18-witness-foreclosure-documents_N.html.

promissory notes, repackaged, resold and haphazardly tracked (or not tracked at all) through the private MERS system. Nevertheless, this promissory note is *not* publically recorded and oftentimes is lost or misplaced. Subsequently, when a property goes into default, the foreclosing party must prove ownership (conveying standing) to foreclose. This becomes a problem. The last promissory note assignee, (who may or may not possess the promissory note) claims ownership. Meanwhile, the land title mortgage may be held by MERS. [23]

Banks have subsequently argued, with limited success, that even though separated, the mortgage actually follows the note. It is the marriage of the promissory note (often times lost or nonexistent) and the mortgage (after lost or nonexistent assignments) that was the incentive for robo-signer fraud. Using robo-signers to falsify and recreate these previously lost or nonexistent documents was the remedy created by the servicers—resulting in fraud, forgery and falsification of legal documents. The irony of the foreclosure mills and robo-signers is that at any given bank, front line bank teller requires multiple forms of identification, thumb prints and signature verifications in order for a customer to cash a check while the same banks use robo-signers to create tens of thousands of forgeries (or their latest preferred term of "surrogate signatures").[24]

This conduct at foreclosure mills reached fraudulent levels and caused the fifty states attorneys general to convene a committee (headed by Tom Miller, Attorney General of Iowa) to investigate this fraudulent activity by mortgage servicers.[25] Bank executives and states' attorneys general came up with initial settlement terms in March, 2011 with a price tag of $20 billion and wide ranging releases of liability.[26] Preliminary agreement terms for any settlement between the attorneys general and large banks have been deeply criticized.[27] New York Attorney General Eric T. Schneiderman is one of a hand full of attorneys general not willing to

23. *See* Diagram B *infra*.

24. Christine Stapleton, *Surrogate Signers Signed Countless Foreclosure Documents With Someone Else's Name*, WALL STREET MAIN STREET (Apr. 1, 2011), http://www.wallstreetmainstreet.com/2011/04/surrogate-signers-signed-countless.html.

25. Lorraine Woellert, Dakin Campbell & Carter Dougherty, *Mortgage Servicers Said To Agree to Fix Foreclosure Procedures*, BLOOMBERG (Apr. 5, 2011), http://www.bloomberg.com/news/2011-04-05/mortgage-servicers-said-to-agree-to-fix-foreclosure-procedures.html. *See also* Dave Clarke, *Update 1 – Iowa AG Looks To Foreclosure Deal Within 2 Months*, REUTERS (Mar. 7, 2011), http://www.reuters.com/article/2011/03/07/financial-regulation-servicing-idUSN0712043720110307.

26. Gretchen Morgenson, *The Banks Still Want a Waiver*, N.Y. TIMES, July 23, 2011, www.nytimes.com/2011/07/24/business/bank-settlement-in-mortgage-mess-may-hinge-on-mers.html.

27. Gretchen Morgenson, *Attorney General of N.Y. Is Said to Face Pressure on Bank Foreclosure Deal*, N.Y. TIMES, Aug. 21, 2011, www.nytimes.com/2011/08/22/business/schneiderman-is-said-to-face-pressure-to-back-bank-deal.html?pagewanted=all.

support the proposed settlement.[28] Nevertheless, high level government officials have pressured Schneiderman to agree to the proposed settlement.[29] Most recently, when Schneiderman refused to fall in line, he was kicked off of the fifty-state task force.[30] Subsequently, John O'Brien, Registry of Deeds for Southern Essex County, Massachusetts, and an outspoken opponent of MERS, called for Tom Miller to step down as task force chairperson.[31]

Massachusetts Attorney General Martha Coakley stated that she would not sign on to any deal that would release the banks from liability for MERS practices and Attorneys General from Delaware, Minnesota, Kentucky and Nevada joined New York's Scheiderman in believing that the negotiations were absolving banks of too much liability.[32]

More recently, California's Attorney General Kamala Harris broke away from the fifty state mortgage settlement.[33] Looming issues regarding any settlement between the attorneys general committee and banks relate to potential liability stemming from MERS.[34] Harris stated that she pulled out of the talks because the pending deal was "inadequate for California homeowners" and gives bank officials too much legal immunity.[35] The departure of California (a large state in terms of population, foreclosure exposure and electoral college) along with the other states that have abandoned the settlement talks means that any settlement between remaining states has limited practical meaning or credibility.[36] David Pelligrinelli, president of AFX Title, a title research company, stated that MERS contributed to the problem of thousands of mortgages lacking a

28. Morgenson, *supra* note 27.

29. *Id*.

30. Richard Zombeck, *John O'Brien MA Registry of Deeds: AG Tom Miller Should Step Down*, HUFFINGTON POST, Sept. 2, 2011, www.huffingtonpost.com/richard-zombeck/john-obrien-ma-registry-o_b_935417.html.

31. *Id*.

32. Jon Prior, *Iowa AG: Banks May Face Criminal Liability After Robo-Signing Settlement*, HOUSINGWIRE.COM (Sept. 2, 2011), www.housingwire.com/2011/09/02/iowa-ag-banks-may-face-criminal-liability-after-robo-signing-settlement. *See also* Letter from Lori Swanson, Attorney General of Minnesota, to Tom Miller, Iowa Attorney General, (Sept. 9, 2011) *available at* http://static1.firedoglake.com/37/files/2011/09/Document.pdf (stating that any settlement between government regulators and the mortgage industry should have "teeth" and hold "banks accountable for their wrongful conduct, enjoining future unlawful activity, and helping injured homeowners"). *See also* Yves Smith, *Game Over: California Attorney General Breaks From "50 State" Mortgage Settlement*, NAKED CAPITALISM (Sept. 30, 2011), www.nakedcapitalism.com/2011/09/california-attorney-general-breaks-from-50-state-mortgage-settlement.html.

33. Smith, *supra* note 32.

34. Morgenson, *supra* note 27.

35. Smith, *supra* note 32. *See also* Matt Taibibi, *The Next Big Bank Bailout*, ROLLING STONE (Oct. 5, 2011), www.rollingstone.com/politics/blogs/taibblog/attorneys-general-settlement-the-next-big-bank-bailout-20111005.

36. Smith, *supra* note 32.

complete ownership chain.[37] According to Pelligrinelli "[y]ou can't go back and re-document these things, because some of the companies aren't around anymore. Even if they are, the charters for these companies don't allow for backdating of assignments."[38]

Lawyers who have examined this issue state that it would be unprecedented to grant a broad release from liability to banks that own MERS from claims that have not been investigated.[39] Furthermore, a broad release of liability would vastly diminish the possibility of an in-depth investigation of MERS and might also make it harder for borrowers to argue that MERS had no right, or standing, to foreclose on them.[40]

New York Attorney General Eric T. Schneiderman is also moving to block a proposed $8.5 billion settlement struck in June, 2011 by Bank of New York Mellon and Bank of America over troubled loan pools issued by Countrywide.[41] Attorney General Schneiderman filed suit against Bank of New York for fraud in its role as trustee overseeing pools of investors.[42] Additionally, the Office of the Comptroller of Currency, the Federal Reserve, the Office of Thrift Supervision and the Federal Deposit Insurance Corporation are negotiating with the largest U.S. mortgage servicers and signing consent decrees to improve foreclosure procedures.[43]

The Federal Reserve recently requested that Bank of America buy back (known as "put backs") residential mortgage backed securities ("RMBS"), exclusive of the commercial mortgage market, totaling $47 billion.[44] These securities were called into question when authorities discovered the robo-signer problem. Fannie Mae and Freddie Mac requested that Bank of America buy back RMBS totaling $5.6 billion in June 2010.[45] Bank of America, in turn, sued the FDIC for $1.75 billion for

37. Morgenson, *supra* note 26.

38. *Id*.

39. *Id*.

40. *Id*.

41. Gretchen Morgenson, *Mortgage Settlement Changed*, N.Y. TIMES, Aug. 4, 2011, http://www.nytimes.com/2011/08/05/business/new-york-moves-to-block-mortgage-settlement.html. See also Yves Smith, *New York Attorney General Schneiderman Drops Bomb on Bank of America Settlement and Bank of New York*, NAKED CAPITALISM (Aug. 5, 2011), http://www.nakedcapitalism.com/2011/08/new-york-attorney-general-schneiderman-drops-bomb-on-bank-of-america-settlement-and-bank-of-new-york.html.

42. *Id*.

43. Lorraine Woellert, Dakin Campbell and Carter Dougherty, *Mortgage Servicers Said To Agree to Fix Foreclosure Procedures*, BLOOMBERG, (Apr. 5, 2011), http://www.bloomberg.com/news/2011-04-05/mortgage-servicers-said-to-agree-to-fix-foreclosure-procedures.html.

44. "Securitization" refers to mortgage loans pooled into trusts and converted into mortgage-backed securities that can be bought and sold by investors. U.S. Bank Nat'l Ass'n v. Ibanez, 941 N.E.2d 40, 46 (2011).

45. *Bank of America Corp. Has $11.1 Billion In Mortgage Purchase Requests*, AMERICAN BANKING AND MARKET NEWS (Aug. 9, 2010). http://www.americanbankingnews.com/2010/08/09/

"putbacks".[46] Bank of America has also sued First American Title claiming that First American has refused to cover more than 5,500 loans that have caused $535 million in losses.[47] In August 2011, insurer AIG filed a $10-billion suit against Bank of America, accusing them and their Countrywide Financial and Merrill Lynch units of misrepresenting the quality of mortgages that backed the securities purchased by AIG.[48] The SEC charged Citigroup's principal U.S. broker dealer subsidiary with misleading investors about a $1-billion collateralized debt obligation ("CDO") tied to the U.S. housing market in which Citigroup bet against investors as the housing market showed signs of distress.[49] After the CDO defaulted, investors were left with losses while Citigroup made $160 million in fees and trading profits.[50] Citigroup agreed to settle the SEC's charges (without admitting liability) on October 19, 2011, for $285 million to be returned to investors.[51]

The Federal Deposit Insurance Corporation ("FDIC") is warning that flaws may have infected millions of foreclosures and questioning whether other regulators' inquiries into problems at the U.S. mortgage-servicing companies have been sufficiently thorough.[52] Most recently, the Federal Housing Finance Agency ("FHFA") that oversees the mortgage giants Fannie Mae and Freddie Mac is set to file lawsuits, seeking billions of dollars in compensation, against more than a dozen big banks (including Bank of America, JPMorgan Chase, Goldman Sachs, and Deutsche Bank), accusing them of misrepresenting the quality of mortgage securities they assembled and sold at the top of the mortgage bubble.[53] The suits will argue that banks, which assembled the mortgages and marketed them as securities to investors, failed to perform the due diligence required under securities law, and overlooked evidence that borrowers incomes were

bank-of-america-corp-nyse-bac-has-11-1-billion-in-mortgage-purchase-requests/#.

46. Karen Gullo, *FDIC Sued By Bank of America Over Taylor Bean Mortgage Losses*, BLOOMBERG, (Oct. 19, 2010), http://www.bloomberg.com/news/2010-10-20/bank-of-america-sues-fdic-over-taylor-bean-mortgage-s-1-75-billion-losses.html.

47. David Mildenberg, *Bank of America Sues First American on Lien Protection Claims*, BLOOMBERG, (Feb. 22, 2011), http://www.bloomberg.com/news/2010-10-20/bank-of-america-sues-fdic-over-taylor-bean-mortgage-s-1-75-billion-losses.html.

48. Nelson D. Schwartz, *U.S. Is Set to Sue a Dozen Big Banks Over Mortgages*, N.Y. TIMES, Sept. 1, 2011, at A1.

49. Press Release, U.S. Securities and Exchange Commission, *Citigroup to Pay $285 Million to Settle SEC Charges for Misleading Investors About CDO Tied to Housing Market* (Oct. 19, 2011), *available at* http://www.sec.gov/news/press/2011/2011-214.htm.

50. *Id*.

51. *Id*.

52. Alan Zibel, *FDIC's Bair: Millions of Foreclosures Could Be 'Infected'*, WALL ST. J., May 12, 2011, http://blogs.wsj.com/developments/2011/05/12/fdics-bair-millions-of-foreclosures-could-be-infected.

53. Nelson D. Schwartz, *U.S. Is Set to Sue a Dozen Big Banks Over Mortgages*, N.Y. TIMES, Sept. 1, 2011, http://www.nytimes.com/2011/09/02/business/us-is-set-to-sue-dozen-big-banks-over-mort gages. html.

inflated or falsified.[54] When borrowers were unable to pay their mortgages, the securities backed by the mortgages quickly lost value.[55] Fannie and Freddie lost more than $30 billion, in part as a result of these deals, and the subsequent losses were mostly passed on to taxpayers.[56]

In 2008, the Housing and Economic Recovery Act ("HERA") established the Federal Housing Finance Agency ("FHFA") as a supervisor and regulator of Fannie Mae and Freddie Mac.[57] Through its investigation in 2010, the FHFA recommended that it review the circumstances surrounding FHFA's failure to identify foreclosure abuses by the retained attorney network used by Fannie Mae and Freddie Mac, develop procedures for default related legal services and develop and implement policies and procedures to address poor performance by default-related legal services vendors.[58]

Furthermore, according to a Reuters investigation (as reported by the *Huffington Post*), despite these actions by elected officials and governmental regulators, mortgage lenders are continuing to take the same shortcuts, from sketchy paperwork to the use of robo-signers.[59] Reuters found that some of the biggest U.S. banks and other loan servicers continue to file questionable foreclosure documents with courts and county clerks using the same tactics that triggered an outcry, multiple investigations and temporary moratoriums on foreclosures.[60] In recent months, servicers have filed thousands of documents that appear to have been fabricated or improperly altered, or have sworn to false facts.[61] Reuters also identified at least six "robo-signers" who have each recently falsely signed thousands of mortgage assignments.[62] A similar Associated Press article published in November 2011 revealed that, in investigations in July of the same year, servicers were continuing to generate documents signed by well-known robo-signers, including the notorious "Linda Greene".[63] According to the

54. Schwartz, *supra* note 53.
55. *Id*.
56. *Id*.
57. OFFICE OF INSPECTOR GENERAL, FED HOUSING FIN. AGENCY, *FHFA'S OVERSIGHT OF FANNIE MAE'S DEFAULT-RELATED LEGAL SERVICES*, 8 (Sept. 30, 2011), http://www.fhfaoig.gov/Content/Files/AUD-2011-004.pdf.
58. *Id*. at 16–17.
59. Scot J. Paltrow, *Banks Continue 'Robo-Signing' Foreclosure Practices In Spite Of Promises To Contrary: Investigation*, REUTERS (July 18, 2011, 7:39 PM) http://www.reuters.com/article/2011/07/18/foreclosure-banks-idUSL3E7II1UC20110718.
60. *Id*.
61. *Id*.
62. *Id*.
63. Yves Smith, *Bank CEOs Lying When They Say They've Stopped Robosigning*, NAKED CAPITALISM (Nov. 4, 2011), http://www.nakedcapitalism.com/2011/11/banks-lying-when-they-say-theyve-stopped-robosiging.html.

April 2011 *60 Minutes* piece, "Linda Greene" was supposedly a vice president at twenty different banks at the same time.[64]

Additionally, Nevada Attorney General Catherine Cortez Mastro recently filed a 606 count indictment against two title officers of Lender Processing Services ("LPS") in Clark County, Nevada for supervising and filing tens of thousands of documents in a robo-signing scheme.[65] Many of these charges were category C and D felonies.[66] A Nevada grand jury subsequently indicted two LPS employees on alleged robo-signing of foreclosure documents.[67]

Gone are the days of the S&L bailouts ultimately resulting in a net loss to tax payers of approximately $124 billion by the end of 1999.[68] Ironically, some of the same players are involved again. Now, some of the former Keating Five (still in public service) can advise our current government how to wade through the MERS fiasco. Banks, originators and servicers are Lucy and the American taxpayer is Charlie Brown.

IV. THE MERS SYSTEM

A. WHAT IS MERS?

MERS is a corporation registered in Delaware and headquartered in the Virginia suburbs of Washington, D.C.[69] that operates a computer database designed to track servicing and ownership rights of mortgage loans anywhere in the United States.[70] Originators and secondary market players pay inexpensive membership dues and per-transaction fees to MERS in exchange for the right to use and access MERS' records.[71] In

64. Chris Kirkham, *Sarah Palin's Arizona Home Purchase Clouded By Foreclosure Fraud, Analysis Finds*, HUFFINGTON POST (June 10, 2011), http://www.huffingtonpost.com/2011/06/10/sarah-palin-arizona-home-foreclosure fraud_n_875186.html.

65. Yves Smith, *Nevada Attorney General Mastro Files 606 Count Criminal Indictment Against Two Title Officers (Updated: Lender Processing Services Employees)*, NAKED CAPITALISM (Nov. 16, 2011), http://www.nakedcapitalism.com/2011/11/nevada-attorney-general-mamsto-files-606-count-criminal-indictment-against-two-title-officers.html.

66. *Id*.

67. Andrew Scoggin, *Nevada Grand Jury Indicts 2 LPS Workers On Robo-Signing Charges*, HOUSING WIRE, (Nov. 16, 2011), http://www.housingwire.com/2011/11/16/nevada-grand-jury-indicts-2-on-robo-signing-charges.

68. Timothy Curry & Lynn Shibut, *The Cost of the Savings and Loan Crisis: Truth and Consequences, Federal Deposit Insurance Corporation*, 13 FDIC BANKING REV. 26, 33 (2000), *available at* http://www.fdic.gov/bank/analytical/banking/2000dec/brv13n2_2.pdf.

69. Carson Mullen, *MERS: Tracking Loans Electronically*, MORTGAGE BANKING 63 (May 31, 2000) http://www.allbusiness.com/finance/3594162-1.html.

70. Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING 42 (Jan. 1, 1997) http://www.allbusiness.com/finance/608126-1.html.

71. Schneider, *supra* note 70.

addition to tracking ownership and servicing rights, when closing on home mortgages, many mortgage lenders now list MERS as the "mortgagee of record" on the paper mortgage rather than the actual mortgagee.[72] MERS was designed to improve the efficiency and profitability of the primary and secondary mortgage markets.[73] The benefit of naming MERS as the nominal mortgagee of record is that when the member transfers an interest in the mortgage loan to another MERS member, MERS may (or may not) privately track the assignment within its system, however, MERS remains the mortgagee of record in publicly recorded documents.[74] In 2011, MERS proposed a rule change to stop members from foreclosing in its name.[75]

B. MERS CONNECTION TO SUB-PRIME LOANS AND SECURITIZATION

Before 1995, typically a qualified home buyer applied for a mortgage loan (whole-loan) with his/her local bank, credit union or savings and loan.[76] The credit-worthy borrower agreed to make payments until the mortgage debt was paid in full. Around 1995, a new breed of loan came into play—the sub-prime loan. These loans (often times for one hundred percent or more of the market value of the residential property and no longer dependent upon a borrower's credit worthiness) changed the landscape of mortgage banking, leading, in part, to the current foreclosure crisis. These loans were created and supported by lawmakers. For example, according to Congresswoman Maxine Waters:

> [U]nder the outstanding leadership of Mr. Frank Raines everything in the 1992 act has worked just fine. In fact, the GSE's [Fannie and Freddie] have exceeded their housing goals. What we need to do today is to focus on the regulator, and this must be done in a manner so as not to impede their affordable housing mission, a mission that has seen innovation flourish from desktop underwriting to 100 percent loans.[77]

Knowing that their borrowers were not credit worthy and that the borrowers' home mortgages would almost certainly end in default,

---

72. R.K. Arnold, *Yes, There Is Life On MERS*, 11 PROB. & PROP. 16, 32–34 (1997).

73. John R. Hooge & Laurie Williams, *Mortgage Electronic Registration Systems, Inc.: A Survey of Cases Discussing MERS Authority To Act*, NORTON BANKR.LAW ADVISOR, Aug. 2010, at 2.

74. *Id*.

75. Laura Marcinek, *BofA, Citigroup Say Mortgage Database Draws Scrutiny In Foreclosure Probe*, BLOOMBERG (Mar. 2, 2011), http://www.businessweek.com/news/2011-03-02/bofa-citigroup-pnc-say-mers-mortgage-database-draws-probes.html.

76. Scot Paltrow & Leslie Adler (editor), *Factbox: The Role of MERS In Foreclosure Furor*, REUTERS (Oct. 13, 2010), http://www.reuters.com/article/2010/10/13/us-usa-foreclosures-mers-idUSTRE69C69720101013.

77. *The Secondary Mortgage Market Enterprises Regulatory Improvement Act: Hearing on H.R. 2575 Before the H. Comm. On Fin. Serv. U.S. H.R.*, 108th Cong. 9 (2003) (statement of Rep. Maxine Waters), *available at* http://www.gpo.gov/fdsys/pkg/CHRG-108hhrg92628/pdf/CHRG-108hhrg92628.pdf. (emphasis added).

mortgage lenders unloaded these loans as quickly as possible to large institutional banks. These banks, in turn, bought and sold the loans amongst themselves and subsequently pooled them into trusts and then converted them into mortgage backed securities (also referred to as collateralized debt obligations ("CDOs"), meaning that the asset behind the paper is real property). These CDOs were bought and sold by and to investors.[78] Mortgage-backed securities were almost uniformly rated AAA or Aaa by Fitch, Moody's and Standard & Poors.[79] The AAA rating was appealing to risk adverse investors and these mortgage backed securities ended up in conservative pension funds such as CalPERS and conservative investment brokerage funds owned by companies such as MetLife, Blackrock, Inc. and Allstate.[80]

In the midst of creating these trusts and mortgage-backed securities, MERS was created to shuffle these loans quickly between lenders, leaving homeowners unable to find out who actually owned their mortgage at any given time.[81]

> Mortgages would be changing hands dozens of times, going from loan originators to banks to Wall Street investment houses, which would collect them by the thousands and package them into complex debt instruments that would be chopped up into shares and sold off to multiple investors all over the world.[82]

C. What is Wrong with MERS?

After the financial collapse of 2008, MERS began foreclosure actions on behalf of lenders.[83] The creation of MERS allowed mortgage companies to list MERS as the proxy for the true mortgage holder in local government records and to record subsequent changes of ownership in the MERS

78. Yasha Levine, *How an Obscure Outfit Called MERS Is Subverting Our Entire System of Property Rights*, ALTERNET (Dec. 16, 2010), http://www.alternet.org/economy/149189/dude,_where%27s_my_mortgage_how_an_obscure_outfit_called_mers_is_subverting_our_entire_system_of_property _rights/?page=entire.

79. Peter Cohan, *Behind the $4 Trillion in CDOs: Sneaky Banks and Worthless Ratings*, DAILY FINANCE (Apr. 26, 2010, 10:45AM), http://www.dailyfinance.com/2010/04/26/explaining-the-4-trillion-cdo-scam-worthless-ratings-hide-inve/ (also stating that ninety-three percent of the 2006 AAA ratings were later downgraded to junk).

80. *Allstate Sues BofA on MBS Purchase*, ZACKS.COM (Dec. 30, 2010), http://www.zacks.com/stock/news/45341/Allstate+Sues+BofA+on+MBS+Purchase (last visited Feb. 3, 2012).

81. This lack of knowledge often led to payments made to the wrong bank or lender because the homeowner could not look to publicly recorded deeds to determine the ever changing identity of their lender. Michael Grover, *Fed-led Research Reveals Need for Better Twin Cities Foreclosure Data*, COMMUNITY DIVIDEND (Sept. 1, 2006), http://www.minneapolisfed.org/publications_papers/pub_display.cfm?id=2200.

82. Levine, *supra* note 78.

83. Robbie Whelan, *Lawmaker Questions Power To Foreclose*, WALL ST. J. (Nov. 1, 2010), http://online.wsj.com/article/SB10001424052748704865104575588791583567372.html.

system only.[84] A spokeswoman for Fannie Mae told the *New York Times* that Fannie Mae could never rely on MERS to find ownership of a loan.[85] In 2010, Alan M. White (Law Professor at Valparaiso University Law School, Indiana) matched MERS ownership records against those in the public domain and found that fewer than thirty percent of the mortgages had accurate records in MERS.[86] Robo-signed documents, inaccurate or non-existent record keeping, the failure to publically record assignments of mortgages and the use of MERS as the mortgagee or nominee have led to the homeowners' inability to figure out who owns and services their mortgages or to trace back their chain of title. In using the inaccurate and alleged to be fraudulent MERS system, banks are actually denying homeowners their due process rights before they lose their homes to foreclosure.

Furthermore, because the MERS system allowed lenders to avoid the time and expense of going through the County Recorder's office to file and record title documents, MERS also robs County Recorders of filing fees. In fact, various county recorders have begun to take action attempting to recoup some of these fees. In Massachusetts, South Essex Register of Deeds John O'Brien reported that he had received a green light to withdraw what could be millions of dollars from Bank of America accounts by arguing that banks have used MERS to deny the South Essex registry millions of dollars in fees to which it was entitled.[87] Dallas County District Attorney Craig Watkins filed a lawsuit (later turned into a class action) against MERS and Bank of America Corp. over unpaid filing fees.[88] Similarly, counties in Kentucky, Michigan, Ohio and Oklahoma have also sued MERS—all claiming that the MERS system has cheated them out of filing fees.[89]

Some homeowners are arguing that MERS does not have a right to initiate foreclosure actions because MERS does not hold the title and the corresponding note to their properties. These same homeowners are also

84. Marian Wang, *Backgrounder: A Closer Look at MERS, the Industry's Controversial Mortgage Clearinghouse*, PROPUBLICA (Mar. 7, 2011, 4:53 PM), http://www.propublica.org/blog/item/backgrounder-a-closer-look-at-mers-the-industrys-controversial-mortgage-cle (emphasis added).

85. Wang, *supra* note 84.

86. *Id*.

87. Eric Convey, *Deeds Head Gets OK To Yank BofA Funds*, BOS. BUS. J. (April 6, 2011, 9:46AM),http://www.bizjournals.com/boston/news/2011/04/06/deeds-head-gets-ok-to-yank-bofafunds.html; *see also* Austin Kilgore, *Recorder Wants To Close Account at Bank of America To Protest MERS*, NAT'L MORTG. NEWS (Apr. 11, 2011, 11:20PM), http://www.nationalmortgagenews.com/on_features/recorder-wants-to-close-bofa-account-1024417-1.html.

88. Margaret Cronin Fisk, *Dallas Revises MERS Filing-Fee Suit to Add All Texas Counties*, BLOOMBERG (Nov. 1, 2011), http://www.bloomberg.com/news/2011-11-01/dallas-seeks-to-add-all-texas-counties-to-mers-filing-fee-suit.html.

89. *Id*.

arguing that the MERS system does not accurately show which lender holds the trust deed for title on the foreclosed property. Furthermore, even if MERS forecloses a property for a lender (that does not actually have title and the corresponding note to the property), an argument could be made that the lender may be prohibited from reselling the property because the lender cannot sell that which it does not own. According to recent court rulings, there may be no standing to foreclose without proof of title and the note, there may be no standing to foreclose.[90] To foreclose on real property, the plaintiff must establish the chain of title entitling plaintiff to relief.[91] MERS has acknowledged, and recent cases have held, that MERS is a mere nominee—an entity appointed by the true owner simply for the purpose of holding property in order to facilitate transactions.[92] Recent court opinions stress that this defect is not just a procedural one but is also a substantive failure, one that is fatal to the plaintiff's ability to foreclose.[93] Sheila Bair, former Chairperson of the FDIC, testified before a Senate Committee opining that flawed banking processes, including faulty transfers of loan documents, "have potentially infected millions of foreclosures, and the damages to be assessed against these operations could be significant and take years to materialize."[94] Bank-friendly legislators and attorneys generally would have the public believe that the entire economic recovery is tied to the public's willingness to look the other way.

MERS was set up without considering how it would destroy or seriously dilute accurate and recorded chain of title records in event of mass foreclosure. Already, chains of title have been lost in the frenzy of trading and packaging these mortgages into mortgage-backed securities. Today, MERS servicers and related foreclosure mills are literally breaking a centuries-old custom that protected property rights by requiring every sale of property to be publically recorded (pursuant to race/notice statutes) and requiring that any creditor claiming a right to foreclose demonstrate clear title (with an endorsed note in the creditor's name and a record at the county office showing transfer of the property). Subsequently, many

90. *See U.S. Bank National Ass'n v. Ibanez*, 941 N.E.2d 40, 44 (Mass. 2011); *In re* Agard, 444 B.R. 231, 254 (Bankr. E.D.N.Y. 2011).

91. Ellen Brown, *Homeowners' Rebellion: Could 62 Million Homes Be Foreclosure-Proof?*, YES! MAGAZINE (Aug. 18, 2010), http://www.yesmagazine.org/new-economy/homeowners-rebellion-could-62-million-homes-be-foreclosure-proof.

92. *Id*.

93. *Id*.

94. *Oversight of Dodd-Frank Implementation: Monitoring Systematic Risk and Promoting Financial Stability*: *Hearing Before the Senate Comm*. *On Banking, House*., *and Urban Affairs*, 112 Congress 22–23 (2011) (statement of Sheila C. Bair, Chairman, Federal Deposit Insurance Corporation), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=94d50f1a-75eb-4586-b025-76e44870816b.

homeowners can no longer search public records to find out who holds their mortgage because the record shows MERS as the mortgage holder and/or the purchaser of the foreclosed property, even though financial entities may act as a trustee to transactions. Chain of title may become lost due to its inability to be traced amongst the hundreds of thousands of MERS transactions. In the event the chain of title is lost (or at least diluted), MERS has a negative effect on the mortgaged homes, and each adjoining property adjacent to those homes, including those without a mortgage.[95] MERS is simply not a viable substitute for the four hundred year old system of publicly recording deeds pursuant to race/notice statutes in county records offices that make the deeds available for anyone to reference in determining property rights.

D. Recent Court Rulings Critical of MERS

MERS and securitization problems have come to light in several publicized court cases. A sampling of these recent cases include:

1. U.S. Bank National Association v. Ibanez

In January 2011, the Massachusetts Supreme Court affirmed a lower court's invalidation of two home foreclosures, stating that lenders Wells Fargo Bank and U.S. Bank had failed to prove that they owned the mortgages.[96] *Ibanez* dealt with loans that had been pooled into mortgage-backed securities. The two foreclosures were made in the names of Wells Fargo and US Bank; however, neither of the banks had written mortgages.[97] Instead, they were acting as trustees, or financial caretakers, for pools of loans made and serviced by other lenders.[98] The Massachusetts' Supreme Court stated:

> We agree with the judge that the plaintiffs, who were not the original mortgagees, failed to make the required showing that they were the holders of the mortgages at the time of foreclosure. As a result, they did not demonstrate that the foreclosure sales were valid to convey title to the subject properties, and their requests for a declaration of clear title were properly denied.[99]

The Court stated that, for plaintiffs to obtain the judicial declaration of

95. *See* Section 5 *infra*.
96. E. Scott Reckard, *Foreclosure Ruling Could Be Setback for Banks*, L.A. Times (Jan. 7, 2011), http://articles.latimes.com/2011/jan/07/business/la-fi-foreclosure-ruling-20110107. See also *Ibanez*, 941 N. E. 2d at 44.
97. *Id*. at 96.
98. Reckard, *supra* note 96.
99. U.S. Bank Nat'l Ass'n v. Ibanez, 941 N.E.2d 40,44 (Mass. 2011) (emphasis added).

clear title "they had to prove their authority to foreclose under the power of sale and show their compliance with the requirements on which this authority rests."[100] Plaintiffs could not provide this proof.[101] Plaintiffs needed to be assignees of the mortgage at the time of the notice of sale and subsequent foreclosure sale in order to exercise the power of sale contained in the mortgages.[102] Furthermore, the Court held that, like a sale of land itself, the assignment of a mortgage is a conveyance of interest in land that requires a writing signed by the grantor.[103]

As for the remedy in the case, the Supreme Court of Massachusetts ruled that the defendants' foreclosures had to be undone because industry securitization practices had violated real estate law governing how mortgages could be transferred.[104] Massachusetts is one of twenty-seven non-judicial foreclosure states. Although this ruling is only binding in Massachusetts, we can expect the other twenty-six states to more closely examine their previous lower court rulings. The end result may be an individual homeowner that owes the holder of their note the dollar value of the mortgage on the property; however, the property itself is no longer collateral for the loan.

Other courts have agreed with the reasoning in *Ibanez*. For example:

> It is the general rule that courts have power to vacate a foreclosure sale where there has been fraud in the procurement of the foreclosure decree or where the sale has been improperly, unfairly or unlawfully conducted, or is tainted by fraud, or where there has been such a mistake that to allow it to stand would be inequitable to purchaser and parties.[105]

The *Ibanez* problem highlights the flaws with the securitization process and the MERS system. Its failure to publically record deed transfers and conveyances (along with sloppy paperwork) led these mortgage transfers to be deemed invalid.

2. In re Agard

In the course of the bankruptcy case entitled *In re Agard*, a creditor sought relief from an automatic stay to foreclose on a second interest in the

100. *Ibanez*, 941 N.E.2d at 51 (emphasis added).

101. *Id*. at 54.

102. *Id*. at 55 (citing *In re Schwartz*, 366 B.R. 265, 269 (Bankr. D. Mass. 2007) ("Acquiring the mortgage after the entry and foreclosure sale does not satisfy the Massachusetts statute.").

103. *See Id.*

104. Thom Weidlich, *Foreclosures May Be Undone by Massachusetts Ruling on Mortgage Transfers*, BLOOMBERG (Jan. 6, 2011), www.bloomberg.com/news/print/2011-01-06.

105. 6 Angels, Inc. v. Stuart-Wright Mortgage, Inc., 85 Cal. App. 4th 1279, 1286 (2011); *see also In re* Agard, 444 B.R. 231, 244 (Bankr. E.D.N.Y. 2011)

debtor's real property.[106] MERS, as an intervener, argued that the terms of its membership agreement with the original lender and its successors in interest, as well as New York state agency laws, gave MERS the authority to assign a mortgage.[107] MERS argued that it held legal title to mortgages for its members/lenders as both "nominee" and "mortgagee of record."[108] In his highly critical response to MERS's request that the Court analyze the MERS business model, Judge Robert E. Grossman stated:

> The Court recognizes that an adverse ruling regarding MERS's authority to assign mortgages or act on behalf of its members/lenders could have a significant impact on MERS and upon the lenders which do business with MERS throughout the United States. . . . This Court does not accept the argument that because MERS may be involved with 50% of all residential mortgages in the country, that is reason enough for this Court to turn a blind eye to the fact that this process does not comply with the law.[109]

The Court rejected MERS arguments that it acted as nominee, mortgagee or agent, adding that "in all future cases which involve MERS, the moving party must show that it validly holds both the mortgage and the underlying note in order to prove standing before this Court."[110]

3. Bevilacqua v. Rodriguez

This Massachusetts Supreme Court case involves the rights of a third party Bevilacqua, who acquired title to a home in good faith against the procedural and legal safeguards surrounding the foreclosure process and procedural protections against wrongful foreclosures.[111] Bevilacqua acquired a home by quit claim deed from U.S. Bank (as trustee and note holder) in 2006.[112] U.S. Bank initiated foreclosure on the home's previous owner Pablo Rodriguez without receiving an official mortgage assignment from MERS.[113] Unfortunately, U.S. Bank did not actually have title to the property when it transferred the home to Bevilacqua.[114] On April 12, 2010, Bevilacqua filed a "try title" action in the Massachusetts Land Court to compel Rodriguez to try title to the property.[115] In his complaint, Bevilacqua claimed to reside at the property and hold record title but,

106. *In re Agard*, 444 B.R. at 235.
107. *Id*.
108. *Id*.
109. *Id.*
110. *Id*. at 254.
111. Bevilacqua v. Rodriguez, 955 N.E.2d 884, 918 (Mass. 2011).
112. *Id*. at 888.
113. *Id*.
114. *Id*.
115. *Id*.

because MERS had not assigned the mortgage to U.S. Bank at the time of foreclosure, Bevilacqua alleged that there was a cloud on his title in the form of "the possibility of an adverse claim by Rodriguez against Bevilacqua's title to the property."[116] Rodriguez had not been located and did not enter an appearance in this case.[117]

In 2005, Rodriguez granted a mortgage on the property to MERS, as nominee for Finance America, LLC.[118] This mortgage was recorded.[119] As of June 29, 2006, MERS had not assigned this mortgage to U.S. Bank, however, on this date, U.S. Bank executed a foreclosure deed referencing the mortgage and purporting to transfer the property pursuant to a foreclosure sale from U.S. Bank to U.S. Bank "as Trustee under the securitization Servicing Agreement dated as of July 1, 2005 . . . ."[120] One month later, MERS assigned the mortgage to U.S. Bank in a recorded assignment.[121] A confirmatory foreclosure deed was then granted on October 9, 2006, by U.S. Bank to U.S. Bank as trustee under the servicing agreement.[122] On October 17, 2006, U.S. Bank, as trustee, granted a quitclaim deed to Bevilacqua.[123]

The issue in this case was whether a person who holds title to property by virtue of a recorded deed, but whose title is clouded by a possible adverse claim due to deficiencies from a prior foreclosure in his chain of tile, has standing to try title. The Massachusetts Supreme Court, citing precedent from *U.S. Bank National Association v. Ibanez*, wrote that "Massachusetts adheres to the familiar rule that one who sells under a power of sale must follow strictly its terms so, where a foreclosure sale occurs in the absence of authority, there is no valid execution of the power, and the sale is wholly void."[124] The Court continued to explain that "[o]ne of the terms of the power of sale that must be strictly adhered to is the restriction on who is entitled to foreclose."[125]

The Court reasoned that by Bevilacqua "alleging that U.S. Bank was not the assignee of the mortgage at the time of the purported foreclosure, Bevilacqua is necessarily asserting that the power of sale was not complied with, that the purported sale was invalid, and that his grantor's title was

116. *Rodriguez*, 955 N.E.2d, at 888.
117. *Id*. at 887.
118. *Id*. at 888.
119. *Id*.
120. *Id*.
121. *Id*.
122. *Id.* at 888.
123. *Id*.
124. *Id*. at 892–93 (quoting U.S. Bank Nat'l Ass'n v. Ibanez, 458 Mass. 637, 646 (2011), quoting Moore v. Dick, 72 N.E. 967 (1905)).
125. *Id.*

defective."[126] The Court then stated that "[i]n light of its defective title, the intention of U.S. Bank to transfer the property to Bevilacqua is irrelevant and he cannot become owner of the property pursuant to a quit claim deed."[127]

The Court held that, although the purchaser was in physical possession of the property when he filed the try title action, he lacked standing because his chain of title rested on a foreclosure sale conducted by someone other than the mortgagee or his successors and that a single deed considered without reference to its chain of title was insufficient to show record title as required by Massachusetts law.[128] Additionally, the Court held that the purchaser could not claim record title based on a theory that he was a *bona fide* purchaser for value and without notice and dismissed Bevilacqua's complaint.[129]

Bevilacqua contrasts the principles of nemo dat quod non habet (you can't give away what you do not own) and bona fide purchaser (one who takes in good faith for value and without notice of defect will get legal protection against claims).[130] As exemplified in *Bevilacqua*, nemo dat prevails.[131]

One commentator summarized the problems associated with *Bevilacqua* as follows:

> The court just said you might be able to go back and re-foreclose (on the property) and prove title, but you do not have clear title now . . . . The issue for a homeowner has to prove that a foreclosing entity had the right to foreclose. But if I am someone who has bought a foreclosure, I now cannot sell my home until I can prove that the foreclosing entity had that right of foreclosure, which might be difficult for me to prove.[132]

126. *Rodriguez*, 955 N.E.2d, at 888.
127. *Id*.
128. *Id*. at 886.
129. *Id*.
130. Adam Levitin, *Nemo Dat Trumps Bona Fide Purchaser*, Credit Slips (Oct. 2011) http://www.creditslips.org/creditslips/2011/10/nemo-dat-trumps-bona-fide -purchaser.html
131. *Id*.
132. Kerri Panchuk, *Buyer of Invalid Foreclosure Loses Appeal to Clear Property Title*, HOUSING WIRE (Oct. 18, 2011).

V. HOW MERS HAS BROKEN OR DILUTED CHAIN OF TITLE FOR BOUNDARY DISPUTES BETWEEN FORECLOSED PROPERTIES AND ALL OF THEIR NEIGHBORS

A. MERS HAS BROKEN OR SEVERELY DILUTED CHAIN OF TITLE

In the midst of buying and selling mortgages between banks and creating mortgage backed securities, MERS was created to shuffle home loans quickly between lenders, leaving homeowners unable to find out who actually owned their mortgage at any given time.[133] In addition to tracking ownership and servicing rights, when closing on home mortgages, mortgage lenders now often list MERS as the "mortgagee of record" on the paper mortgage rather than the real mortgagee.[134] The mortgage is then recorded with the county property recorder's office under MERS, Inc.'s name rather than under the lender's name.[135] Historically, employees of county recording offices kept records of each individual company that recorded mortgage loans and mortgage loan assignments, but not today—today MERS is the only company listed.[136] Currently, it is estimated that MERS holds over half of all mortgages in the United States—approximately 60 million mortgages[137]

In this process, while MERS holds mortgages as the "mortgagee of record" promissory notes are separated and sequentially transferred from community bank to larger bank to investment bank to mortgage backed security without these transfers between banks ever being publically recorded or traceable in the grantor/grantee indexes.[138] Sometimes these transfers are documented in the MERS system (rather than the county property recorder's office) and sometimes they are never documented at all.[139] MERS then initiates foreclosure actions on behalf of lenders.[140] As

133. This lack of knowledge often led to payments made to the wrong bank or lender because the homeowner could not look to publicly recorded deeds to determine the ever changing identity of their lender. Michael Grover, *Fed-led Research Reveals Need For Better Twin Cities Foreclosure Data*, THE FED. RES. BANK OF MINNEAPOLIS (Sept. 2006), http://www.minneapolisfed.org/publications_papers/pub_display.cfm?id=2200.

134. R.K. Arnold, *Yes, There Is Life on MERS*, 11-AUG PROB. & PROP. 32, 32–34 (1997). See also Christopher L. Peterson, *Foreclosure, Subprime Mortgage Lending, and the Mortgage Electronic Registration System*, 78 U. CIN. L. REV. 1359 (2010), for a comprehensive explanation of the MERS process.

135. Peterson, *supra* note 134, at 1361.

136. *Id*. at 1362.

137. Michael Powell & Gretchen Morgenson, *MERS? It May Have Swallowed Your Loan*, N.Y. TIMES, Mar. 6, 2011, at BU1.

138. *See* Marian Wang, *Backgrounder: A Closer Look at MERS, the Industry's Controversial Mortgage Clearinghouse*, PROPUBLICA (Mar. 7, 2011), http://www.propublica.org/blog/item/backgrounder-a-closer-look-at-mers-the-industrys-controversial-mortgage-cle.

139. Wang, *supra* note 138.

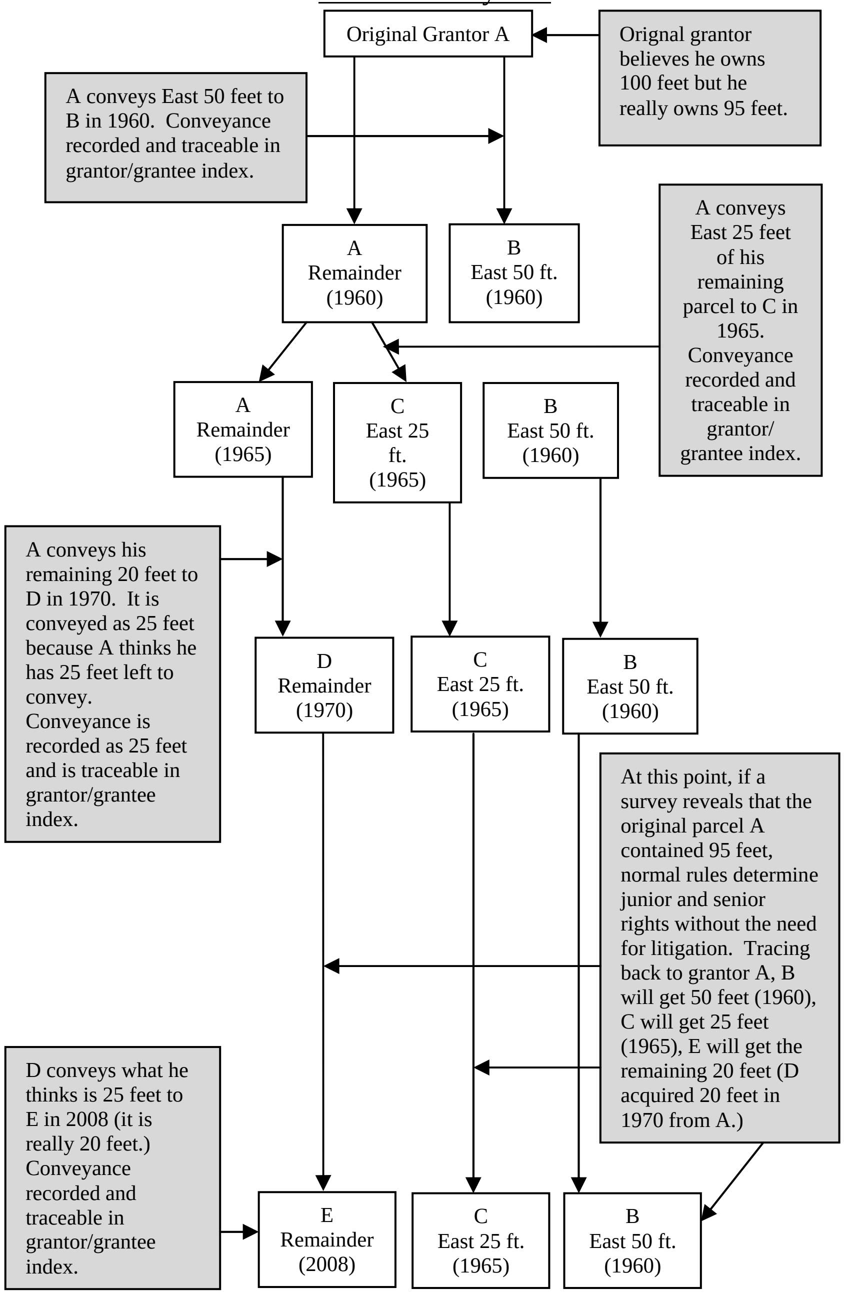
stated above, courts have held that MERS lacks standing to foreclose on a particular property, and many times, the actual owner of the property cannot even be determined because of falsified (robo-signed), backdated or lost/nonexistent records.

This phenomenon also means that the property's chain of title is lost in public records or severely diluted (because it cannot be traced amongst the hundreds of thousands of MERS transactions). If the chain of title is lost for a foreclosed property, any property that shares a common property boundary line with that foreclosed property may have also lost its senior rights in a boundary dispute. Boundary disputes between neighbors are very common; however, they were historically not well publicized. This is simply because these boundary disputes were previously resolved by searching chain of title records and dividing property according to the principles listed above. Now that chain-of-title is destroyed/severely diluted, these same boundary disputes will require court intervention to set boundary lines. Additionally, because of clouded titles, both foreclosed property owners and their neighbors may not be able to sell their properties because buyers will not be able to obtain title insurance (or provide the same warranty deed issued by a lender) and consequently, buyers will not be able to obtain financing.

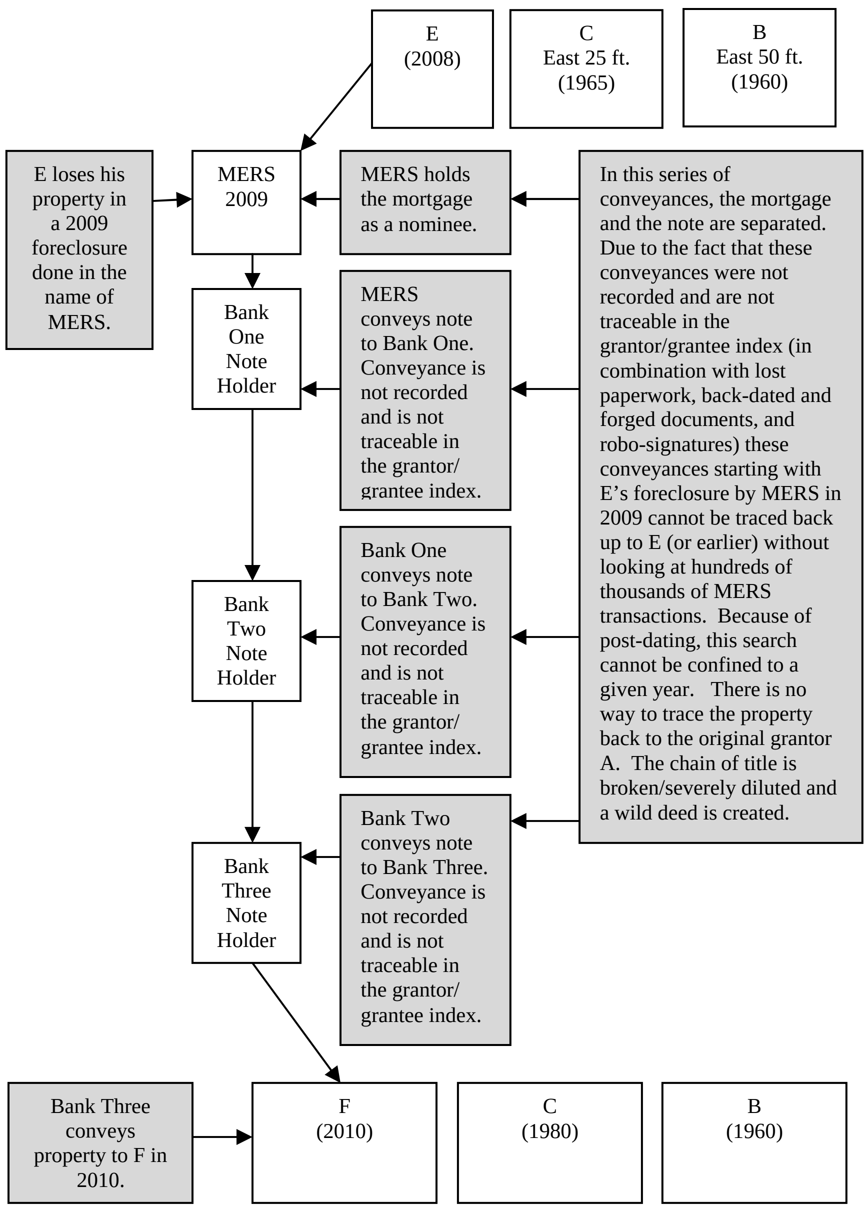
As an example of these principles, see Diagram B on the next two pages.

140. Robbie Whelan, *Lawmaker Questions Power to Foreclose*, WALL ST. J., (Nov. 1, 2010), http://online.wsj.com/article/SB10001424052748704865104575588791583567372.html.

Diagram B
MERS Conveyance



NOW THE PROBLEM STARTS
MERS Conveyance



Bank three (note holder) conveys the foreclosed property to F in 2010.

There are several problems with this conveyance:

First Set of Problems:

1. Bank Three cannot prove it actually owns title to the property because the note and the mortgage were separated in 2009 (MERS held the mortgage and the note was assigned to Bank One, Bank Two, and Bank Three in a series of transactions and none of the transactions were recorded.) This is a wild deed.

a. Because Bank Three cannot prove they own title to the property to convey to F, F cannot obtain title insurance on the property unless Bank Three agrees to indemnify F (or provide a warranty deed) against any title claims or losses as part of F's title insurance policy.

b. Similarly, F cannot prove that he owns title to the property (clouded title/wild deed); therefore, F will have a problem selling the property because:

(1) Realistically, F will not be able to indemnify a prospective buyer against any title claims or losses (as Bank Three had done for F);

(2) A prospective buyer will not be able to obtain title insurance because the property's title is clouded and the property has a wild deed. Without title insurance or a redeemable warranty deed, a prospective buyer cannot obtain financing (leaving only cash buyers);

(3) A clouded title/wild deed will diminish the market value of the property when F tries to sell the property even if he can find a cash buyer.

Second Set of Problems:

2. When F purchased the property in 2010, Bank Three believed that it was conveying twenty-five feet to F. F also believed that he was purchasing twenty-five feet. F had a survey done in 2010 to determine boundaries. In conducting the survey, the surveyor found:

a. The original grantor A (traced back from B and C properties) only had a total of ninety-five feet to convey due to a prior survey discrepancy.

b. The surveyor must determine the senior rights between F, C, and B in order to determine who gets what portion of the ninety-five feet (senior and junior rights); however, this cannot be determined because:

(1) F thinks he owns twenty-five feet, C thinks he owns twenty-five feet, and B thinks he owns fifty feet.

(2) The surveyor cannot trace F's property back to E due to the MERS transactions, so you cannot determine whose conveyance came first in time (thus senior by race/notice statutes)—F, B, or C.

(3) Therefore, the surveyor cannot determine who has senior and who has junior rights between F, B, and C.

c. All three properties (F, B, and C) now have unclear boundary lines creating a cloud on all three properties' titles.

(1) F, B, and C will have to disclose the boundary discrepancy when they attempt to sell their properties.

(2) The boundary discrepancy will create a cloud on title for all three properties, diminishing the properties' values.

(3) The cloud on title will make it impossible for prospective buyers to obtain title insurance (and financing) on any of the three properties.

d. Because of the broken/diluted chain of title and the boundary discrepancy, F, B, and C will have to go to court to have their boundary lines adjudicated (even if they agree to a compromise) because a surveyor cannot make this determination absent a court order. This process is expensive and time consuming, holding up land sales, disposition of estates and family trust, and negatively affecting the American economy.

B. A Purchaser May Not Be Able to Obtain Title Insurance on a Foreclosed Property Processed through MERS

Title insurance "involves the issuance of an insurance policy promising that, if the state of the title is other than as represented on the face of the policy, and if the insured suffers loss as a result of the difference, the insurer will reimburse the insured for that loss and any related legal expenses, up to the face amount of the policy."[141] When a title insurance policy represents that a title search was made, it impliedly represents that the defects, impediments and other matters mentioned in the policy and excluded from coverage are the only ones disclosed by a search of public records (or disclosed on a new proper survey commissioned at the time the policy is issued). To the average person who has paid for a title search made in connection with a policy of title insurance, the policy itself serves as the abstract of title.[142] The GAO 07-401 reported on the nefarious loss and loss adjustment claims of title insurance premiums.[143] The concept of title insurance is largely not understood by the average homeowner. Title insurers pay few claims (usually high dollars) with only five percent of the premiums paid as losses/ loss adjustments (2005).[144]

MERS has broken or severely diluted the chain of title for foreclosed properties (see Diagram B above) and their neighbors (with sequential conveyances and a boundary discrepancy). Consequently, all of these homeowners will have clouded titles. With clouded titles, subsequent purchasers of any of these properties (foreclosure or neighbor with sequential conveyance and boundary discrepancy) will not be able to obtain title insurance without specific exemptions, and in turn, they will also not be able to obtain financing, leaving only investment purchasers able to pick up properties for cash at a discounted price. These same investors may not be able to resell these properties—except to other investors. In fact, many pundits have attempted to tie unemployment and economic recovery directly to the housing crisis while portraying homeowners as irresponsible for failing to pay their mortgages. What they have failed to acknowledge is that, at the end of the day, the United States has a glut of houses available to very few legitimately qualified buyers. Gone are the days of income stated loans, $0 down payments and giving mortgages to anyone with a pulse. Letting lenders and MERS off the hook without liability after their own strategic defaults and mortgage swaps for pennies on the dollar will not increase the number of qualified buyers. The real question is, who will buy these title-defective houses now?

The inventory of foreclosed properties is being off-loaded to cash paying investors. Many of these investors pay cash allowing them to act quickly without lender involvement. Lenders typically require title insurance as a condition of a real property loan. Investors, paying cash to

141. Lick Mill Creek Apartments v. Chicago Title Ins. Co., 283 Cal. Rptr. 231, 233 (Ct. App. 1991). *See also* CAL. INS. CODE § 12340.1 (West 2011).

142. Banville v. Schmidt, 112 Cal. Rptr. 126, 131–36 (Ct. App. 1974).

143. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-07-401, TITLE INSURANCE: ACTIONS NEEDED TO IMPROVE OVERSIGHT OF THE TITLE INDUSTRY AND BETTER PROTECT CONSUMERS, 41–42 (2007).

144. *Id*.

purchase properties, may forego title insurance. Although these investors are presumed to be bona fide purchasers, they may not hold clear and marketable title or title insurance on the property they purchased. In fact, they may have to litigate.[145] In actuality, this resourceful cash buyer may be stuck with the property purchased. When the investor attempts to resell the property to a subsequent purchaser, they will have a problem. In this scenario, a prudent lender will require additional title insurance endorsements as protection against clouded title issues. Title companies will not offer these endorsements and, when the subsequent purchaser's loan falls apart, the investor will be stuck with the property unless he/she can find another cash buyer or file an expensive and lengthy quiet title action. Also, if the investor attempts to sell the property, he/she faces liability including, but not limited to, contract rescission due to state disclosure statutes.[146] Time will prove that the purchase of many foreclosures (at any price) was a foolish investment. Purchasers should be asking "How good is the warranty (on a warranty deed) issued by a limited liability company liquidating an inventory of housing?" See Section VII below regarding consumer protection tips regarding purchasing foreclosures.

We have already started to see this MERS problem in the context of title insurance become a reality. According to Bloomberg October 20, 2010 "*Fidelity National To Require Banks To Sign Foreclosure Warranty*," because of the problems with MERS, in order for an individual buyer to obtain title insurance on a foreclosed home purchased from a bank, banks were required to provide a written indemnity to the title insurer and buyer stating that the bank actually owns the property and would defend against any subsequent claims on title.[147] At one point in October 2010, Old Republic was reportedly refusing to write title policies for some foreclosures all together[148] (although this policy was subsequently changed and the indemnification requirement was relaxed).[149] Why? Because if one

145. *See* Bevilacqua v. Rodriguez, 955 N.E.2d 884 (Mass. 2011).

146. *See* Scotch Bonnett Realty Corp. v. Matthews, 417 Md. 570 (2011) (analyzing the differences between a forged deed and a deed obtained by false pretenses in Maryland; a deed obtained through fraud, deceit or trickery is voidable as between the parties thereto, but not as to a bona fide purchaser. A forged deed on the other hand, is void ab initio).

147. Danielle Kucera, *Fidelity National To Require Banks To Sign Foreclosure Warranty*, BLOOMBERG (Oct. 20, 2010), http://www.bloomberg.com/news/2010-10-20/fidelity-national-to-require-banks-to-sign-warranty-for-foreclosure-sales.html.

148. Stephanie Armour, *Old Republic To Stop Writing Policies For Some Foreclosures*, USA TODAY (Oct. 2, 2010), http://www.usatoday.com/money/economy/housing/2010-10-02-old-republic-foreclosures_N.htm.

149. Danielle Kucera, *Fidelity National Drops Plan For Lender Foreclosure Guarantee*, BLOOMBERG (Oct. 27, 2010), http://www.bloomberg.com/news/2010-10-27/fidelity-national-drops-plan-for-lender-foreclosure-guarantee.html.

of the four major title companies required indemnity or refused to insure foreclosures altogether, this would be the demise of the title industry. The problems with boundary disputes will soon follow.

The only thing holding the title companies together is a piece of duct tape and a stick of gum. Currently, title companies are being hit with large claims due to the loss of priority of liens and loans (another form of junior and senior rights).

As shown in Diagram B above:

- A bank cannot prove that it actually owns the foreclosed property because the note and the mortgage are separated creating a wild deed.

- As a result, a first subsequent buyer of the foreclosed property may not be able to obtain title insurance unless the bank agrees to indemnify this first subsequent buyer against any title claims or losses as part of the first subsequent buyer's title insurance policy.

- Even if the bank and the title insurer work together to provide title insurance to this first subsequent buyer for the foreclosed property, when this first subsequent buyer goes to re-sell the foreclosed property to a second subsequent buyer, the first subsequent buyer will have a clouded title and wild deed and the second subsequent buyer will not be able to obtain title insurance and financing without indemnity from the first subsequent buyer (which in all likelihood this buyer cannot provide).

- If there is a boundary dispute and land shortage as a result of sequential conveyances between the first subsequent buyer and his/her neighbors and the parties cannot trace the conveyances back to the original grantor to determine junior and senior rights because MERS has destroyed or severely diluted chain of title records, this first subsequent buyer's neighbors will also have unclear boundaries, clouded titles that must be disclosed and these neighbors will not be able to sell their properties to buyers requiring title insurance to obtain financing.

- This first subsequent buyer's property and all of this party's neighbors' properties will be diminished in value because of the clouded titles on their properties.

C. The Torrens System—An Alternative?

The only known alternative to the chain of title system is the Torrens system which registers the owner, not the land.[150] Minnesota and Massachusetts (via the Massachusetts Land Court system) have established Torrens systems, as well as cities such as Chicago and San Francisco, where fire destroyed the land title records.[151]

To institute a Torrens system, you must have a court finding that eliminates the necessity for a chain of title and a declaration of the property location.[152] Under the Torrens system, the owner's certificate of title defeats any competing claims not declared at the initial proceedings.[153] Furthermore, a Torrens system would require a survey and court costs for each individual property. Conceivably, if done properly, a Torrens system would take hundreds of years to create—not exactly a feasible solution. Additionally, once established, each state must guarantee rights of ownership and establish a fund to pay the costs for errors in court determined ownership. Although a Torrens system would, in essence, eliminate the need for title insurance, it would be too expensive and take too long to implement. As it stands, there is simply no reasonable alternative to maintaining our chain of title system—a system that MERS has frustrated.

VI. CONCLUSION

Recently, there have been calls to create a national system/standard for originating, selling and servicing mortgage loans.[154] The MERS system is an example of a flawed national system that did not take into account the fact that each state determines its own real property laws and recording system. A nationalized system simply will not work. Land ownership is local. Each state has its own laws governing the real property and the laws applicable to one state cannot work in another state.

Kurt Pfotenhauer, chief executive of the American Land Title Association, said MERS is an "elegant solution" to the inefficiencies of

150. Curtis M. Brown, Walter G. Robillard & Donald A. Wilson, Brown's Boundary Control and Legal Principles, 52–53 (6th ed. 2009).

151. *Id*. at 53.

152. *Id*.

153. *Id*.

154. Christopher Whalen, *The Ibanez Decision: What It Means For Homeowners and Investors*, Reuters (Jan. 10, 2011) (referencing *An Open Letter To U.S. Regulators Regarding National Loan Servicing Standards* (Dec. 21, 2010)), http://blogs.reuters.com/christopher-whalen/2011/01/10/the-ibanez-decision-what-it-means-for-home-owners-and-investors.

paperwork.[155] Although he would welcome more regulatory oversight, Pfotenhauer said title companies have found the database to be accurate and that its main flaw is that it doesn't contain every mortgage in America. This is a remarkable statement from a title insurance industry representative. The idea may be to apply the golden rule—he with all the gold rules. If MERS controlled all mortgages, maybe MERS would be deemed too big to fail (like AIG). However, land title is not about securities. It just so happened that mortgage backed securities were formed as a market gamble. Investors may have gambled and lost, however, MERS cannot be allowed to ruin land title as a result of this securitization.

MERS, a shell company with forty-five employees and 20,000 Vice Presidents (paying $25.00 each for the right to use the MERS name), may destroy our land title records affecting all American homeowners (not just those unfortunate enough to face foreclosure) if appropriate actions are not taken. Chain of title destruction boils down to the destruction of a basic American right—land ownership with a verifiable clear title. If states are forced to accept a new system, Americans will lose the legal theories that establish and protect real property rights including marketable title, prescriptive rights, acquiescence, equitable estoppels, adverse possession and others. Think about the following:

- Do we really want to force Americans to litigate their property rights that were documented and maintained for nearly 400 years until the introduction of MERS?

- If these conclusions are incorrect, why did the title insurance industry threaten to refuse to insure foreclosures in October 2010?[156]

- What is the indemnity relationship between lenders and title insurers today (keeping in mind land title insurance covered risk usually includes fraud or forgery in the execution of documents in the

155. Ariana Eunjung Cha, Steven Mufson, *How The Mortgage Clearinghouse MERS Became A Villain In the Foreclosure Mess*, WASHINGTON POST (Dec. 30, 2010), http://www.washingtonpost.com/wp-dyn/content/article/2010/12/30/AR2010123003056.html.

156. David Streitfeld, *Company Stops Insuring Title In Chase Foreclosures*, N.Y. TIMES (Oct. 2, 2010). In April 2011, the Michigan Court of Appeals held that MERS was ineligible to use Michigan's nonjudicial foreclosure process because MERS did not meet foreclosure by advertisement requirements and MERS should have filed the foreclosures through Michigan's judicial foreclosure process. Austin Kilgore, *MERS Ruling Forces HUD to Reforeclose on Mich. REO*, National Mortgage News (May 27, 2011). Most major title insurance company underwriters had ceased issuing title insurance to any properties where MERS closed by advertisement. Consequently, Michigan REO properties in HUD's inventory that cannot close due to the inability to obtain title insurance, must be re-foreclosed. *Id.*

chain of title (deeds, mortgages, mortgage satisfaction pieces, etc.)?[157]

On October 13, 2010, the American Land Title Association (ALTA) indicated that title insurers are looking to lenders to provide appropriate indemnities.[158] In fact:

> ALTA drafted a model indemnity agreement with Fannie and Freddie that acknowledged the insurer's obligation to defend its policyholders in the event of a court challenge to the property's title, and required the servicer to reimburse the title insurer for any cost of defending the title of the purchaser of an REO property.[159]

Title insurers are aware of the problems and are presumably paying claims for loss of priority (subordination).

Fast forward, first time buyers purchase their first home with the "title insurance indemnification from lenders" policy. The title is not repaired, there may or may not be bona fide purchaser rights which may or may not be trumped by nemo dat theories. The first time buyers offer to sell the home; can they indemnify the title insurance company for the subsequent purchaser?

VII. CONSUMER PROTECTION TIPS

Although foreclosed properties may appear to be a "bargain," no American (from the sophisticated investor to the layperson buying a home for their family to reside) should purchase a foreclosed property owned by a bank or servicer without first taking the following actions with the advice, counsel and assistance of a licensed attorney in your state well versed in real property laws and litigation, boundary disputes, title insurance, financing and contract law:

1. Do not pay cash for a foreclosure, even if you have cash available.

2. Do not rely on the "warranty" provided by an LLC or an individual seller unless they provide indemnity in the form of collateral or a security interest separate from the deed and of value equal to or greater than the purchase price of the subject property.

3. Obtain an "Owner's Policy" from a reputable title insurer in addition to and separate from a "Lender's Policy."[160] The Owner's Policy

157. House Financial Services Subcommittee on Housing and Community Opportunity, Testimony of Anne Anastasi (President of the American Land Title Association) on Behalf of the Amercian Land Title Association, *Robo-Signing, Chain of Title, Loss Mitigation, and Other Issues in Mortgage Servicing* (Nov. 18, 2010).

158. *Id*. at 13.

159. *Id*.

160. Lenders routinely negotiate "ALTA Endorsements" to title policies. Title insurers want this

should contain specific endorsements and should protect the buyer against liens on the subject property. Consult a knowledgeable attorney for the requisite language and endorsements that must be contained in the Owner's Policy.

4. Do not buy a foreclosure with a sequential conveyance without obtaining a chain of title on the property to be purchased (and on all adjacent parcels as these may have also been prior foreclosures). If the chain of title cannot be made available, there may be a problem.[161]

5. Retain a qualified attorney to render a written opinion as to the status of title to the foreclosed property, title insurance coverage and any exceptions to title insurance coverage.

6. Verify that the attorney you retain has proper errors and omissions (malpractice) insurance coverage that exceeds the value of the property you are considering purchasing.

7. As an innocent purchaser, know the difference between a deed obtained by fraud and a deed that has been forged. If a deed is forged, it cannot pass good title. If a deed is procured by fraud, then it can pass good title to a bona fide purchaser without notice.[162] However, to realize the property rights may require expensive litigation and a quiet title action may have a period of time (oftentimes years) to take effect.

The bottom line is that if two properties have equal appeal and all other factors being equal between purchasing a foreclosure versus a non-foreclosure, it may be preferable to purchase a non-foreclosure unless you are willing to perform the necessary and substantial due diligence on the foreclosed property with the assistance of a qualified attorney.

VIII. EPILOGUE

Prior to this article's publication, several events occurred, including:

1. An audit by San Francisco county officials of approximately four hundred recent foreclosures revealed almost all had either legal violations or suspicious documentation—eighty-four percent of the files contained apparent clear violations of law and two-thirds had at least four violations or irregularities.[163] This audit examined files between January 2009 to

additional insurance to protect their investment from adverse title claims. Oftentimes, title insurers will spend thousands of dollars on due diligence before lending on large real property loans.

161. Bevilacqua v. Rodriguez, 955 N.E.2d 884, 918 (Mass. 2011). Nemo dat trumps bona fide purchaser rights. Adam Levitin, *Nemo Dat Trumps Bona Fide Purchaser*, Credit Slips (Oct. 2011), http://www.creditslips.org/creditslips/2011/10/nemo-dat-trumps-bona-fide -purchaser.html

162. *See* Scotch Bonnett Reealty Corp. v. Matthews, 417 Md. 50, 570 (Bankr. D. Md. 2011).

163. Gretchen Morgenson, *Audit Uncovers Extensive Flaws in Foreclosures*, N.Y. TIMES (Feb. 15, 2012).

November 2011.[164]

> Banks involved in buying and selling foreclosed properties appear to be aware of potential problems if gaps in the chain of title cloud a subsequent buyer's ownership of the home. Lou Pizante, a partner at Aequitas who worked on the audit, pointed to documents that banks now require buyers to sign holding the institution harmless if questions arise about the validity of the foreclosure sale.[165]

Subsequently, Democratic Leader Nancy Pelosi and Congresswoman Jackie Speier sent a letter to Attorney General Eric Holder asking him to involve the Justice Department's Financial Fraud Enforcement Task Force to examine whether any violations of Federal law occurred in San Francisco.[166]

Furthermore, the MERS servicer identification system often does not produce any information on the beneficial ownership of loans.[167] Instead, it states: "Investor: This investor has chosen not to display their information. For assistance, please contact the servicer."[168] Does this ambiguous sentence mean (1) MERS does not know who owns the loan (meaning that we no longer have a record keeping system to track legally recognized ownership interests in land back to a root of title) or (2) the owner of the loan actually refused to be identified (meaning that the MERS system has abated an important legal incentive to provide public notice of land ownership interests)?[169]

2. New York Attorney General Eric Schneiderman filed a civil suit against various units of JP Morgan Chase, Bank of America, Wells Fargo, MERSCORP and MERS over the use of MERS in foreclosures.[170] The suit alleges that the creation and use of MERS has resulted in a wide range of deceptive and fraudulent foreclosure filings in New York State and the federal courts, including the use of robo-signers who failed to review the underlying records as required and served to disguise gaps in chain of

164. Morgenson, *supra* note 163

165. *Id*.

166. Press Release, *Pelosi, Speier Request Justice Department Examination into Possible Violations of Federal Law in San Francisco Foreclosures* (Feb. 17, 2012), http://www.democraticleader.gov/news/press?id=2496

167. United States House of Representatives Committee on the Judiciary, written Testimony of Christopher L. Peterson, *Foreclosed Justice: Causes and Effects of the Foreclosure Crisis* (Dec. 2, 2010).

168. *Id*.

169. *Id*. (also stating "We must recognize that our heritage of legal certainty in property rights created by the interaction of public recording systems and land title statutes is an important national economic resource that has been depleted by the MERS system").

170. Yves Smith, *Schneiderman Files Civil Fraud Lawsuit Against Three Major Banks for Use of MERS*, Naked Capitalism (Feb. 23, 2012). See also Press Release: *A.G. Schneiderman Announces Major Lawsuit Against Nation's Largest Banks For Deceptive & Fraudulent Use of Electronic Mortgage Registry* (Feb. 3, 2012) http://www.ag.ny.gov/media center/2012/feb/feb03a 12.html.

title.[171] The complaint alleges that the practices outlined harmed homeowners and undermined the integrity of the judicial foreclosure process.[172] The lawsuit alleges that employees and agents of various financial institutions named, acting as "MERS certifying officers" have repeatedly submitted court documents containing false and misleading information that made it appear that the foreclosing bank had authority to do so when it actually did not have this authority.[173]

This lawsuit further alleges that MERS has effectively eliminated homeowner's and the public's ability to track property transfers through the traditional public records system and asserts that this information is now stored only in a private database plagued with inaccuracies and errors over which MERS and its financial institution members have sole control.[174]

3. After lengthy negotiations and prior opting out by many state attorneys' general, it appears that lenders and the attorneys' general will come to an agreement for partial settlement on foreclosure practices in the amount of $26 billion.[175] The settlement had been previously held up by concerns of New York Attorney General Eric Schneiderman that the terms provided too broad of a release for banks for past misdeeds and would make future investigations difficult; however, Schneiderman was able to win concessions on this point.[176] Releases are expected to be limited to the foreclosure process and prosecutors and regulators will still have the right to investigate other possible violations such as the assembly of risky mortgages into securities that were sold to investors and then went bad along with insurance and tax fraud.[177] Officials will be able to pursue any allegations of criminal activity.[178] Furthermore, Schneiderman's lawsuit against MERS will be allowed to go forward.[179] Fannie Mae and Freddie Mac (who combined own about half of U.S. mortgages) will not be covered by any Attorney General settlement.[180]

171. Smith, *supra* note 178. *See also* Complaint filed in Supreme Court of the State of New York, Kings County entitled *The People of the State of New York, by Eric T. Schneiderman v. JP Morgan Chase Bank N.A, et al*. (Feb. 3, 2012).

172. *Id*.

173. *Id*.

174. *Id*.

175. Dawn Kopecki and David McLaughlin, *Foreclosure Accord Said to Ensure Same Terms for All 50 States*, BUSINESSWEEK (Feb. 14, 2012) http://www.businessweek.com/news/2012-02 14/foreclosure- accord-said-to- ensure-terms-for-all-50-states.html; See also Nelson D. Schwartz and Shaila Dewan, *States Negotiate $26 Billion Agreement for Homeowners*, N.Y. TIMES (Feb. 8, 2012), http://nytimes.com/2012/02/09/business/states-negotiate-25-billion-deal-forhomeowners.html?pagewanted=all.

176. Schwartz and Dewan, *supra* note 175.

177. *Id.*

178. *Id*.

179. *Id*.

180. Schwartz and Dewan, *supra* note 175.

By allowing Fannie Mae, Freddie Mac and Ginnie Mae to purchase MERS-recorded loans, the federal government has inadvertently undermined sensible state consumer protection and land title laws/records.[181] MERS now faces uncertain legal costs and, going forward, Congress should bar Government Sponsored Enterprises ("GSEs") from becoming more deeply involved with MERS.[182] Furthermore, Congress should not intervene in state's property laws with a MERS "whitewash" bill over the basic legal problems associated with MERS, as such a bill is likely to have unforeseeable and unintended consequences on state laws.[183]

181. United States House of Representatives Committee on the Judiciary, written Testimony of Christopher L. Peterson, *Foreclosed Justice: Causes and Effects of the Foreclosure Crisis* (Dec. 2, 2010).
182. *Id*.
183. *Id*.

* * *