TWO FACES: DEMYSTIFYING THE MORTGAGE ELECTRONIC REGISTRATION SYSTEM'S LAND TITLE THEORY

Christopher L. Peterson[*]

TABLE OF CONTENTS

I. THE EVOLVING LEGAL FOUNDATION OF MERS
II. GATHERING STORM CLOUDS OF TITLE
III. MORTGAGES WITHOUT MORTGAGEES: MERS AND THE PROBLEM OF CONVEYANCE
IV. WHAT ABOUT THE MONEY? THE RIGHT OF COUNTIES TO RECOVER UNPAID RECORDING FEES
V. REBUILDING A TRUSTWORTHY REAL PROPERTY RECORDING SYSTEM
VI. CONCLUSION

INTRODUCTION

In Roman mythology, the god Janus, for whom each year's first month is named, was the deity of beginnings and endings.[1] According to legend, the titan Saturn gave the two-faced God the power to see both the future and the past. Romans carved both of Janus' two faces on gates and doorways to solemnize momentous transition.[2] Most notably, in the Roman forum the Senate erected the ritual gates called the *Janus Geminus* which the Romans opened in times of conflict.[3] At war's outset Priests made sacrificed here to curry favor from the gods and forecast the prospects of success.[4] No deity could better symbolize what financiers hoped to create when they founded the Mortgage Electronic Registration System—known as MERS. MERS sits as a dichotomous, enigmatic gatekeeper on the vestibule of our nation's complex and turbulent mortgage finance industry. Financiers invoked MERS' name at the beginning of millions of subprime and

[*] Associate Dean for Academic Affairs and Professor of Law, University of Utah, S.J. Quinney College of Law. The author wishes to thank the following for helpful conversations, comments, encouragement, research assistance, and/or suggestions: Abraham Bates, Gregory Clark, Thomas Cox, Lynn Drysdale, Max Gardner, Kathleen Keest, Robert Hager, Rebecca Holt, Tera Peterson, Rylee McDermott, Michael Wolf, and Nick Wooten.

[1] MIKE DIXON-KENNEDY, ENCYCLOPEDIA OF GRECO-ROMAN MYTHOLOGY 179 (1998).

[2] *Id.*

[3] Ovid, Fasti 1.89-282, selections.

[4] Dixon-Kennedy, *supra* note 1, at 179.

Electronic copy available at: http://ssrn.com/abstract=1684729

exotic mortgage loan transactions, and again invoke its name as they attempt to terminate so many of these loans through foreclosure. And like Janus, MERS is two-faced: impenetrably claiming to both own mortgages and act as an agent for others that also claim ownership.

This essay examines recent case law developments in an update to an earlier article on the legal problems associated with MERS.[5] In particular, this essay looks at two of the most fundamental unanswered legal questions regarding MERS' role in mortgage lending. Given recent cases questioning MERS' ownership interests in loans registered on its database, do security agreements naming MERS as a mortgagee or deed of trust beneficiary actually succeed in conveying a property interest? Moreover, financial institutions used MERS to avoid paying billions of dollars in recording fees to county and state governments. Should these governments—many of which are facing dire financial crises—be entitled to recoup unpaid recording fees? And perhaps most important, does the fact that such fundamental issues remain live controversies tell us something more about the commercial norms our country needs to rebuild a trustworthy financial system.

This essay begins with a short introduction to MERS' role in the residential mortgage finance including the still evolving legal foundation of the company's business model. Next, Part II explores whether security agreements naming MERS as a mortgagee or deed of trust beneficiary meet traditional common law title conveyance requirements. Then, the Part III explores the financial industry's exposure to county and state government lawsuits seeking to recoup unpaid recording fees. This essay concludes by reflecting on the difficult position facing appellate judges and legislators that will be called upon to resolve these controversies, as well as investors contemplating the purchase of MERS-recorded mortgages.

I. THE EVOLVING LEGAL FOUNDATION OF MERS

Since the founding of the American republic each county in the United States has maintained records of who owns the land within that county.[6] Most states have tracked changes in ownership of land, including mortgages and deeds of trust, by maintaining records indexed through the names of grantors and grantees.[7] These grantor-grantee indexes allow individuals and businesses contemplating the purchase of land to investigate (or hire a title insurer to investigate) whether a seller or mortgagor actually owns the land they are offering for sale or mortgage. Communities have traditionally elected their county recorders or registers of deed, providing an important democratic check and balance in the preservation of property rights. A public, enduring, authoritative, transparent record of all land ownership provides a vital information infrastructure that has proven indispensible in facilitating not only mortgage finance, but virtually all

---

[5] Christopher L. Peterson, *Foreclosure, Subprime Mortgage Lending, and the Mortgage Electronic Registration System*, 78 U. OF CINCINNATI LAW REVIEW 1359 (2010).
[6] PATTON AND PALOMAR ON LAND TITLES § 4 (3d ed. 2003).
[7] 14 POWELL ON REAL PROPERTY §82.03[2][b].

Electronic copy available at: http://ssrn.com/abstract=1684729

forms of commerce.[8] County real property records are the oldest and hitherto most stable metric t tracking the "American dream" of family homeownership.

To facilitate this service, county recorders charge modest fees on documents they record. While there is considerable variety in amount and in the method of calculating these fees, a charge of about $35.00 for a mortgage is typical. County recorders use these fees to fund their offices as well as to contribute to county and state revenue. Some county's use real property recording fees to fund their courts, legal aid offices, schools, and police departments.

For centuries American mortgage lenders have eagerly recorded their mortgages loans with county recorders because of incentives created by state land title laws. For example, if a mortgagee fails to properly record its mortgage, and then someone subsequently buys or lends against the home, the subsequent purchaser can often take priority over the first mortgagee.[9] Similarly, where a mortgagee assigns a mortgage to an investor, that investor would eagerly record documentation reflecting the assignment to protect herself from the possibility that the original mortgagee would assign the same mortgage to a different investor.[10]

In the mid-1990s mortgage bankers decided they did not want to pay recording fees for assigning mortgages anymore.[11] This decision was driven by securitization—a process of pooling many mortgages into a trust and selling income from the trust to investors on Wall Street. Securitization, also sometimes called structured finance, usually required several successive mortgage assignments to different companies. To avoid paying county recording fees, mortgage bankers formed a plan to create one shell company that would pretend to own all the mortgages in the country—that way, the mortgage bankers would never have to record assignments since the same company would always "own" all the

---

[8] Gary A Jeffress & Lynn C. Holstein, *An International Survey of Real Property Recording Costs and Some Characteristics: A Preliminary Evaluation*, 5 URISA J. 53, 53 (1993) (international survey suggesting recording systems are a "precondition of an efficient land market").

[9] POWELL ON REAL PROPERTY § 82.02[1][a].

[10] *See, e.g.,* Connecticut Mut. Life Ins. Co. v. Talbot, 14 N.E. 586 (Ind. 1887) ("It is settled everywhere that unrecorded assignments of mortgages are void as against subsequent purchasers, whose interests may be affected thereby, and whose conveyances are duly recorded, provided such assignments are embraced by the recording acts."); Bacon v. Van Schoonhoven, 42 Sickels 446, 1882 WL 12538 (N.Y. 1882) ("The assignments of the . . . mortgage are also conveyances within the act. This is well settled by authority, and such assignments, if not recorded, are void, not merely as against subsequent purchasers of the same mortgage, but also as against subsequent purchasers of the mortgaged premises, whose interests may be affected by such assignments, and whose conveyances are first recorded.")

[11] Phyllis K. Slesinger & Daniel McLaughlin, *Mortgage Electronic Registration System*, 31 ID. L. REV. 805, 810-12 (1995) (describing an Ernst & Young study commissioned by mortgage banker to study how much money they could avoid paying to county governments through the MERS system).

DRAFT

mortgages.[12] They incorporated the shell company in Delaware and called it Mortgage Electronic Registration Systems, Inc.[13]

Even though not a single state legislature or appellate court had authorized this change in the real property recording, investors interested in subprime and exotic mortgage backed securities were still willing to buy mortgages recorded through this new proxy system.[14] Because the new system cut out payment of county recording fees it was significantly cheaper for intermediary mortgage companies and the investment banks that packaged mortgage securities. Acting on the impulse to maximize profits by avoiding payment of fees to county governments much of the national residential mortgage market shifted to the new proxy recording system in only a few years. Now about 60% of the nation's residential mortgages are recorded in the name of MERS, Inc. rather than the bank, trust, or company that actually has a meaningful economic interest in the repayment of the debt.[15] For the first time in the nation's history, there is no longer an authoritative, public record of who owns land in each county.

MERSCORP, Inc., a company closely affiliated with MERS, Inc., now maintains an electronic database that tracks mortgage servicing rights—the right of a company to collect monthly payments on behalf of the actual economic owner or owners of a loan. Instead of paying county governments, financial institutions pay MERSCORP membership fees and per transaction fees for access to the MERS database and to compensate MERS, Inc. for pretending to own the mortgages these financial institutions register on the MERSCORP database.[16] Sometimes MERSCORP also tracks ownership rights—that is actual assignments—but only if

---

[12] Peterson, *Foreclosure, supra* note 5, at 1368-73; Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997.

[13] Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997; Carson Mullen, *MERS: Tracking Loans Electronically,* MORTGAGE BANKING, May 31, 2000, 62.

[14] Peterson, *Foreclosure supra* note 5, at 1368-73. At least one state, Minnesota, later explicitly authorized MERS recording by amending its recording act to expressly permit nominees to record "[a]n assignment, satisfaction, release, or power of attorney to foreclose." Act of Apr. 6, 2004, ch. 153, § 2, 2004 Minn. Laws 76, 76-77 (codified at Minn.Stat. § 507.413 (2008)). *See generally* Jackson v. Mortgage Electronic Registration Systems, Inc., 770 N.W.2d 487 (Minn. 2009) (interpreting this statute). However, this legal change was not enacted until long after financial institutions had already been using the MERS system in that state. Similar changes have not been enacted nationwide.

[15] Kate Berry, *Foreclosures Turn Up Heat on MERS*, AM. BANKER, July 10, 2007, at 1.

[16] Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997. Unlike mortgage loan servicers which are compensated for foreclosure services, MERS does not receive any compensation for assisting in foreclosures. Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 88 (hereinafter: Arnold Deposition).

investors willingly volunteer this information. [17] Financial institutions have been cavalier about informing MERSCORP of changes in servicing and ownership rights of mortgages because they believe there are no legal penalties for neglecting to make this information available.

MERS's rights vis-à-vis mortgages registered on the MERSCORP database have created a conundrum for courts, borrowers, and foreclosure attorneys. In boilerplate security agreements included in mortgages and deeds of trust around the country, lenders include this clause:

> "MERS" is Mortgage Electronic Registration Systems, Inc. MERS is a separate corporation that is *acting solely as nominee for Lender* and Lender's successors and assigns. *MERS is the mortgagee* under this Security Instrument. MERS is organized and existing under the laws of Delaware, and has an address and telephone number of P.O. Box 2026, Flint, MI 48501-2026, tel. (888) 679-MERS.[18]

This passage, and a similar passage naming MERS the beneficiary in deeds of trust, is confusing to courts, borrowers, and even foreclosure attorneys. On the one hand, MERS purports to be acting as a nominee—a form of an agent. On the other hand, it also is claiming to be an actual mortgagee, which is to say an owner of the real property right to foreclose upon the security interest. It is axiomatic that a company cannot be both an agent and a principal with respect to the same right.[19] In litigation all across the country, attorneys representing MERS frequently take inconsistent positions on the legal status of the company, depending on the legal issue at hand.

Both the MERS-as-an-agent and the MERS-as-an-actual mortgagee theories have significant legal problems. If MERS is merely an agent of the actual lender, it is extremely unclear that it has the authority to list itself as a mortgagee or deed of trust beneficiary under state land title recording acts. These statutes do not have provisions authorizing financial institutions to use the name of a shell company, nominee, or some other form of an agent instead of the actual owner of the interest in the land. After all the point of these statutes is to provide a transparent, reliable, record of actual—as opposed to nominal—land ownership. Conversely, if MERS is actually a mortgagee, then while it may have authority to record mortgages in its own name, both MERS and financial institutions investing in MERS-recorded mortgages run afoul of longstanding precedent on the inseparability of promissory notes and mortgages. Since the 19th century a long and still vital line of cases has held that mortgages and deeds of trust may not be separated from the promissory notes that create the underlying obligation triggering foreclosure rights.[20] These cases do not merely hold that mortgages

---

[17] Financial institutions have not reliably updated the MERS maintained database when they assign loans to businesses that are not members of the MERS system. *See* In re Hawkins, 2009 WL 901766, at n.35 (B.D.Nev).

[18] Mortgage Electronic Registration Systems, Inc. v. Bluming, No. GD05-16795, Civil Division, Court of Common Pleas of Allegheny County, PA, slip op. (May 31, 2006) (J. Timothy Patrick O'Reilly).

[19] Restatement (Third) of Agency Law §§1.01, 1.02.

[20] *In* re Bird, 2007 WL 2684265, at ¶¶ 2-4 (Bkrtcy.D.MD. 2007) ("The note and mortgage are inseparable; the former as essential, the latter as an incident. An

follow notes as a matter of default law, but that mortgages cannot legally be separated from notes. Thus, in Carpenter v. Longan the United States Supreme

---

assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity. . . . It is equally absurd to assume that such bifurcation was intended because such a bifurcation of the note from the deed of trust would render the debt unsecured.”); *In re Leisure Time Sports, Inc.* 194 B.R. 859, 861 (9th Cir.1996) (stating that “[a] security interest cannot exist, much less be transferred, independent from the obligation which it secures” and that, “[i]f the debt is not transferred, neither is the security interest”); In re BNT Terminals, Inc., 125 B.R. 963 (Bankr. N.D. Ill. 1990) (“An assignment of a mortgage without a transfer of the underlying note is a nullity. . . . It is axiomatic that any attempt to assign the mortgage without transfer of the debt will not pass the mortgagee's interest to the assignee.”); Yoi-Lee Realty Corp. v. 177th Street Realty Associates, 208 A.D.2d 185, 626 N.Y.S.2d 61, 64 (N.Y.A.D. 1 Dept.,1995) (“The mortgage note is inseparable from the mortgage, to which the note expressly refers, and from which the note incorporates provisions for default.”); In re AMSCO, Inc., 26 B.R. 358, 361 (Bkrtcy. Conn., 1982) (reaffirming that “[t]he note and mortgage are inseparable”); Barton v. Perryman, 577 S.W.2d 596, 600 (Ark., 1979) (“[A] note and mortgage are inseparable.”); Trane Co. v. Wortham, 428 S.W.2d 417, 419 (Tex. Civ. App. 1968) (“The note and mortgage are inseparable. . . .”); Kirby Lumber Corp. v. Williams, 230 F.2d 330, 333 (5th Cir. 1956) (“The rule is fully recognized in this state that a mortgage to secure a negotiable promissory note is merely an incident to the debt, and passes by assignment or transfer of the note. * * * The note and mortgage are inseparable. . . .”); *Kelley v. Upshaw,* 39 Cal.2d 179, 192, 246 P.2d 23 (1952) (“In any event, Kelley's purported assignment of the mortgage without an assignment of the debt which is secured was a legal nullity.”); Hill v. Favour, 52 Ariz. 561, 84 P.2d 575 (Ariz. 1938) (“The note and mortgage are inseparable; the former as essential, the latter as an incident.)”; Denniston v. C.I.R., 37 B.T.A. 834, 1938 WL 373 (B.T.A. 1938) (“All the authorities agree that the debt is the principal thing and the mortgage an accessory. . . The mortgage can have no separate existence.”); West v. First Baptist Church of Taft, 123 Tex. 388, 71 S.W.2d 1090, 1098 (Tex. 1934) (“The trial court's finding and conclusion ignore the settled principle that a mortgage securing a negotiable note is but an incident to the note and partakes of its negotiable character. . . . The note and mortgage are inseparable; the former as essential, the latter as an incident.”) (citations omitted); First Nat. Bank v. Vagg, 65 Mont. 34, 212 P. 509, 511 (Mont. 1922) (“A mortgage, as distinct from the debt it secures, is not a thing of value nor a fit subject of transfer; hence an assignment of the mortgage alone, without the debt, is nugatory, and confers no rights whatever upon the assignee. The note and mortgage are inseparable; the former as essential, the latter as an incident. An assignment of the note carries the mortgage with it, while the assignment of the latter alone is a nullity. The mortgage can have no separate existence.”) (citations omitted); Southerin v. Mendum, 5 N.H. 420, 1831 WL 1104, at ¶ 7 (N.H. 1831) (“[T]he interest of the mortgagee is not in fact real estate, but a personal chattel, a mere security for the debt, an interest in the land inseparable from the debt, an incident to the debt, which cannot be detached from its principal.”).

DRAFT

Court announced the classic statement of this rule: "the note and mortgage are *inseparable*…, the assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity."[21]

As a practical matter, the incoherence of MERS' legal position is exacerbated by a corporate structure that is so unorthodox as to arguably be considered fraudulent. Because MERSCORP is a company of relatively modest size, it does not have the personnel to deal with legal problems created by its purported ownership of millions of home mortgages. To accommodate the massive amount of paperwork and litigation involved with its business model, MERSCORP simply farms out the MERS, Inc. identity to employees of mortgage servicers, originators, debt collectors, and foreclosure law firms.[22] Instead, MERS invites financial companies to enter names of their own employees into a MERS webpage which then automatically regurgitates boilerplate "corporate resolutions" that purport to name the employees of other companies as "certifying officers" of MERS.[23] These certifying officers also take job titles from MERS stylizing themselves as either assistant secretaries or vice presidents of the MERS, rather than the company that actually employs them. These employees of the servicers, debt collectors, and law firms sign documents pretending to be vice presidents or assistant secretaries of MERS, Inc. even though neither MERSCORP, Inc. nor MERS, Inc. pays any compensation or provides benefits to them. Astonishingly, MERS "vice presidents" are simply paralegals, customer service representatives, and foreclosure attorneys employed by other companies. MERS even sells its corporate seal to non-employees on its internet web page for $25.00 each.[24] Ironically, MERS, Inc.—a company that pretends to own 60% of the nation's residential mortgages—does not have any of its own employees but still purports to have "thousands" of assistant secretaries and vice presidents.[25] This corporate structure leads to inconsistent positions, conflicts of interest, and confusion.[26]

---

[21] Carpenter v. Longan, 83 U.S. 271, 274, (1872) (emphasis added).

[22] Arnold Deposition at 196-98; Mortgage Electronic Registration System, Inc., MERS Law Seminar for USFN Conference, 15-16 (April 21, 2002) (document on file with author) (providing a sample certifying officer resolution).

[23] MERS, Corporate Resolution Request Form, www.mersinc.org/MersProducts/forms/crrf/crrf.aspx (last viewed: April 6, 2009).

[24] *Id.*

[25] MERS does not appear to publically share the total number of individuals that pretend to act as MERS vice presidents and assistant secretaries. However, in a recent deposition MERSCORP's president testified:

> Q. [D]o you know what the total number of certifying officers are as of today? . . .
> A. MERS knows.
> Q. Sure. And – but as CEO have you been privy to that information? Have you seen that number?
> A. Oh, I've –I hear that number.
> Q. Yeah. But—and I'm not trying to hold you to anything specific. I'm just trying to get a ballpark. Do you have a ballpark of how many people that is?
> A. Thousands.

DRAFT

As millions of foreclosures have been working their way through the judicial system, appellate courts have finally had some opportunities to analyze MERS based recording. An increasing number of courts have begun taking a dim view of MERS-recorded mortgages and deeds of trust. To date, every state Supreme Court that has looked at the issue has concluded that, despite its boilerplate language, MERS is not a mortgagee or deed of trust beneficiary. For example, In MERS, Inc. v. Southwest Homes of Arkansas,[27] a first position lender named MERS as the beneficiary on its deed of trust. Later the family took out a second mortgage which did not use the MERS system. When the family fell behind on the second mortgage, the subsequent lender's assignee foreclosed without notifying either MERS or the real owner of the first mortgage. When MERS, acting through local counsel attempted to set aside the foreclosure, a unaniomous Supreme Court of Arkansas, with its Chief Justice writing, held that MERS had no property rights with respect to the loan whatsoever.[28] Even though MERS never had service of process, the court allowed the foreclosure to stand because MERS had lost nothing.[29] In the Court's words, "MERS is not the beneficiary, even though it is so designated in the deed of trust."[30]

Similarly, the Kansas Supreme Court has also refused to allow MERS to set aside a first mortgagee's default judgment in a foreclosure action.[31] In its opinion, the Kansas Supreme Court diagnosed MERS' schizophrenic self characterization as a nominee, puzzling:

> What meaning is this court to attach to MERS's designation as nominee for Millennia? The parties appear to have defined the word in much the same way that the blind men of Indian legend described an elephant—their description depended on which part they were touching at any given time.[32]

Arnold Deposition at 196.

[26] *Compare* MERS Forum, FAQ with Sharon Horstkamp, MERS Vice President and Corporate Counsel, www.mersinc.org/forum/viewreplies.aspx?id=13&tid=73 last viewed June 9, 2004 ("Mortgage Electronic Registration systems, Inc. (MERS) gets its authority to assign and/or discharge a mortgage because *MERS is the mortgagee*, and as such holds legal title to the mortgage. … The nominee language does not take away from the fact that *MERS is the mortgagee*.") (emphasis added); *with* Brief in Support of Defendant's Motion to Dismiss at 3, King v. Ocwen, Civil Action No. 07-11359, 2008 WL 2063553 (E.D.Mich, April 14, 2008) (arguing that MERS could not be liable for Fair Debt Collection Practices Act violations because "*HSBC was the mortgagee* for the property. Ocwen is the servicer for the property. [And,] MERS acted solely as the nominee for the original mortgagee of the property") (emphasis added).

[27] Mortgage Elec. Registration System, Inc. v. Southwest Homes of Arkansas, 2009 Ark. 152, 301 S.W.3d 1 (Ark. 2009).

[28] *Id.* at 2. ("Because MERS was at most the mere agent of the lender . . . , it held no property interest and was not a necessary party.").

[29] *Id.* at 4.

[30] *Id.*

[31] Landmark Nat. Bank v. Kesler, 216 P.3d 158,169 (Kan. 2009).

[32] *Id.* at 165-66.

DRAFT

In response to both statutory and constitutional arguments, Kansas followed Arkansas' skepticism regarding whether MERZS actually owns anything: "MERS did not demonstrate, in fact, did not attempt to demonstrate, that it possessed any tangible interest in the mortgage beyond a nominal designation."[33]

While Arkansas and Kansas both involved late efforts by MERS to set aside earlier dispositions, the Supreme Court of Maine reached similar results when MERS itself filed a foreclosure complaint. In MERS, Inc. v. Saunders, MERS filed a foreclosure complaint, but during the pending case, Deutsche Bank attempted to substitute itself into the action instead of MERS.[34] When the trial court awarded summary judgment to Deutsche Bank the family appealed arguing that MERS lacked standing and that this jurisdictional defect could not be cured by substitution of another party during the pending case. The appeal forced the Maine Supreme Court to look at the simple question of whether MERS has standing to bring a foreclosure action on behalf of the real economic loan owner. Despite contrary boilerplate language in the security agreement, the Court flatly rejected MERS' ownership claim stating: "MERS is not a mortgagee… because it has no enforceable right in the debt obligation securing the mortgage."[35] Because MERS lacked standing, the court reversed summary judgment to give the family an opportunity to "appropriately defend the foreclosure action against the real party in interest."[36]

In Missouri, appellate courts have gone a step further in challenging MERS' ownership claims vis-à-vis mortgages tracked on its database. In Bellistri v. Ocwen Loan Servicing,[37] MERS' involvement in the loan effectively led to the stripping of deed of trust lien from the land. In this case, a debtor borrowed money from a mortgage lending company named BNC Mortgage and signed a deed of trust naming MERS as beneficiary of the trust. After the loan closed, no one paid property taxes on the residence for several years.[38] Eventually the local government established a tax lien and sold the property at auction to Bellistri.[39] Bellistri sent notice of the sale to the original mortgage lender, BNC. But—while the facts of the case are silent on this point—BNC probably sold the loan to an investment bank for securitization shortly after origination and had no appetite whatsoever facilitating repayment. Hoping to make his rights clear, Bellistri sued in state court to quiet title on the land he had purchased. Because the debt had still not been repaid Ocwen, a mortgage loan servicing company, attempted to argue that the tax sale did not transfer title to the land from the original debtor to Bellistri. Ocwen produced an assignment of the deed of trust from MERS to Ocwen that had been recorded by an employee of Ocwen pretending to be a Vice President of MERS. The Missouri Court of Appeals treated the recorded

---

[33] *Id.* at 168.
[34] MERS, Inc. v. Saunders, Slip op. 2010 ME 79, at ¶ 1 (August 12, 2010).
[35] *Id.* at ¶ 15.
[36] *Id.* at ¶ 21.
[37] Bellistri v. Ocwen Loan Servicing, LLC, 284 S.W.3d 619 (Mo.App. E.D.,2009).
[38] Normally, property taxes are paid by lenders or their servicing companies out of eschrow accounts drawn from borrowers' monthly payments. It is not clear from the appellate opinion why the taxes were not paid in this case. *Id.* at 621.
[39] *Id.*

DRAFT

assignment as a legal nullity.[40] Unlike many courts which have side stepped the troubling issues behind the purported severance of mortgages and notes in MERS security agreements, the Missouri Court of Appeals attempted to analyze the issue. Looking to the American Law Institute's Third Restatement of Property Law the court stated:

> Typically, the same person holds both the note and the deed of trust. In the event that the note and the deed of trust are split, the note, as a practical matter becomes unsecured. Restatement (Third) of Property (Mortgages) § 5.4. Comment. The practical effect of splitting the deed of trust from the promissory note is to make it impossible for the holder of the note to foreclose, unless the holder of the deed of trust is the agent of the holder of the note. Id. Without the agency relationship, the person holding only the note lacks the power to foreclose in the event of default. The person holding only the deed of trust will never experience default because only the holder of the note is entitled to payment of the underlying obligation. Id. The mortgage loan became ineffectual when the note holder did not also hold the deed of trust.[41]

Ultimately, the Court held that "MERS never held the promissory note, thus its assignment of the deed of trust to Ocwen separate from the note had no force."[42] The Court effectively quieted title in favor of Bellistri, stripping off the lien.

Collectively, these cases in Arkansas, Kansas, Maine, and Missouri, as well as a growing number of trial court decisions in other states, have cracked the edifice of Janus-masked façade of MERS-recorded mortgages and deeds of trust. It is now legally unclear whether financiers will prevail upon courts to grant MERS the power to both own mortgages and represent owners of mortgages at the same time.

II. GATHERING STORM CLOUDS OF TITLE

While cases successfully challenging MERS' status as a mortgagee or deed of trust beneficiary were litigated in the context of standing to foreclose, they also foreshadow tempestuous title disputes. MERS describes itself as "an innovative process that . . . eliminates the need to prepare and record assignments when trading residential and commercial mortgage loans."[43] The phrase, which the company uses both in legal briefs and public relations material, hints that recording assignments was merely some useless, archaic formality. It is far from clear that state appellate courts will agree that MERS does eliminate the need to record assignments. But even if MERS does eliminate the need to record, it most certainly does not eliminate the need for records. The policy justifications behind recording statutes are as germane today as they were hundreds of years ago when the first American colonies began adopting the statutes. Society needs an authoritative,

---

[40] *Id.* at 624.
[41] *Id.* at 623.
[42] *Id.* at 624.
[43] Welcome to MERS, www.mersinc.org (last visited Sept. 17, 2010).

DRAFT

transparent source of information on who owns land in order to protect property rights, encourage commerce, expose fraud, and avoid disputes. Recent case law is beginning to show gathering judicial skepticism regarding the privatized record keeping system that is displacing public county systems.

Apologists for MERS argue that so long as MERS' name is recorded in county records as a lien holder, prospective purchasers will be on notice that they must inquire further before lending against or buying the land. But who exactly are these purchasers to consult? MERS has maintained a toll free phone number where homeowners are allowed to inquire who holds the servicing rights to their mortgage.[44] But, servicers themselves do not always have accurate records of their own. And even if they did, talking to mortgage servicing company customer service representatives is often, whose business incentives are focused on cutting costs, is often unproductive, slow, and unreliable.[45] In recent years mortgage servicing and origination companies have gone in and out of business in cycles recalling the permanence of a strobe light. Even federally insured banks have been collapsing by the hundreds.[46] After seeing loan after loan in her court room with incomplete documentation and incoherent transactional records, Judge Jennifer Bailey, a Circuit Court Judge in Miami recently stated:

> [T]here are 60,000 foreclosures filed last year. Every single one of them— . . . almost every single one of them—represents a situation where the bank's position is constantly shifting and changing because they don't know what the Sam Hill is going on in their files.[47]

That MERS maintains a database of servicing rights simply does not provide a commercially reliable, authoritative source of lien information because servicers, who are in business to make profit through providing financial services, do not have an incentive to maintain permanent, transparent, publically available records of mortgage ownership.

MERS also does not systematically track beneficial ownership rights of the mortgages registered on its system. Recall that MERS only maintains a database which its members can enter information upon if they want to.[48] When the beneficial ownership interest in a loan changes hands, such as through

---

[44] Welcome to MERS for Homeowners, http://www.mersinc.org/homeowners/index.aspx#3 (last visited Sept. 17, 2010) (the current phone number is 888-679-6377).

[45] *See* Kathreine M. Porter, *Misbehavior and Mistake in Bankrutpcy Mortgage Claims,* 87 TEX. L. REV. 121 (2008).

[46] Over 250 banks have failed since 2008. Federal Deposit Insurance Corporation, Failed Banks List, available at: http://www.fdic.gov/bank/individual/failed/banklist.html (Sept. 17, 2010).

[47] HSBC Bank USA, NA as Trustee for Monura Asset Acceptance Corporation, Mortgage Pass-Through Certificates Series 2006-ARI v Eslava, Hearing Transcript on Order to Show Cause, No. 1-2008-CA-055313, at 5 (Fl 11th Cir. Ct., Miami-Dade County, May 6, 2010).

[48] Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 176 (hereinafter: Arnold Deposition).

negotiation of a promissory note and a written assignment of the mortgage, the parties to that transaction can send an electronic message to MERS updating a field of information in the database. MERS calls this process an "electronic handshake."[49] But, unlike most county real property recorders, MERS does not keep digital or hard copies of documents that embody the agreement—making it much more difficult to track fraud and errors through the record keeping system. Even more troubling, MERS members are not legally bound to update this information on the database. In the words of the MERS' CEO, the system "is capable of being used to track [beneficial ownership interests] if the members utilize it for that reason."[50] But, if the MERS members choose not to use the database to reveal themselves, MERS does not investigate further or otherwise insist that members actually use this feature of the database. Instead, MERS leaves this to the "business model" of the financial institution. When asked whether MERS expects financial institutions to update the MERS database regarding changes in loan ownership, the company's CEO replied, "not so much. . . ."[51]

In a laudable, but ultimately anemic effort to respond to mounting criticism of the system's lack of transparency, MERS recently announced a new feature of its internet web page servicer identification system that allows borrowers to inquire as to the identity of a loan's investor. [52] However, the company's press release is somewhat misleading in that for securitized mortgages, MERS only reveals the name of the securitization trustee, rather than the trust that is the true beneficial owner of most loans. Private correspondence from MERS' communications manager explains that "the MERS® System only has the name of the trustee in the Investor field and does not capture information about the trust."[53] Learning the name of a borrower's securitization trustee does not allow the borrower to research the pooling and servicing agreement that controls a servicer's or trustee's authority to negotiate loan modifications. It also does not identify the name of the trust that could be held liable for purchasing loans that violate the Home Ownership and Equity Protection Act or other state predatory lending

---

[49] *Id.*

[50] Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 176 (hereinafter: Arnold Deposition) (on file with author).

[51] The deposition transcript on this point reads:

> [Nicholas Wooten] Q: So whenever a transfer occurs of any interest, be it a beneficial interest in the promissory note or be it servicing interest, those you expect to be entered on the MERS system?
> [R.K. Arnold] A: It's not so much that we expect it. We operate a system that offers that capability."

Arnold Deposition at 178.

[52] Press Release, MERS Expands Website To Disclose Loan Investor Information, http://www.mersinc.org/newsroom/press_details.aspx?id=241 (July 16, 2010).

[53] Electronic Mail of Karmel Lejarde, MERSCORP, Inc. Communications Manager, Sept. 3, 3010, (copy on file with author).

laws.[54] Even when the name of a securitization trustee is provided, this search result is still not a legally authoritative search upon which a searcher is entitled to rely in ruling out the possibility of other potential purchasers that could achieve priority in an ownership dispute. Rather it is simply a query to see whether any companies happened to have used an optional "electronic handshake" to enter assignment information on a private database.

Furthermore, the MERS servicer identification system often does not produce any information on beneficial ownership of loans at all, instead giving the message: "Investor: This investor has chosen not to display their information. For assistance, please contact the servicer."[55] Note that this sentence is ambiguous as to whether MERS does not know who owns the loan or the owner of the loan actually refuses to be identified. The former is disturbing in that it illustrates that we as a society no longer have a record keeping system that actually tracks legally recognized ownership interest in land back to a root of title. The latter is disturbing because it reveals how the MERS system has abated an important legal incentive to provide public notice of land ownership interests.

Both updating the MERS database and publically recording a mortgage assignment are permissive choices for financial institutions. But, a key difference is that the public system was backed by strong legal incentives to encourage financiers to provide notice of assignments. In contrast, the MERS system—designed by and operated for the exclusive benefit of mortgage finance companies—deliberately undermines and altogether lacks that incentive. Under the still current (but presently circumvented) law of all fifty states, the owner of an interest in land may intentionally conceal herself, but does so at the risk of losing that ownership interest. In both notice and race-notice jurisdictions, if a mortgage assignee fails to record, and the assignor either intentionally or unintentionally assigns the same mortgage to a second, subsequent assignee who does record, then first assignee will lose priority.[56] Where both assignees are using the MERS system, the only official recorded notice would be the original mortgage in the name of MERS. The MERS database may simply have no information on whether any assignments have taken place—leaving prospective investors (and courts adjudicating the conflicts that will develop) to speculate on who actually owned rights in the property. There is currently no legal penalty for failing to update the MERS database on changes in loan ownership that would incentivize financiers to avoid this situation. Because many mortgage companies in the boom years planned to sell their loans to investors, they focused on the short term commissions and

[54] *See* Christopher L. Peterson, *Predatory Structured Finance*, 28 CARDOZO L. REV. 2185, 233-46 (2007) (summarizing mortgage loan assignee liability law).
[55] MERS Servicer Identification System Search for Servicer Information Search Results, September 6, 2010 (results available on file with author).
[56] *See* 66 Am. Jur. 2d *Records and Recording Laws* § 162 (2010). *See, e.g.,* Second Nat. Bank of New Haven v. Dyer, 184 A. 386, 388-89 (Conn. 1936) ("That an assignment of a mortgage falls within the purview of the recording statute follows from the nature of such an instrument. . . . indeed to hold otherwise would make a serious inroad upon the policy of this state that purchasers of interests in real estate are entitled to rely upon the land records as disclosing the true title. . . .").

DRAFT

profits from originating loans. They, quite frankly, did not bother with documentation that would preserve our national legacy of certainty in property rights. As a result, the MERS database does not provide reliable, authoritative information on legally cognizable beneficial ownership of loans registered in its system. County real property records that hold only a reference to the MERS system now have a systemic break in chains of title. Perhaps this is what MERS means by its corporate slogan: "Process Loans, Not Paperwork."[57]

The full risk of confusion and litigation from this system will not be known for years to come. But already cases are emerging that reveal serious clouds on title. For example, in late 2009 a Florida mortgage origination and servicing company called Diversified Mortgage, Inc. sued MERS seeking a declaratory judgment resolving uncertainty over ownership of Florida mortgages registered on the MERS system.[58] In its complaint, Diversified—a mortgage lender, rather than a borrower—states:

> While the MERS system may benefit its members by enabling them to sell, transfer, and assign mortgages amongst themselves without the burden of documenting their transactions on paper or in the public records, this system has wreaked havoc on our nation's homeowners. In fact, the system implanted by MERS has essentially privatized the mortgage records while undermining the value of county public records. No longer can a homeowner visit a government office, review the public records, and learn the identity of who actually owns his mortgage. Doing so today will only lead to the discovery of that MERS is acting as nominee for whichever of its paying members currently owns the mortgage in question. While MERS may know which member owns a particular mortgage, the public cannot access the MERS system; it is a private virtual playground intended for members only. In essence, MERS' stance towards homeowners can be summarized as "one of our members owns your mortgage and that is all you need to know." While some stories of the aftermath resulting from this secretive system have come to light, such as those of homeowners who want to work with their lenders to avoid foreclosure, but are unable to identify their lenders, the full extent of the damage has yet to be done.[59]

While it must be edifying for critics of MERS to hear this argument from a mortgage origination and servicing company, the case is more interesting because of allegations about MERS role in facilitating ownership disputes.

In its complaint Diversified alleges that MERS may have allowed trading partners of Diversified to list themselves as owners of Diversified's loans without permission from Diversified.[60] When the lender asked MERS to produce a list of all Diversified's trading partners that may have claimed to own some of Diversified's loans, MERS either could not or refused to do so. After persistent

---

[57] *See* Welcome to MERS, www.mersinc.org (last visited Sept. 17, 2010).
[58] Complaint for Declaratory Judgment and Other Relief, Diversified Mortgage, Inc, v. MERSCORP, Inc and Mortgage Electronic Registration Systems, Inc., Case No. 8:09-cv-02497-VMC-EAJ (Fl 6th Circ, Pinellas County, December 10, 2009).
[59] *Id.* at ¶ 6.
[60] *Id.* at ¶ 10.

DRAFT

requests for more information, Diversified alleges that MERS employees became "confusing and hostile" and "demanded that Diversified not attempt further contact with MERS."[61] "Dumbfounded as to why MERS would cease communicating with a member mortgage company, and refuse it the basic information to which it was entitled, Diversified attempted further contact with MERS," but to no avail. Eventually, Diversified learned that other third party financial institutions had initiated foreclosure proceedings on mortgages that Diversified believed it owned.[62]

While this is only one example, some of the appellate courts that have been critical of the MERS system foretell further long term uncertainty surrounding property rights connected to MERS claims of ownership. For example, recognizing the implications of their own decision in *Landmark National Bank v. Kesler*, the Kansas Supreme court pointed out that "[i]n attempting to circumvent the statutory registration requirement for notice, MERS creates a system in which the public has no notice of who holds the obligation on a mortgage."[63] The Arkansas Supreme court goes even further stating that "[p]ermiting an agent such as MERS purports to be to step in and act without a recorded lender directing its action would wreak havoc on notice in this state."[64] And yet, that is precisely what the MERS system is designed to do. In the prototypical MERS as original mortgagee transactions *there are no recorded lenders.* [65] MERS is designed to be the cradle-to-grave notice proxy for all the half-dozen or so financial institutions and shell companies that hold title to the loan at different times—yet remain undocumented both in the public record and often on MERS' own database.

III. MERS AND THE PROBLEM OF CONVEYANCE

If the growing line of cases asserting that MERS is neither a mortgagee nor a deed of trust beneficiary is correct, then courts must soon confront profound questions about the very enforceability of MERS' security agreements. Not merely an ancillary issue, MERS registered loans have fundamental problems related to the very nature of what a mortgage *is*. There is a compelling legal argument that loans originated through the MERS system fail to create enforceable liens.

MERS' security agreements name MERS as the mortgagee or deed of trust beneficiary. If this is a legally incorrect statement—as every state supreme court looking at the issue has agreed—then the security agreements *do not name an actual mortgagee or beneficiary*. Loans originated with MERS as the original

---

[61] *Id.* at ¶ 11.
[62] *Id.* at ¶ 13.
[63] Landmark Nat. Bank v. Kesler, 216 P.3d 158,168 (Kan. 2009).
[64] Mortgage Elec. Registration System, Inc., 301 S.W.3d at 5.
[65] Some county recorders track the originating lender's name in addition to MERS' name when a mortgage is first recorded. But, once the mortgage is assigned, the name of the original lender is no longer useful and leads to a dead end in searching for actual ownership interest in the land.

Mortgagee purport to separate the borrower's promissory note, which is made payable to the originating lender, from the borrower's conveyance of a mortgage, which is purported to be granted to MERS. The mortgage industry has premised its proxy recording strategy on this separation despite the U.S. Supreme Court's holding that "the note and the mortgage are inseparable."[66] If today's courts take the *Carpenter* decision at its word, then what do we make of a document purporting to create a mortgage entirely independent of an obligation to pay? If the Supreme court is right that a "mortgage can have no separate existence"[67] from a promissory note, then a security agreement that purports to grant a mortgage independent of the promissory note attempts to convey something that cannot exist.[68]

While this argument will surely strike a discordant note with the mortgage bankers that invested billions of dollars in loans originated with this simple flaw, the position is consistent with a long and hitherto uncontroversial line of cases. Many courts have held that a document attempting to convey an interest in realty fails to convey that interest when an eligible grantee is not named.[69] Courts all around the country have long held: "there must be, in every grant, a grantor, a grantee and a thing granted, and a deed wanting in either essential is absolutely void."[70] Indeed, this common sense rule dates back to Blackstone's Commentaries

---

[66] Carpenter v. Longan, 83 U.S. 271, 274, (1872). *See also* Nagle v. Macy 9 Cal. 426, 1858 WL 818 (Cal. 1858) ("The debt and the mortgage are inseparable.")
[67] Carpenter, 83 U.S. at 274.
[68] There is no clear reason why deeds of trust would be any different in this respect. Domarad v. Fisher & Burke, Inc. 270 Cal App 2d 543, 76 Cal Rptr 529, 535-36 (Cal App 1st Dist 1969) ("[A] deed of trust is *inseparable* from the debt and *always* abides with the debt, and it has *no market or ascertainable value, apart from* the obligation it secures.") (emphasis added).
[69] Disque v. Wright, 49 Iowa 538, 1878 WL 623 (Iowa 1878) ("It has been frequently held that slight omissions in the acknowledgment of a deed destroy the effect of the record as constructive notice. *A fortiori,* it seems to us, should so important and vital an omission as that of the name of the grantee have that effect."); Chauncey v. Arnold, 24 N.Y. 330 (N.Y. 1862) ("No mortgagee or obligee was named in [a mortgage], and no right to maintain an action thereon, or to enforce the same, was given therein to the plaintiff or any other person. It was, *per se,* of no more legal force than a simple piece of blank paper."); Richey v. Sinclair, 47 N.E. 364 (Ill. 1897) ("The law is well settled that a deed without the name of a grantee is invalid. It is said there must be in every grant a grantor, a grantee, and a thing granted; and a deed wanting in either essential will be void."); Allen v. Allen, 51 N.W. 473, 474 (1892) (omission of name of grantee invalidated conveyance because "A legal title to real property cannot be established by parol."); 59 CJS MORTGAGES § 306 ("Notice may be deemed not present in cases of insufficient attestation or where the instrument itself is so defective as to be void as a matter of law, as where it wholly omits the name of the mortgagee.") (citations omitted).
[70] Whitaker v. Miller, 83 Ill. 381, 1876 WL 10353 (Ill. 1876); Trout v. Taylor, 32 P.2d 968 (Ca. 1934); Green v. MacAdam, 346 P.2d 474, 485 (Cal.App. 1959); Hulsether v. Peters, 167 N.W. 497, 498 (S.D. 1918); Allen v. Allen,

DRAFT

which state: "What are the requisites of a deed? … There must be persons able to contract and be contracted with, for purposes intended by the deed; and also a thing, or subject matter, to be contracted for; all of which must be expressed by sufficient names."[71] And more recently, Patton and Palomoar's treatise agrees that: "It is axiomatic that a deed will be inoperative as a conveyance unless it designates someone to whom the title passes. A grantee is as necessary to the validity of a grant as that there should be a grantor or a property granted."[72]

An 1869 New York Court of Appeals case illustrates the point. In *Chauncey v. Arnold* a debtor attempted to create an "in blank" mortgage comparable to a negotiable instrument payable to bearer.[73] Rather than specifying the name of the actual mortgagee, the debtor left the name of the mortgagee blank with the intention of facilitating subsequent transfer of the mortgage to any interested party willing to invest in it.[74] This might make some sense in that writing a security agreement with no stated mortgagee might have the potential to facilitate easy transfer of the mortgage, just like banks quickly transfer personal checks that have been indorsed in blank. Leaving the name of the mortgagee silent was an effort to eliminate the need to draw up (and perhaps pay recording fees on) a subsequent assignment of the mortgage. Unlike mortgages, promissory notes and drafts may be made "payable to bearer."[75] This legal language in an instrument allows any person in physical possession of the bearer paper (including even a thief), to demand payment from the maker in the case of a note or the drawee in the case of a draft.[76] Negotiable instruments have this feature because the architects of Article 3 of the Uniform Commercial Code and the English common law set out by Lord Mansfield that preceded it believed that transfer of the right to receive payment by mere possession of the instrument was useful in enhancing the liquidity of the payment right.[77] Nonetheless, in *Chauncey*, the trial court, intermediate appellate court and New York's highest court all agreed that the attempt to convey an "in blank" mortgage failed.[78] The Court of Appeals explained, "No mortgagee or obligee was named in [the security agreement], and no right to maintain an action thereon, or to enforce the same, was given therein to the plaintiff or any other person. It was, *per se,* of no more legal force than a simple piece of blank paper."[79]

---

51 N.W. 473, 473 (Minn. 1892); Beard v. Griggs, 1 J.J.Marsh. 22, 1829 WL 1139 (Ky.App. 1829); Morris v. Stephens,
46 Pa. 200, 1863 WL 4942, 10 Wr.Pa. 200 (Pa., 1863).

[71] 2d Blackstone's Commentaries, 296.

[72] 2 PATTON AND PALOMAR ON LAND TITLES § 338 (3d ed. 2009)

[73] Chauncey v. Arnold, 24 N.Y. 330, 332 (N.Y. 1862).

[74] *Id.*

[75] Unif. Com. Code §§ 3-104(a)(1) & 3-109(b).

[76] *Id.* § 3-301& 1-201(b)(21).

[77] Edward L. Rubin, *Learning from Lord Mansfield: Toward a Transferability Law for Modern Commercial Practice*, 31 ID. L. REV. 775, 777-786 (1995).

[78] Chauncey, 24 N.Y.at 331 ("[T]he cases arising upon bills and notes are plainly distinguishable.").

[79] *Id.* at 335.

The Supreme Court of California reached a similar result in a deed of trust state. In *Trout v. Taylor* a shady finance company induced "an elderly woman, without business experience, and of very limited schooling and education" into signing a blank deed conveying her land.[80] After execution and delivery of the deed, the finance company filled in the name of a company insider, took out a few loans against the land and sold them to investors. In analyzing whether the deed was enforceable the Court pointed to the absence of a named grantee and held that "the deed in question was not voidable, but was void in toto; a nullity."[81]

An Illinois Supreme Court case provides an interesting contrast. In *Richey v. Sinclair*, a debtor simultaneously signed a promissory and a mortgage.[82] The note specified the name of the creditor, but due to a drafting error the mortgage did not specify the creditor's name—leaving the identity of the mortgagee unintentionally ambiguous. While the Illinois Court of Appeals held the mortgage was unenforceable, the Supreme Court of Illinois reversed. The Supreme Court agreed in principle that mortgages that do not specify a mortgagee are unenforceable.[83] But, it pointed out that particular circumstances of the case—including the simultaneously executed promissory note identifying a payee and boilerplate within the mortgage document indicating that the mortgagee was the same person as the note –made the identity of the mortgagee sufficiently clear to remain enforceable. In comparison, the case for enforcement of MERS loans is arguably worse, since MERS is never identified on the promissory note and is a *different* party than the actual economically interested business.

The *Chauncey v. Arnold* decision and cases like it have long lied dormant as settled and uncontroversial law. Indeed, since the mid-nineteenth century, the often harshly introspective New York appellate courts have not once limited or distinguished *Chauncey*. The reason must lie in simple common sense recognition that we ought not to allow interests in land to be transferred where the true identity of the party that receives the granted land is not plain, clear, and presently revealed at the time of the attempted conveyance. Unlike simple monetary payment rights which are habitually created and extinguished every day of a consumer's life, the conveyance of land has a special place in American law.[84] The lives and fortunes of generation after generation America's middle class turn more on their ownership of land than any other asset.[85] Just like the *Chauncey* court, most American jurists have traditionally recognized that the conveyance documents of land rights must

[80] Trout v. Taylor, 32 P.2d 968, (Ca. 1934).
[81] *Id* .at 970.
[82] Richey v. Sinclair, 167 Ill. 184, 47 N.E. 364 (Ill. 1897).
[83] *Id.*
[84] *In re Stubbs*, 330 B.R. 717, 730 (N.D. Ind. 2005) ("There is no other "thing" more important historically in our culture than an interest in land, whether that interest be in a condominium, in a house, or in farm. Land. The transferring of interests in land has been entrusted to a system of records that allows people to be certain that this single most important asset in their lives is *indeed* going to be theirs, and that the encumbrances recorded with respect to this asset are in fact accurate and valid.").
[85] *See* Dalton Conely, Being Black, Living in the Red: Race, Wealth, and Social Policy in America 16 (1999).

DRAFT

carefully and clearly memorialize ownership. If a grantor, be it a prospective mortgage debtor or even one who wishes to convey fee simple title to land as a gift, wants to transfer an ownership interest in that land, surely it is not too much to ask that she specify who exactly will receive it in the document that purports to make the conveyance.

Reminiscent of these facts, MERS mortgages and deeds of trust attempt to create the equivalent of bearer paper mortgages. While the debtor in *Chauncey v. Arnold* left the name of the mortgagee blank, debtors in MERS as original Mortgagee loans do quite nearly the same thing by attempting to convey the property interest to a nationally ubiquitous proxy that has no meaningful financial intention of taking it. The line of cases that hold MERS is not a mortgagee suggest that MERS security agreements are essentially silent on identity of the mortgagee. By inducing debtors to specify a hollow placeholder as the grantee of their property interests, mortgage bankers have attempted to create a completely fungible mortgage where the true owner of the lien (or the land itself in title theory states) becomes whoever the error prone, virus infected, customer service representative bulwarked computer records of mortgage loan servicers say it is.[86]

Even under the jurisprudence most favorable to MERS with respect to the severability of notes and mortgages, it remains unclear whether MERS as original mortgagee security agreements can effectively convey a mortgage. Some courts have held that under very limited circumstances mortgages are severable from notes, but that prior to foreclosure the ownership of the note and the mortgage must be unified in one party that both suffers a default and asks the court for a remedy.[87] Under this view—which is not the view of mortgages supported by the Supreme Court's decision in *Carpenter v. Longan*—some courts might be willing to re-unite the mortgage with the note, possibly satisfying some standing to foreclose concerns.[88] But, even this controversial line of cases much less clearly stands for the proposition that a contract can *create* a mortgage severed at the outset from an obligation. Such a decision would require the reversal of cases such as *Chauncey v. Arnold* and would risk great mischief in property conveyance law, which has

[86] *See* Kathreine M. Porter, *Misbehavior and Mistake in Bankrutpcy Mortgage Claims,* 87 TEX. L. REV. 121 (2008); Gretchen Morgenson, *Dubious Fees hit Borrowers in Foreclosure,* New York Times, Nov. 6, 2007.

[87] 5-Star Management, Inc. v. Rogers, 940 F.Supp. 512, 521 n.5 (E.D.N.Y. 1996) ("The Court observes that a determination that the mortgage at issue, having been separated from the underlying promissory note, may be unenforceable would not leave the plaintiff in possession of a worthless instrument. This conclusion obtains because the plaintiff presumably can sell the mortgage to the holder of the underlying obligation. The plaintiff also can purchase the underlying obligation from the holder of the note. In that case, plaintiff, as holder of both the mortgage and the note, could foreclose on the mortgage on the New York Property.").

[88] The inherent problem in this position is that it is unclear how MERS would assign the mortgage to someone if it is not a mortgagee. Surely MERS cannot assign something that it does not own. Even if MERS is attempting to assign the mortgage as an agent, it remains unclear in most cases who MERS is assigning the mortgage for since, after all, the security agreement does not specify who (other than MERS) owns the mortgage in the first place.

DRAFT

always had high standards for clarity of language in deeding and bequeathing property. This rule is tantamount to allowing the conveyance of a property interest that cannot be enforced, since the mortgage grantee would not have a foreclosure right. To convey a mortgage which does not include a foreclosure right is to convey nothing at all. Moreover, allowing the creation of a mortgage separate from the note will expose mortgagors to a constant threat of double liability since the holder of the promissory note and a different owner of the mortgage may both show up at different times demanding payment.[89] Over the long term, the more simple, the more sustainable, the more conflict deflating rule will be to follow the U.S. Supreme Court's position that mortgages and deeds of trust ought remain inseparable from the obligation that triggers foreclosure rights.

In a stunning betrayal of the policies that ground the ancient statute of frauds principal commanding that we commit transfers of land interests to writing, mortgage bankers wrote millions of mortgage loans that did not specify who the actual mortgagee was. For over a hundred years, our courts have held that "legal title to real property may not be established by parole."[90] Had the parties to these transactions followed the simple policy of specifying in the documents who owns what, a vast amount of the confusing litigation and commercial uncertainty could have been avoided. These anchorless liens now flail in the wind of our commercial tempest. Courts that come to understand this situation will be in a bitter predicament. On the one hand, if they employ a "tough love" policy invalidating liens because they do not specify a mortgagee, they will throw the mortgage market into further turmoil. On the other hand, if the courts write opinions allowing MERS to act as a ubiquitous national proxy mortgagee, they will write into the American common law fundamental legal mischief that will plague generations to come.

In the short term, the harsh consequences of opinions that insist on security agreements that name an actual mortgagee could be tempered by granting the true loan owner (if it can be identitifed) an equitable mortgage. Traditionally, courts of equity were sometimes willing to imply an equitable mortgage where the parties to the transaction intended that there be security for the loan, but failed to comply with formal conveyance requirements. Generally speaking the elements of an equitable mortgage include:

> (1) the mortgagor has a mortgageable interest in the property sought to be charged as security; (2) clear proof of the sum which it was to secure; (3) a definite debt . . . to be secured, due from the mortgagor to the mortgagee; and (4) the intent of the parties to create a mortgage, lien or charge on the property sufficiently described or identified to secure the obligation.[91]

---

[89] 5-Star Management, 940 F.Supp. at 520 ("To allow the assignee of a security interest to enforce the security agreement would expose the obligor to a double liability, since a holder in due course of the promissory note clearly is entitled to recover from the obligor.") (Citation omitted).
[90] Allen v. Allen, 51 N.W. 473, 474 (Minn. 1892)
[91] 54A Am.Jur.2d Mortgages § 13.

The sensible policy behind the rule is to give effect to the substance of the transaction rather than its form. [92] This equitable doctrine seems to fit the circumstances of MERS-as-mortgagee loans because there is no real doubt that borrowers intended to grant security interests. Generally, it is not fair, nor should reasonable borrowers expect, to receive a home for free. Awarding equitable mortgages to securitization trusts could strike a reasonable balance in the interests of borrowers and lenders without ignoring the fact that the standard security agreement does not name an actual mortgagee.

Even in the absence of an equitable mortgage, borrowers that did not succeed in conveying a lien still signed the promissory note and will generally owe an unsecured debt. Creditors can sue on unsecured debts and, within the limits of state exempt property statutes, obtain judicial liens on family homes. Of course, this is a more time consuming process than foreclosure and one that is subject to intervening liens. Moreover, it is one that will be more difficult given the state of the financial industry's records. Given this situation, some courts could reasonably believe that the mortgage industry has stored up some "need to get my paperwork done" karma.[93]

While awarding equitable mortgages is surely a better approach for financiers and their investors than simply invalidating liens, it would not solve all their problems. Replacing legal mortgages with equitable mortgages would give borrowers significant leverage. Historically, state law has not uniformly treated equitable mortgagees vis-à-vis other competing creditors. Generally, the holder of an equitable mortgage had priority against judgment creditors.[94] But, it is likely that an equitable mortgage could be avoided in bankruptcy. [95] Moreover, it is likely

---

[92] *See, e.g.,* Burkhardt v. Bailey, 680 N.W.2d 453 (2004) ("An equitable mortgage places the substance of the parties' intent over form.").

[93] HSBC Bank USA, NA as Trustee for Monura Asset Acceptance Corporation, Mortgage Pass-Through Certificates Series 2006-ARI v Eslava, Hearing Transcript on Order to Show Cause, No. 1-2008-CA-055313, at 17-18 (Fl 11th Cir. Ct., Miami-Dade County, May 6, 2010) (dismissing foreclosure complaint with prejudice, cancelling promissory note, and conveying clear title to homeowner as a sanction for inconsistent record keeping and litigation tactics); Deutsche Bank National Trust Company, as Trustee for GSAMP 2006-FMI v. Lippi, No. CA08-0127 (Fla. 7th Cir. Ct., St. Johns County, Feb. 11, 2010) (order dismissing foreclosure complaint with prejudice on MERS recorded loan for failure to show any evidence of standing following two years of litigation and multiple dismissals with leave to amend); HSBC Bank USA, N.A. v. Yeasmin, 27 Misc.3d 1227, 2010 WL 2089273 (N.Y. Sup. 2010) (cancelling foreclosure action on MERS recorded loan in an order that states: "The instant motion, attempting to cure the four defects explained by the Court . . . are so incredible, outrageous, ludicrous and disingenuous that they should have been authored by the late Rod Serling, creator of the famous science-fiction televison series, *The Twilight Zone."*).

[94] Pagenhardt v. Walsh, 250 Md. 333, 243 A.2d 494 (1968).

[95] 11 U.S.C. § 544(a) (2010); *In re* Paul J. Paradise & Associates, Inc., 217 B.R. 452, 455 (1997); Mortgage Lenders Network, USA v. Sensenich, 177 Vt. 592, 873 A.2d 892 (2004); Citizens Nat. Bank in Zanesville v. Denison, 133 N.E.2d 329 (Oh. 1956).

DRAFT

that financiers would have less luck seeking deficiency judgments when foreclosing on equitable mortgages. Perhaps most important, as financiers bargain in the shadow of losing their legal mortgage, they might well come to the negotiating table more inclined to offer realistic modification agreements. The judicial threat of invalidating mortgages and replacing them with less tactically useful equitable mortgages could decrease court's dockets by forcing securitization trustees and servicers to the negotiating table.

IV. What About the Money? The Right of Counties to Recover Unpaid Recording Fees

MERS and its member use false documents to avoid paying recording fees to county governments. At the most simple level, mortgages and deeds of trust recorded at origination represent that MERS is the mortgagee or deed of trust beneficiary. Taking the appellate decisions in Arkansas, Kansas, Maine, and Missouri at face value, MERS recorded mortgages contain a false statement. While it is true that MERS recorded mortgages and deeds of trust also have qualifying language suggesting that MERS is also a "nominee," the representation that MERS is the owner of the lien is not some innocuous legalism. It causes county recorders that maintain grantor-grantee indexes to list MERS in the chain of title for the land. The false designation of MERS as a mortgagee or beneficiary creates a false lead in the true chain of title defeating an essential purpose of recording mortgages and deeds of trust.

But perhaps even more troubling are the documents recorded in the name of MERS later in the life of mortgage loans. Recall that MERS' business model does not include actually recording documents relating to its purported ownership itself. Instead, it allows employees of mortgage servicing companies and law firms to do so on its behalf. MERS has an internet web page where mortgage servicers and law firms can enter names of their own employees to automatically produce a boilerplate "corporate resolution" that purports to designate the serviers' and law firms' employees as certifying officers of MERS with the job title of assistant secretary and/or vice president. These servicer and law firm employees then sign and record documents such as mortgage assignments, substitution of deed of trust trustees, and substitutions of deed of trust beneficiaries—all including the representation that they are a MERS vice president or assistant secretary. Some states require that the individual signing a document conveying an interest in land have the job title of vice president or higher. Surely this policy is to prevent mistakes, confusion, and disputes over land ownership. But many servicer and law firm employees use the "vice president" title even when it is not required—perhaps because it just sounds better.

Only, it is not true. The representation that employees of mortgage servicing companies and foreclosure law firms are "vice presidents" of MERS is false. In the English language the words vice president primarily mean: "an officer next in rank to a president and usually empowered to serve as president in that officer's absence or disability."[96] Sometimes, vice president can mean "any of several officers serving as a president's deputies in charge of particular locations or

[96] MERRIAM WEBSTER DICTIONARY (3d ed. 2002).

DRAFT

functions."[97] The reality of what MERS "vice presidents" actually do, from whom they receive their paychecks, and their actual job titles are fundamentally inconsistent with a corporate officer than serves as president when the president is disabled, or acts as the president's deputy. A deposition transcript taken from a foreclosure case brought by a Florida debt collection law firm is illustrative. The deponent was a non-attorney employee of the firm that was claiming MERS certifying officer status. The employee was responsible for signing 20-40 mortgage assignments that would be recorded with county officials per day.[98] The firm's rationale for allowing this was one of the boilerplate "corporate resolutions" taken off of MERS' website that stated: "The attached list of candidates are employees of Florida Default Law Group and are hereby appointed as assistant secretaries and vice-presidents of MERS." When this "Vice President" of MERS was asked about her relationship with MERS she responded:

> Q Did you have to have any sort of training to become a Certified Officer?
> A No.
> Q Do you know where MERS is located?
> A No.
> Q Have you ever been there?
> A No.
> Q Have you ever spoken with anyone at MERS?
> A No.
> Q Have you ever had e-mail transmissions back and forth with anyone from MERS?
> A No.
> Q Do you file any reports with MERS relating to assignments?
> A No.
> Q Do you know who the president of MERS is?
> A No.
> * **
> Q And I guess at some point, somebody explained to you that you were a Certified Officer is that correct? . . . .
> A Yes.
> Q And what do you remember as to their explanation as to what that meant?
> A Why I was being chosen as a Certified Officer?
> Q Yes.
> A That it was actually a group of us, we had one meeting and they explained that people that had an understanding of what an assignment was were going to go ahead and become

---

[97] *Id.*

[98] Wells Fargo Bank v. Van Seigman Deposition Transcript, Kimberly Litchfield, Direct Examination, at 36.

> certified officers because we then had authorization to execute on behalf of MERS.[99]

It is inconsistent with even the most expansive definition of the term vice president, that an individual who is not an employee of the company, has never been to the company's location, does not even know where the company is located, has never met the company's president, does not know who the president is, and has never personally *communicated* with the company in any way can be considered a vice-president of that company. It does not follow that because a belief is convenient, it is also true.

Perhaps the designation of servicer and law firm employees as "assistant secretaries" of MERS is less absurd, but it is also still false. While many of these servicer and law firm employees are secretarial workers in the businesses that they actually work for, they are not assistant secretaries *of* MERS in any meaningful economic sense. They have no more contact with MERS than vice presidents do. Indeed the fact that MERS' boilerplate resolutions allow the employees to just pick which title they want to use is compelling evidence that the whole concept is twaddle. MERS Assistant secretaries are not paid by MERS. They receive no health benefits from MERS. In yet one more example of Orwellian doublespeak, it is the financial institutions and law firms that *pay MERS* to allow them to pretend that they have MERS employees.[100] Who *pays* to be an assistant secretary? [101] While mortgage brokers and financiers may be keen on entrusting the nation's real property records to a company with these standard business practices, one can imagine that this might make the democratically elected county recorders that have dedicated their professional careers to preservation of land ownership rights somewhat uncomfortable.

County recorders deserve a fair hearing if they were to request payment of recording fees for assignments avoided through use of documents containing these

---

[99] Wells Fargo Bank v. Van Seigman Deposition Transcript, Kimberly Litchfield, Direct Examination, at 39-41 (available on file with author). *Compare In Re* Haque, Order Granting Wells Fargo, Bank, N.A.'s Motion for Relief from State and Imposing Sanctions for Negligent Practice and False Representations, Case No. 08-14257-BKC-JKO, (Bkrptcy. S.D. FL, Oct., 28 2008) (imposing $95,130.45 in sanctions on Florida Default group for filing affidavit claiming unjustified interest charges).

[100] For a complete schedule of membership and transactional fees members pay to MERS see Pricing, www.mersinc.org/MersProducts/pricing.aspx?mpid=1, (last visited Sept. 19, 2008).

[101] Ironically, MERS actually sometimes charges a fee to members when it has to forward mail *addressed to MERS* to the member that actually has an interest in the loan. MERSCORP, INC. Rules of Membership, Rule 5, § 4 (June 2009) (available at: www.mersinc.org/MersProducts/pricing.aspx?mpid=1) ("If MERS determines that MERS receipt of mail involving a foreclosure proceeding, lawsuit or code violation resulted from a violation of any of the MERS Rules or Procedures, then MERS shall be entitled to charge the Member a fee of $12.00 for each filing or document in the proceeding or for each piece of mail received related to the code violation that MERS forwards to the Member beyond the initial service of process or notification that MERS received on behalf of that Member.").

DRAFT

false statements. Recording of these legally and factually false statements caused a reduction in the revenue that county governments would have collected from mortgage financiers. MERS itself used projections of this reduction in revenue in its sales pitches and marketing material. Indeed the studies done by accountants that justified the creation of MERS show how use of the MERS system—which entailed recording false documents—would cause a reduction in fees paid to counties.

But perhaps most compelling, pooling and servicing agreements packaging mortgage loans into securities legally require finance companies to record (and pay recording fees on) every assignment of a mortgage loan from orgination through deposit in a securitization trust. A 2005 Pooling and Servicing Agreement between J.P. Chase Morgan's subprime subsidiary as a depositor, J.P. Chase Morgan's actual bank as servicer, and Wachovia Bank as trustee Chase's subprime subsidiary provides a typical example. The pool included both non-MERS and MERS loans, but had different assignment recording warranties for each. In the agreement Chase's subprime subsidiary promised to turn over to the securitization trustee "Originals of all recorded intervening Assignments of Mortgage, or copies thereof, certified by the public recording office in which such Assignments or Mortgage have been recorded *showing a complete chain of title from the originator to the Depositor*, with evidence of recording . . . ."[102] Conversely, in the case of MERS-recorded loans, the same agreement does not require recording of intermediate assignments. Instead it only requires the depositor to take "such actions as are necessary to cause the Trustee to be clearly identified as the owner of each such Mortgage Loan on the records of MERS. . . ."[103] In this typical securitization deal, Chase used the MERS system to duck a contractual obligation to produce recorded assignments for every non-MERS loan included in the pool—even though counties depend on the revenue produced by those assignments.

Using false documents to avoid paying fees to the government sounds a lot like tax fraud. If county governments sue to recover unpaid recording fees, MERS and its member financiers will probably argue that tax fraud is distinguishable from using false documents to avoid paying recording fees. In typical cases of unpaid taxes there is some underlying obligation to pay by virtue of statutory tax law. But, in MERS recording fee cases the underlying choice to record a mortgage or assignment, and pay the required fee, is permissive under state land title laws. Thus, the argument: while it may be true that the use of allegedly false statements caused financiers to choose not to pay recording fees, they were free to assume the risk of this choice. Taxes, unlike recording fees, are not permissive.

However, state supreme courts offended by using false documents to avoid paying fees do not need to play the financier's music as written. Where

---

[102] CHASE MORTGAGE FINANCE CORPORATION, DEPOSITOR, JPMORGAN CHASE BANK, N.A., SERVICER AND WACHOVIA BANK, N.A., TRUSTEE POOLING AND SERVICING AGREEMENT Dated as of November 1, 2005, $1,900,007,729.12, Multi-Class Mortgage Pass-Through Certificates Series 2005-A1, at § 2.01 (copy on file with author) (emphasis added).
[103] *Id.* § 2.01

DRAFT

financiers recorded false statements of ownership, they could be judicially estopped from denying liability for unpaid recording fees. Courts have held that "[A] party will not be permitted to maintain inconsistent positions or to take a position in regard to a matter which is directly contrary to, or inconsistent with, one previously assumed by him, at least where he had, or was chargeable with, full knowledge of the facts."[104] The policy behind judicial estoppels is "to preclude one who prevents a thing from being done from availing himself of the nonperformance which he has himself occasioned."[105] Courts are particularly likely to use estoppel where the party making inconsistent representations accepts some benefit from the misrepresentation. At the time of origination, and in many foreclosure cases, members of the MERS system maintain that MERS owns the mortgage. But, when it comes time to deposit the mortgage loan into a securitization trust, they maintain that depositor owns the mortgage.

The J.P. Chase Morgan securitization pooling and servicing agreement is again illustrative. In it the depositor warrants that "the Mortgage Loan, including the Mortgage Note *and the Mortgage*, . . . [are]not subject to an assignment or pledge, and *the Depositor* had good and marketable title to and . . . *[is] the sole owner thereof*."[106] Trust depositors claim to own the mortgage they are selling to investors because they want to insure that courts will recognize the trust's assets as purchased through a true sale. True sale opinions were a *sine qua non* of securitization deals because rating agencies would not give satisfactory credit ratings to securities drawn from pools of assets that the trust does not actually own. And, all rights to a mortgage loan must be deposited into the trust for it to achieve tax exempt status under federal REMIC law—which does not contemplate the use of a proxy mortgagee. Yet, despite claiming sole ownership of mortgages sold to investors, in documents regularly recorded with county officials these same institutions maintain that MERS is the sole owner of the mortgage. The chain of financial institutions linking originators to securitization depositors collectively want to have their lien and sell it too.

When financiers talk to investors, they claim to own mortgages in order to convey the sense that they own what they are selling. But when financiers talk to the government they claim not to own what they are selling so as to not be obliged to pay fees associated with owning it. MERS and its members prevent recording fees from being paid on assignments—that was the whole point of MERS—but then attempt avail themselves of the protection that having taken such an action would have afforded. The law of judicial estoppel gives state courts the power to

---

[104] 28 AMJUR2d, Estoppel § 71.

[105] 28 AMJUR2d, Estoppel § 71; Pannunzio v. Monumental Life Ins. Co., 168 Ohio St. 95, 5 Ohio Op. 2d 356, 151 N.E.2d 545 (1958) (a defendant cannot be permitted to rely upon his own intentional failure to perform a duty owed to an innocent party as the basis for a defense against that party).

[106] CHASE MORTGAGE FINANCE CORPORATION, DEPOSITOR, JPMORGAN CHASE BANK, N.A., SERVICER AND WACHOVIA BANK, N.A., TRUSTEE POOLING AND SERVICING AGREEMENT, Dated as of November 1, 2005, $1,900,007,729.12, Multi-Class Mortgage Pass-Through Certificates Series 2005-A1, at § 3.01(l) (copy file with author).

DRAFT

the pull back the MERS' two-faced mask by estopping financial intuitions from denying liability for intermediate recording fees.

Of course the equitable remedy of judicial estoppels requires courts to consider whether justice is served by requiring financial instutions to pay fees assignments that were left unrecorded through use of MERS subterfuge. Here, there is a stark and ironic contrast between the largest financial institutions that benefited from recording subterfuge (and federal bailouts) the most and the budget crises facing many county governments. While financial institutions are defending the practice of recording false documents to avoid paying modest fees, county governments have been laying off teachers,[107] firefighters,[108] police officers,[109] infectious disease clinic workers,[110] closing criminal detention centers for violent juveniles,[111] and shuttering courthouses.[112] Surely some courts will find it

---

[107] Nick Anderson, *100,000 Teachers Nationwide Face Layoffs*, Washington Post, May 27, 2010 ("California is ground zero for the school budget crisis. The most populous state, with a budget deficit of $19 billion, is shedding summer school, music and art classes, bus routes, days from the school year, and yet-uncounted thousands of teachers.").

[108] Josh Brogadir, *Lawrence Fire Layoffs Create Burden for Surrounding Towns*, NECN.COM, August 11, 2010; Matt Byrne, *Layoff Cause Station to Close,* Boston Globe, August 9, 2010; *Newark Submits Plan to Eliminate Nearly 1,000 City Jobs*, New Jersey Star-Ledger, August 26, 2010; Derek Spellman, *Police, Firefighter Layoffs Take Effect in Neosho*, Joplin Globe (Joplin, Missouri), August 10, 2010.

[109] Sandra Livingston, *Ashtabula Judge Says People May Want to Arm Themselves Since Budget Cuts Have Slashed Law Enforcement*, Cleveland Plain Dealer, April 19, 2010 ("Budget cuts have whacked Ashtabula County so hard that just one sheriff's cruiser now patrols 720 square miles, raising a troubling question: Who will protect residents of this sprawling, rural Northeast Ohio county when sheriff's deputies are miles away? A county judge has a suggestion: Concerned people may want to arm themselves.").

[110] Lisa Schniming, *State Cuts Accelerate Public Health Funding Shortfall,* CIDRAP NEWS, March 1, 2010 ("The National Association of County and City Health Officials (NACCHO) said today in a statement that the departments cut 16,000 jobs last year.").

[111] Tom Brennan, *Budget Cuts Could Close County Juvenile Detention Center,* Tampa Tribune, January 29, 2010; Mike Corn, *Detention Center Closing*, Hays Daily News (Hays, Kansas), June 1, 2010; Gil Halsted, Impasse on Which Juvenile Detention Center Will Close, Wisconsin Public Radio, June 3, 2010, at: http://www.wpr.org/news/archives/1006.cfm.; *Juvie Center Closing Could Give Teen Thugs Their Freedom*, Trentonian, May 21, 2009; Ann Kelley, Budget Cuts May Close Shawnee Juvenile Detention Center, The Oklahoman, May 24, 2010; Dan Linehan, *Juvenile Detention Center to Close: Blue Earth County Drops Its Commitment*, Free Press (Mankato, Minnesota), July 2, 2010; *Monmonth County Could Close Juvenile Detention Center,* New Jersey Star-Leger, January 24, 2009; P.J. Reilly, *Other Juvenile Detention Centers Struggling: Loss is Lancaster County's Gain,* Intelligencer Journal (Lancaster, Pennsylvannia), July 28, 2010; *State May Close Maximum Security Juvenile Detention Center*, 8 NEWSNOW

offensive for the mortgage industry to argue that it can use false documents to avoid paying recording fees at a time when counties are laying off elementary school street crossing guards.[113]

VI. REBUILDING A TRUSTWORTHY REAL PROPERTY RECORDING SYSTEM

Counsel for financial instutions, federal and state housing agencies, and title insurance companies need to take a candid, reflective look at the implications of mortgage bankers' efforts to usurp government control of real property records. Even those who prefer minimalist government must recognize that in a democratic republic divestment of this responsibility from government to industry should have occurred with the consent of elected representatives of the people. In this case, the early involvement of Fannie Mae and Freddie Mac—federally sponsored corporations that do deserve respect for their efforts to facilitate American homeownership –did not dispense with the sovereign right of state governments to control their own real property recording law. Laws for the states are made by the states, not by Government Sponsored Enterprises. Fannie Mae and Freddie Mac could take a step toward restoring national trust by stepping away from the MERS system and requiring traditional recording practices in qualified loans. With their many critics in Congress the last thing the GSEs need is to take on political and legal risks associated with MERS.

As financial services companies begin to rebuild their loan portfolios and take steps toward restarting the securitization of residential mortgages, they would be well advised to insist that mortgage brokers and originators deliver only non-MERS loans. Underwriters, as well as credit rating agencies, should demand much more careful attention to not only indicia of credit quality, but also legal formalities such as physical note delivery and mortgage recordation. The "process loans, not paperwork" mantra still espoused by MERS is a symptom of the industry's cavalier and self-defeating attitude toward attention to detail. Legal compliance—apparently what MERS calls "paperwork"—may create short term savings for brokers and servicers, but it does at the expense of substantial longer

---

(Las vegas), February 16, 2010, http://www.8newsnow.com/global/story.asp?s=11995433.

[112] Christina Pazzanese, *Trial Court to Make 'Devastating'* Cuts, Massachusetts Lawyers Weekly, July 19, 2010 ("Trial Court officials have announced they are moving ahead with plans to lay off hundreds of workers and to relocate or shutter 14 courthouses statewide."); William M. Welch, *Court Budget Cuts Swift Hand of Justice*, USA Today, April 1, 2010 ("At least 15 states have put court workers on furloughs, eight have cut pay, six have imposed layoffs, and six have closed courtrooms to save money in the face of state funding cuts, even as the number of legal cases is rising. . . .").

[113] David Berman, *Crossing Guards, Parents Worry About Kids*, Chillicothe Gazette (Chillicothe, Ohio), August 30, 2010; Peggy Cassidy, *Be Kind to Your Soon-To-Be Laid Off Crossing Guard*, NBCChicago.com, June 9, 2009; Brock Parker, *Arlington Crossing Gaurds Protest Layoffs,* The Boston Globe*,* April 18, 2010; Christopher Ramirez, *Northfield Crossing-Guard Cuts Upset Parents*, Press of Atlantic City, April 13, 2010.

DRAFT

term risks and headaches. Legal counsel for title insurance companies in particular would seem well advised to counsel their clients on the need to adjust insurance underwriting to reflect potential exposure to MERS liability. Refusing to insure MERS loans would perhaps be too drastic a step and would clog up the liquidity of the housing market. But, charging a steeper premium to reflect the real and growing risks associated with MERS' purported ownership makes sense.

Communities around the country have elected and hired county recorders to act as their custodian of property rights. Those recorders who agree the MERS system poses a threat to real property records have an obligation arising from their office to reclaim and restore faith in land title records. While some individual county recorders may reasonably feel reluctant to take on a powerful national system backed by some of the nation's largest financial institutions, this is precisely what they were hired to do. If county recorders do not protect county real property records, who will? A pathway to reclaiming authority over real property records could involve joining with other recorders to raise a unified voice. State and national county recorder trade associations could have a significant impact on pending cases by submitting *amicus curiae* briefs. Courts are likely to respect county recorders' expertise in maintaining and preserving transparent records, both because of recorders' experience but also because of their democratic mandate. Even more to the point, county recorders should consider appealing to the courts directly to stop financial institutions from recording false documents. In lawsuits to recover unpaid recording fees counties could hire private counsel on contingent fee agreements that would place no financial burden county taxpayers.

The more hesitant recorders will hold up the New York Court of Appeals decision in *MERSCORP v. Romaine* as an argument for inaction.[114] In that case, the clerk of Suffolk County, New York obtained an opinion from the Attorney General of New York stating that the MERS system illegally circumvented New York's real property recording statute.[115] Based on this opinion, Suffolk County began refusing to accept MERS documents for recording.[116] MERS sued and the case was appealed up to the highest court in New York on an expedited basis.[117] In a split decision, the New York Court of Appeals sided with MERS holding that the Suffolk County clerk did not have the statutory authority to refuse to accept documents for recording.[118]

Although MERS succeeded in forcing Suffolk County to accept MERS documents, the scope of the Romaine decision is actually quite narrow. The case merely holds that county recorders, as ministerial officers, are not empowered to decide which documents to accept.[119] As a concurring opinion explicitly points out, the decision saved for another day all of the other pressing questions including whether MERS recorded documents actually provide valid notice under New York

---

[114] MERSCORP v. Romaine, 8 N.Y.3d 90, 861 N.E.2d 81 (N.Y. 2006).
[115] *Id.* at 84.
[116] *Id.*
[117] *Id.*
[118] *Id.* at 85.
[119] *Id.*

Law and whether mortgages can be severed from notes.[120] The opinion also does not address—perhaps because the justices were unaware of it—MERS' highly questionable practice of pretending to have thousands of vice presidents all over the country. Moreover, the final appeal was decided in 2006 at a time when the mortgage industry still appeared to by flying high. It is far from clear whether the outcome of the case would have been the same had it been decided a year or two later. Other state supreme courts will address this issue *de novo*, and may very well view the New York decision with the critical eyes of hindsight. Ultimately, Chief Judge Kaye's prescient dissenting opinion may prove more persuasive:

> The lack of disclosure may create substantial difficulty when a homeowner wishes to negotiate the terms of his or her mortgage or enforce a legal right against the mortgagee and is unable to learn the mortgagee's identity. Public records will no longer contain this information as, if it achieves the success it envisions, the MERS system will render the public record useless by masking beneficial ownership of mortgages and eliminating records of assignments altogether. Not only will this information deficit detract from the amount of public data accessible for research and monitoring of industry trends, but it may also function, perhaps unintentionally, to insulate a noteholder from liability, mask lender error and hide predatory lending practices.[121]

Especially in states such as Arkansas, Florida, Idaho, Kansas, Maine, and Missouri, where courts are already on record taking a dim view of the MERS system, a unified legal challenge by state county recorders would be a formidable blow to the long term prospects of the MERS system.

Even county recorders who are reluctant to enter into court battles can still exert a positive influence on the law by encouraging state legislators to explicitly reassert traditional principles of recording law. State legislators should at a minimum consider enacting explicit bans on the use of "nominees" to obscure actual economic ownership of interests in land from the land records. Legislatures could also require complete chain of title information prior to allowing home foreclosure—especially in non-judicial foreclosure states.[122] Moreover, state legislatures should consider legislation clarifying that a recording in the name of a nominee does not provide notice sufficient to perfect a mortgage or deed of trust within that state. This would empower a state's citizens with substantial negotiating leverage and—particularly in struggling states such as California, Florida, Nevada, and Ohio—inject tremendous new energy into financial institutions' thus far lackluster efforts to modify ill-advised loans.

---

[120] *Id.* at 85 ("I wish to note . . . that to the extent that the County and various amici argue that MERS has violated the clear prohibition against separating a lien from its debt and that MERS does not have standing to bring foreclosure actions, those issues remain for another day.") (Ciparick, J., concurring).
[121] *Id.* at 87.
[122] *Cf* Jackson v. Mortgage Elec. Registration Sys., Inc., 770 N.W.2d 487, 491 (Minn. 2009).

DRAFT

Moreover, it may be time for learned legal associations such as the American Law Institute and the National Conference of Commissioners on Uniform State Laws to develop model law assisting legislators in reasserting the need for as well as reforming public land title records. Looking toward the future, states need to create modern, uniform standards to facilitate efficient electronic recording without jettisoning democratic government control of this vital infrastructure. In particular, ALI and NCCUSL should at least consider the possibility of a new article of the Uniform Commercial Code dedicated to mortgage loans. Such an article is long overdue, might actually be possible to pass in the wake of this crisis, and would emphatically reassert the influence of these organizations in the wake of the disappointing reception of the revised Article Two on sales law.

Finally, the nation's judges should recognize that, despite crushing caseloads, mortgage foreclosure cases are no longer routine matters. Putting the short term consequences of enforcing the law to the side, surely jurists will know that ratifying a security agreement which does not specify a true grantee—when never authorized by state legislatures or Congress to do so—is poor lawmaking. Perhaps we should not be too surprised that the mortgage finance industry's bacchanal of "pump-and-dump" mortgage origination happened to coincide with a bizarre and unsustainable theory of land title ownership. But, ratifying a standard industry practice of conveying rights to realty without specifying a true grantee will inevitably cause hidden liens, cases of exposure to double liability, and fraud. It will introduce long term systemic instability, raise the cost of and uncertainly surrounding title insurance, and result in future business and individuals investing in land, only later to discover that they receive nothing. Just as the Federal Reserve Board of Governors treated our largest financial institutions as "too big to fail," our courts might be tempted to capitulate to a silly but nonetheless "too incredible not to believe" interpretation of the law. Decisions that allow security agreements that do not specify the identity of the actual mortgagee would be in a sense, only the latest judicial version of a mortgage banker bail out policy. But unlike the other two branches of government, the greatest asset of an independent judiciary is its willingness to uphold the rule of law, rather than second guess the consequences of doing so.

V. CONCLUSION

This essay has analyzed the still unfolding implications of the dual role claimed by the Mortgage Electronic Registration System in home mortgages and deeds of trust. On the one hand MERS asserts that it is solely a nominee of the lender. But on the other hand, MERS claims that it is a mortgagee or deed of trust beneficiary. Taking the former view, a growing line of cases has asserted that MERS is not in fact a mortgagee or deed of trust beneficiary, but has a limited form of agency. This is almost certainly the correct view given that MERS lacks of any economic interest in the mortgages and deeds of trust it claims to own. And yet, the consequences of this view, and the two-faced security agreements that underlie it, are still yet to be fully seen.

The name of MERS, a company that does not actually own any interests in land, increasingly inserts inert gaps in county recorder grantor-grantee indexes that disseminate the chain of title to millions of homes. This growing separation between actual ownership and legally recognized public notice is likely to significantly undermine the usefulness of real property recording systems over the long term. Moreover, courts have held traditionally held that a security agreement that fails to name a mortgagee is void. Because MERS is not really a mortgagee, financial institutions are, in effect, asking that courts treat lenders and their assigns as mortgagees even though their own security agreements do not. Even if courts reform void security agreements into equitable mortgages, the resulting litigation is likely to pose significant challenges for financial institutions seeking to foreclose, obtain deficiency judgments, and petition of relief from the bankruptcy law's automatic stay. Furthermore, this inconsistent position taken by financial institutions in order to avoid paying modest fees to county recorders has the potential to be challenged. Many counties rely on fees from mortgage and deed of trust assignments to fund the vital services they provide to their communities. Courts that take offense at this use of tens of thousands of uncompensated "vice presidents" could equitably estopp financial institutions from denying liability for unpaid recording fees. Looking toward the future of American mortgage finance, counsel for financial institutions need advise their clients on the real and growing risks associated with using the MERS system. County recorders, state legislatures, and the judiciary each need to do their part to restore confidence, stability, and transparency in public land title records.

While the MERS system may reflect Janus in its two-faced land title theory, a demystified narrative of the company is actually more penetrably simple. Hubris was the essential theme in Greco-Roman mythic tragedies and was the vital sin of figures like Icarus, Narcissus, Andromeda, Niobe, Arachne, and Ulysses. Each found tragedy after their overweening pride showed disrespect to deity and the basic values those deities embodied. MERS and its members believed that they could rewrite property law without a democratic mandate. Although our myths have changed, many of our court houses and capital buildings continue to this day to bear resemblance to Greek and Roman temples as homage to the values of humility and respect for the rule of law. The unfolding drama of the MERS system will tell us much about whether those values endure.

DRAFT