

# Advisory on Risks in Mortgage Backed Securities Dependent on MERS

SEIU Capital Stewardship Program

February 2011

Contact: Gary Steinberg, SEIU Capital Stewardship Program  
[gary.steinberg@seiu.org](mailto:gary.steinberg@seiu.org) 202-730-7409

To: Pension Fund Trustees, Staff, Interested Parties

From: SEIU Capital Stewardship Program

## RECOMMENDATION

SEIU Capital Stewardship Program recommends that pension funds adopt a policy prohibiting their investment managers from purchasing securities dependent on MERS / Mortgage Electronic Registration System.

## DISCUSSION

We are providing this information to help funds avoid investments in potentially defective mortgage backed securities (MBS) – including products where most of the underlying mortgages may not actually be owned by the seller. The specific risks discussed in this memo occur in securities dependent on a new mortgage recording system: MERS / Mortgage Electronic Registration System.<sup>i</sup>

MERS was designed by the mortgage banking industry and includes about 60% of U.S. residential mortgages. MERS was developed to help grow the mortgage backed security industry by avoiding the time and costs required to record transactions using traditional county level systems. MERS typically files once at the county level to get a mortgage into its system, and then skips county level recording for additional transactions.

The MERS business model and corporate structure<sup>ii</sup>, including bypassing the county systems, create risks that securities dependent on MERS may be subject to legal challenges to establish ownership (including chain of title) and/or recover monies important for funding local government services. Recent developments that illustrate these risks include:

- Legal decisions -- including state supreme courts in Arkansas, Kansas, Maine; Missouri court of appeals; NY Federal Bankruptcy Court<sup>iii</sup> -- have found in individual foreclosure and bankruptcy cases that security agreements dependent on MERS are legally void, including MERS lacks legal standing to foreclose or transfer mortgages. Applying these precedents to pooled securities would mean investors bought unsecured loans and/or loans not actually owned by the seller.
- Congress has considered legislation "To prohibit Fannie Mae, Freddie Mac, and Ginnie Mae from owning or guaranteeing any mortgage that is assigned to the Mortgage Electronic Registration Systems or for which MERS is the mortgagee of record." (H.R. 6460 – Transparency and Security in Mortgage Registration Act.)
- Lawsuits have been filed against MERS on behalf of county government recording offices. The suits seek recovery of fees and payment of damages based on false claims and/or unjust enrichment. One suit alleges that MERS owes California a potential \$60 billion to \$120 billion. ("Mortgage database's murky legal status adds another wrinkle to foreclosure mess", LA Times 10-21-10)

It is also worth noting that the failure of MERS (and the banks and other corporations which are its “members”) to provide a definitive, transparent, readily available record of who actually owns a mortgage creates large risks for individual homeowners. People seeking to renegotiate their mortgage or enforce their legal rights during foreclosure, for example, may be prevented from doing so because this information is not available to them at a time of critical need. In addition to protecting their investments, pension funds may want to avoid supporting the MERS business model to avoid harming the interests of individual fund participants and their communities.

Thank you for your attention to this information, and please let us know if we can be of further assistance.

Attachments:

1. “How the mortgage clearinghouse MERS became a villain in the foreclosure mess”, Washington Post 1-1-11
2. Testimony of Christopher L. Peterson, Associate Dean for Academic Affairs and Professor of Law, University of Utah, S.J. Quinney College of Law before the US House of Representatives Committee on the Judiciary, hearing on “Foreclosed Justice: Causes and Effects of the Foreclosure Crisis”.

---

<sup>i</sup> Mortgage Electronic Registration System or MERS. According to its website: “MERS is an innovative process that simplifies the way mortgage ownership and servicing rights are originated, sold and tracked. Created by the real estate industry, MERS eliminates the need to prepare and record assignments when trading residential and commercial mortgage loans.” And: “MERS acts as nominee in the county land records for the lender and servicer. Any loan registered on the MERS System is inoculated against future assignments because MERS remains the nominal mortgagee no matter how many times servicing is traded.” The MERS “process” includes Mortgage Electronic Registration Systems, Inc., a corporation whose members are other corporations in the mortgage industry; and the affiliated Merscorp which maintains the database of mortgages and loans.

<sup>ii</sup> Problems with MERS include that it must make false statements in documents in order to execute its business model. For example, per end-note one, MERS takes the legally problematic position of claiming to simultaneously own (or pretend to own) a mortgage while also acting as an agent for the actual owner. A number of courts have found that in fact MERS is not a deed of trust mortgagee or beneficiary. Another example: MERS routinely designates people employed and paid by other corporations -- not MERS – as MERS “vice presidents” in order to process more transactions and attempt to satisfy state laws regarding who is legally authorized to sign documents. Designating these people as “VPs” is done by completing a form downloaded from the MERS website, and has been a major factor in the “robo-signer” problem.

<sup>iii</sup> Court Cases:

- a. Arkansas. Mortgage Elec. Registration System, Inc. v. Southwest Homes of Arkansas, 2009 Ark. 152, 301 S.W.3d 1 (Ark. 2009);
- b. Kansas. Landmark Nat. Bank v. Kesler, 216 P3d 158, 169 (Kan. 2009);
- c. Maine. MERS, Inc. v. Saunders, Slip op. 2010 ME 79 (August 12, 2010);
- d. Missouri. Bellistri v. Ocwen Loan Servicing, LLC, 284 S.W.3d 619 (Mo.App.ED., 2009)
- e. New York. In re Agard, 10-77338, U.S. Bankruptcy Court, Eastern District of NY Central Islip. Judge Robert E. Grossman: “MERS’s position that it can be both the mortgagee and an agent of the mortgagee is absurd, at best.” Bloomberg 2-14-11: “Merscorp Lacks Right to Transfer Mortgages”

