ACREL News

President's Message

Sleigh Bells ring! Are you listening?

As the holidays fill my thoughts and days, I offer to all of you and your families my very best wishes for happy times with those you love and a prosperous 2012.

Looking ahead to 2012, I know ACREL is in good hands with Ann Saegert at the helm and a terrific team of officers to share the load.

Cast Your Ballots

It's time to vote on the 2012 Class of ACREL candidates. The Member Selection Committee has processed the applications for 41candidates from 22 states and the District of Columbia. I urge you to visit the ACREL website by clicking here http://www.acrel.org/Private/OnlineVoting/default.aspx?PageID=35 to cast your votes.

Building the ACREL of the Future

Speaking of nominating new Fellows, I want to share with you a concern I have about ACREL's future.

ACREL now is a very healthy organization. We currently have 954 members, and the attendance at our meetings has continued to be strong, notwithstanding the seemingly interminable market slump. Our membership count has been like the pre-crash view of housing prices: it only goes up and it couldn't go down, right?

Well, that may be our history, but will that continue in our future? Maybe it will continue to be true, but making it true requires that you personally take action to identify and recruit the new ACREL Fellows of tomorrow.

Here are some statistics to help explain my concern:

57% of our 954 Fellows will be 60 or older by the end of this year. That is 57% of our membership. Keep that number in mind.

37% will be between 51-59 by the end of this year.

So, by the end of 2011, those 51 or older will total 94% of our membership.

Only 56 Fellows will be 50 or younger by the end of this year. That is only 6% of our total.

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And the average age of new Fellows admitted since 2007 is 55.

Now, again, we don't have an impending doom scenario, and we continue to receive nominations for truly strong candidates that demonstrate the characteristics we value in ACREL Fellows. But, ask yourself, have I nominated or seconded a nomination in the last few years? What have I done to spread the word about ACREL in my community or among lawyers I work with across the country, on deals or in professional organizations, or even in my own law firm? What have I done to encourage a speaker at a CLE event who is doing a terrific job to think in terms of building a resume that will support a nomination to ACREL?

If each of us thinks in terms of, at a minimum, recruiting one new Fellow, preferably one who will come to our meetings and be an active contributor to ACREL, the future of ACREL will be assured. Just one worthy new Fellow, before you even think about retiring. That is a very attainable goal.

If you need a refresher on our admission criteria, look to your Directory. In fact, I suggest you look to your Directory even if you think you don't need a refresher. I am sure you all keep that handy on your desks. It includes many resources to help you submit a successful nomination, such as the selection rules embodied in the Bylaws, the Guidelines for Member Selection and Commentary on the Guidelines. Also, you always can reach out to our Member Development Committee, which will be chaired by Roger Winston in 2012, or to any other member of that committee, with your questions about our admission standards and how you can best help to groom a prospective nominee. When you take the time to invest in making a nomination, we want to do all we can to help make it successful.

ACREL Materials Online

In addition to the hard copy books and CDs that Fellows receive at ACREL meetings, registrants also may access the materials online. Meeting registrants receive a link to materials at the meeting, and it is printed in the hard copy materials. 15 months after each meeting, materials are available online through the ACREL website. While ACREL continues to provide hard copy materials, as you know, many CLE providers no longer do so. Please let the Programs Committee know your preferences: do you prefer just the CD or online access?

Do You Use SharePoint?

Under the energetic and very capable leadership of Gordon Tanner, ACREL is conducting a beta test of the SharePoint software program. For those not yet familiar with SharePoint, it's a collaboration tool which promises to make it easier for Fellows to communicate and participate in ACREL. We especially see potential for SharePoint to facilitate more active involvement in committee projects by ACREL Fellows who are not able to attend all of the ACREL meetings.

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STAFF BOX

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A group from the Leasing Committee has been quite enthusiastic about the SharePoint program, so stay tuned for more developments. In the meantime, if you already use SharePoint, please reach out to Gordon to share your tips for maximizing the benefits of this tool.

Survey on Meetings Coming Soon

ACREL meetings continue to have strong attendance, and we receive great feedback about the educational and other aspects of the meetings. The attendance at our Philadelphia meeting in October was among the highest we have enjoyed, and we have a dedicated group of about 200 Fellows who attend pretty much every meeting.

At the same time, we always seek to improve the meetings "experience" and to implement adjustments that are responsive to the needs and preferences of Fellows and their guests. Towards that end of continual improvement, the Meetings Committee will be conducting a survey of Fellows concerning our meetings. You can expect the survey in your Inbox in January.

Mark Your Calendar for Upcoming Webinars

In 2010, we had 6 webinars. In 2011, we have had 8, all with ALI-ABA, and we had our first webinar with the Mortgage Bankers Association on December 15. The MBA program is a new direction and we are very excited to add this new avenue for distribution. There are 2 or 3 additional webinar topics in the hopper right now. Again, your ideas for webinars are always welcome. The arrangements with ALI-ABA and with the Mortgage Bankers Association provide us with an opportunity to expand our outreach efforts, by bringing ACREL to a broader audience, and also allow us to achieve revenue beyond our sponsorship funding.

Update on Local Meetings

Local meetings are cropping up all over. This year there have been 8. Have you been to one yet?

Alvin Katz and Ken Jacobson hosted a well-attended meeting in Chicago on December 7. Hosted by Katten Muchin, this lively event attracted 24 Fellows from Illinois. Many of those at the party have not been to a meeting recently, so, as often is the case with our local meetings, it was a great chance to share information about ACREL news and priorities, such as recruiting candidates for ACREL.

Trev Peterson and Angela Christy of the Orientation and Integration Committee are your "go to" contacts for tips on organizing a local meeting, and Jill and Henri also can help in coordinating the scheduling. While we do appreciate the generosity of some of our Fellows' firms in sponsoring, that is not necessary; most of the local meetings are "pay as you go." Some even meet in private homes, as was the case with the meeting that took place in Mark Senn's home in November. Eleven Colorado members attended, including the host.

And Now a Word About Our Sponsors

ACREL has a loyal group of sponsors whose donations to ACREL support our Directory each year. The sponsors for 2012 include:

Chicago Title Insurance Company
Commonwealth Land Title Insurance Company
Fidelity National Title Insurance Company
First American Title Insurance Company
Stewart Title Guaranty Company

Please keep our sponsors in mind as you seek title insurance and similar services and let them know you appreciate their support.

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Can't Thank You Enough!

The generosity and energy of ACREL Fellows inspires me. We have a long, long list of administrative and substantive committees, task forces and working groups, plus subsets of many of them. As I have asked ACREL Fellows to take on responsibility for yet another ACREL project (and I have asked scores of them), the response is overwhelmingly positive and the productivity is amazing.

Then there are the speakers and authors, who bring to ACREL cutting-edge CLE that is second to none. And, of course, consistent with the mission and spirit of ACREL, the lawyers who provide CLE and work so hard for ACREL Fellows are also serving the profession and the public through volunteer service for state and local bar associations and other first-rate CLE providers.

To each of you who has served ACREL in 2011, please accept my sincere "thank you!"

It has been a humbling experience for me to serve ACREL. I thank you for the opportunity, and look forward to seeing you all at the Spring meeting in Las Vegas.

Las Vegas, Here We Come!

The Programs Committee and the Meetings Committee are putting the finishing touches on plans for the ACREL meeting in Las Vegas March 8 to 11. We have a great room rate for this meeting, the same as the rate for our 2003 meeting in Las Vegas. I hope you have this on your calendar already. Registration materials will be coming your way in early January. ■

ACRELades

Thomas C. Barbuti, A. Hugo Blankingship, Jr., Douglas M. Bregman, Timothy D.A. Chriss, Raymond J. Diaz, Maureen E. Dwyer, Jeffrey R. Dwyer, Jay A. Epstien, Morton P. Fisher, Jr., David H. Fishman, Joseph M. Fries, Michael D. Goodwin, Robert G. Gottlieb, Jan K. Guben, Nancy Haas, John D. Hagner, Thomas A. Hauser, Philip M. Horowitz, Frederic L. Klein, David M. Kochanski, Edward J. Levin, Searle E. Mitnick, Richard A. Newman, Barry P. Rosenthal, Pamela V. Rothenberg, Linda D. Schwartz, Kevin L. Shepherd, Lawrence A. Shulman, Raymond G. Truitt, Stefan F. Tucker, Keith J. Willner, Roger D. Winston, Fred Wolf III, and **James D. Wright** were all recognized as Washington/Baltimore's Best Lawyers 2012 edition.

John W. Daniels, Jr. will be honored in February 2012 at the Spirit of Excellence Awards luncheon by the ABA Commission on Racial and Ethnic Diversity in the Profession.

Norman W. Gutmacher was named the Best Lawyers' 2012 Cleveland Real Estate Law Lawyer of the Year. Only a single lawyer in each specialty in each community receives this distinction.

Jesse S. Ishikawa was named one of Reinhart's Pro Bono Attorneys of the Year. The award is presented annually to recognize the efforts of attorneys who demonstrate commitment to pro bono work.

Charles A. Parsons, Jr. was named to Chambers USA for 2011. It is the fifth consecutive year in which he has been recognized as a "leader in his field." ■

Moving Beyond the Mistakes of MERS to Have A Secure and Profitable National Title System

*by Adam Leitman Bailey and Dov Treiman**

In Homer's Odyssey, the protagonist, Odysseus, is called upon to sail his crew through the Straits of Messina, passing between two legendary monsters, Scylla and Charibdis. To avoid one, the only option was to approach the other, risking a horrible death in either instance. Odysseus was at times a wise captain and managed to minimize the number of deaths, if not avoid them altogether.

Most of the nation is, thanks to the still writhing tendrils of the economic collapse of 2008, part of the larger real estate crisis setting forth the Scylla of further economic collapse by making the foreclosure procedure so difficult for banks that they refuse to issue residential mortgages at all or the Charibdis of wholesale ejection of homeowners from houses they should not have purchased. Tightening the foreclosure rules threatens economic destruction from the top down; loosening them threatens that destruction from the bottom up.

There can be no doubt that any action taken, including complete inaction, threatens to thrust enormous hardship on thousands, if not millions, of people. Exacerbating the problem, there is no one to captain the ship.

Understanding MERS

Although not the cause of the problem by any means, yet still at the heart of its mechanics, is the national "Mortgage Electronic Registration Systems," known as MERS. Operating near Washington, D.C., MERS is involved in nearly 60% of residential mortgage-like transactions nationally, with a registry entailing some 60 million residential mortgages. The authors and sponsors of this national system intended both to simplify and to centralize the tracking process of rights regarding each mortgage-like instrument.

MERS attempts to attain this centrality and uniformity despite the fact that states differ as to whether they have "mortgages" or "deeds of trust,"[1] on how such instruments are recorded, and as to what the remedies are to the promisee in the event of a default by the promissor. MERS's uniformity is further compromised by the fact that each of the 50 state highest courts must decide for itself, as must the federal system decide for itself, exactly what a MERS transaction means. Even Federal District courts sitting in different districts may, or may not, find their rulings influenced by the laws of the host states, depending on whether they find foreclosure rules to be essentially substantive or procedural in nature.[2]

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* Adam Leitman Bailey is the founding partner and Dov Treiman a partner of Adam Leitman Bailey, P.C.. The authors wish to thank Michael Brancheau for his research assistance with this article.

1 Mortgages are mere liens on land. Deeds of trust are actual conveyances of the land to a trustee who acts ostensibly on behalf of both the borrower and the lender, but in actual practice, acts on behalf of the lender in a foreclosure procedure that has no involvement in the court system. In states with the lien theory of mortgages, many have outlawed the non-judicial procedures such liens often allow and require that foreclosure be done exclusively under judicial supervision. Deeds of trust theory states are themselves inherently non-judicially based in their foreclosure procedures, but especially in light of the epidemic of foreclosures sweeping the nations, are finding more and more ways for courts to supervise these nonjudicial processes. While not a sure indicator of local practice, by and large states that started as British colonies tend to be mortgage states and those achieving statehood by Congressional declaration tend to be deed in trust states. This is part of the French and Spanish heritage of the younger states.

2 Since foreclosure proceedings always involve real property, the substantive rights are controlled by the substantive laws of the State or territory where the property is located, but federal procedural rules are uniform under the Federal Rules of Civil Procedure.

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Moving Beyond the Mistakes of MERS ...

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At the peak of MERS's popularity, although precise statistics varied amongst various states, some 50% of mortgages and deeds of trust written in some jurisdictions involved MERS.[3] In a non-MERS mortgage, there is a borrower-mortgagor and a lender-mortgagee.[4] In a non-MERS deed of trust, there is a borrower-grantor, a lender-beneficiary, and a trustee. The lender keeps the promissory note in its files and it or its title company records a copy of the mortgage or deed of trust in the county registry. In this scenario, the lender owns both the promissory note and the mortgage or deed of trust. The lender may sell both, but should keep them together.

In a MERS transaction, the lender still lends the money and the borrower still executes a promissory note in favor of the lender, but the borrower executes the mortgage or deed of trust in favor of or for the benefit of MERS, recorded in the county registry as the bank's so-called nominee. MERS neither does the recording itself nor has physical possession of the mortgage, deed of trust, or promissory note.[5]However, the lender, known as an "originator," sells the note and, at times, informs MERS of the sale.[6] MERS is available to transfer the mortgage or rights under the deed of trust to the vendee of the note, should it become an issue. If such a transfer does become necessary, MERS sells its subscribers a vice-presidency in MERS to effect the transfer. MERS transfers nothing itself. If a subscriber requests it to do so, MERS just makes entries in its database.

Nationally, there are well over 3,000 recording offices, but only one MERS. Non-MERS records across the nation are located generally in county recording offices with considerably varying rules about how the recording is to take place.[7] Although the governmental recording fees are considerably modest compared to the monies involved in the transactions the mortgages are securing, MERS vastly cuts into these fees as its members pass mortgages among themselves as relay race batons, thus depriving government and saving the banking industry roughly $1 billion since the initiation of MERS. Probably with considerable justification, local governments have bitterly complained about this loss of income and point out that recording fees were a way of funding governmental programs having nothing to do with the recording process. It was, prior to MERS, in essence, a real property tax most

3 As some major banks are leaving MERS, the number of new MERS mortgages issued annually appears to be decreasing. While the raw count is indeed undeniably going down, any reasonable analysis of these figures would require adjusting the meaning of these numbers to reflect the decrease in mortgage issuance generally as a result of the still faltering national economy.

4 It is important to realize that the legal nomenclature of mortgagor-mortgagee runs exactly opposite to the common understanding. In common understanding, one "gets a mortgage." However, what one is really getting is a "loan secured by a mortgage." Otherwise put, one is getting money and putting one's house up as collateral to repay it. The document that makes the house the collateral is the "mortgage" and therefore legally one gets money and gives a mortgage.

5 Early drafts of the proposal that became MERS called for it to be the depository of the mortgages and notes as well. However, that idea was abandoned as it became apparent that the other core idea of MERS, that it be cheap to create, maintain, and operate, would be sacrificed by making it contain millions of file cabinets.

6 Nothing except paying MERS its fees is mandatory in the MERS world.

7 Numerous observers have called for the elimination of county-based recording in favor of state-based recording. The county system was originally founded on the idea that land records should be available to anyone with an interest within a single day's horse ride within the jurisdiction where the records are found. That theory is ridiculous under modern transportation systems, unnecessary in light of the ubiquity of the internet, and contrary to actual fact where the more sparsely populated counties of the American West and Alaska can run to vastly more square mileage than the horse theory would allow. North Slope County in Alaska's land area is 89,000 square miles. 40 states of the Union are smaller than that. By contrast, New York County in New York is 36 square miles, including water. Still other observers have called for national land record recording.

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heavily imposed on those most well off, but actually used as general revenue of local and State government.[8]

Further, the MERS system hides from borrowers the history of their mortgages. While some states have systems like New York City's ACRIS[9] system to make fully indexed land records readily available and searchable to anyone with an internet connection, MERS does not allow non-members access to any of its records.[10] MERS ensures that borrowers know nothing beyond to whom they should be sending their check. Furthermore, when there are errors in MERS and the same mortgage gets assigned to more than one financial institution, the homeowner has no way of figuring out who actually has the superior right without resorting to the court system, which itself may not be able to untangle the MERS threads.

There are current calls to replace the 3,000 office system with something both national in scope and governmental in administration. While such a system remains beyond the horizon, calls in some states to have single statewide systems are becoming more urgent. But, for now, that part of the crisis remains in stasis.

Attacks on MERS

In a case of New York's first impression, *Bank of New York v. Silverberg*[11], ruled that since MERS never was either the owner of Mr. Silverberg's promissory note nor ever had physical possession of it, MERS had no assignable interest in the mortgage in its favor as "nominee" and therefore its assignment to Bank of New York was void. With that assignment void, the court found Bank of New York to lack "standing" to bring a foreclosure action.

In 2006, the Silverbergs had executed a mortgage in favor of MERS with an underlying note in favor of originating bank, Countrywide Home Loans. In 2007, they executed a second, similar set of documents, together with a consolidation agreement to which Countrywide was not a party. When the Silverbergs defaulted on this later agreement, MERS assigned the consolidation agreement to Bank of New York who brought a foreclosure action.

Since the court found that MERS lacked physical possession of the note or an assignment of it, it also lacked the authority to assign the consolidation agreement, and the court found the bank lacked "standing" to bring a foreclosure action. "Physical possession" is key, it being sufficient to establish ownership – rather like cash.[12]

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8 Several attorneys general from cash starved States are suing MERS to recover the lost funds or prevent further losses.

9 ACRIS stands for "Automated City Register Information System" and can have its name explained by the observation that in New York City, its City Register instead of its county clerks keep the land records. This no doubt owes its origins to the fact that five counties comprise New York City.

10 Most of New York State does not have the ACRIS-like internet friendly and fully searchable land records of New York City based ACRIS. For many New York State counties, computer based searches are available, but researchers must make the trip to the county clerk's office to access the computer system. In some of New York State's more farming based counties, the records are still nearly entirely exclusively on paper.

11 86 A.D.3d 274, 926 N.Y.S.2d 532, (N.Y.A.D. 2 Dept. 2011).

12 Levy v. Louvre Realty Co., 222 N.Y. 14, 20 (1917); Curtis v. Moore, 152 N.Y. 159, 162, Strause v. Josephthal, 77 N.Y. 622 (1879); Fryer v. Rockefeller, 63 N.Y. 268, 276 (1875).

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Under established doctrine, not only in New York, but in all United States jurisdictions recognizing mortgages,[13] separate ownership of a mortgage and note voids the mortgage.[14] However, in MERS transactions, we see that the mortgagee, MERS, was *never* the lender and was *never* the promisee on the promissory note. Thus, it could well be argued that MERS mortgages are not mortgages at all, but are, at most, unsecured monetary loans to the borrower. In *Matter of MERSCORP, Inc. v. Romaine*,[15] New York's high court determined that the Suffolk County Clerk did not have the discretion to refuse to record MERS mortgages, but never really addressed the question as to whether a MERS mortgage is indeed a mortgage at all. It merely held that the county clerk was obliged to record everything that looks like a mortgage and left unresolved whether MERS's mortgage-lookalikes really were enforceable mortgages. While a finding that a MERS mortgage is no mortgage at all does not, in theory, deprive the bank of all remedies, it does mean that the judgment a bank would acquire for nonpayment of the loan would not necessarily have any particular seniority as a lien against the promisor's real property. It may be so far down in the priorities of pure seniority that it may be completely unenforceable as a practical matter.

Yet another level of complexity is added when one realizes that a vast amount of MERS loans originated during the housing boom, a period in which the banks were extremely sloppy about keeping track of the original promissory notes. This got sloppier still among the banks that failed. For banks seeking to foreclose on these housing bubble mortgages, *Silverberg* adds additional procedural and evidentiary hurdles to overcome to make sure that they can prove possession or ownership of the note underlying the mortgage prior to the commencement of the foreclosure action. In the case of the failed banks, this might include the daunting task of following the paper trail from one bank to the next to find the current owner of the note. However, fears that *Silverberg* ended the world are vastly overstated.

National Reaction

While *Silverberg* was a case of first impression in New York, other jurisdictions across the country had earlier cases that no doubt influenced the New York decision.

Similar rulings against MERS had come down across the country. For example, the Michigan Court of Appeals held in *Residential Funding Co. v. Saurman*[16] that MERS cannot foreclose by advertisement. In Michigan, the Foreclosure by means of Advertisement statute requires the party foreclosing the mortgage to either own or have an interest in the underlying debt that is secured by the mortgage. In this case, the Court found that MERS did not stand to receive any benefit from the debt being paid and did not have a financial interest in the note. As a result, the Court held that MERS did not meet Michigan's statutory requirements as a party either owning or having an interest in the debt. Thus, MERS could not foreclose by advertisement. The court did not address the issue of whether MERS would be able to foreclose in a judicial proceeding.

13 Those jurisdictions who do not recognize mortgages have "deeds of trust" instead where the property owner and the lender appoint a third party trustee to transfer the property nonjudicially in the event of default. That system has received many complaints as a thinly disguised consumer fraud and there are calls in some "deed of trust" jurisdictions to shift over to mortgages where courts can and do supervise the process. Less radical solutions than adopting the mortgage model are finding acceptance nationwide as legislation is coming on line to bring judicial supervision to the foreclosure process in deeds of trust.

14 Carpenter v. Longan, 83 US 271 (1872).

15 8 NY3d 90 (2006).

16 Residential Funding Co. v. Saurman, —— N.W.2d ——, 2011 Mich.App. LEXIS 719 (Mich.Ct.App. Apr. 21, 2011).

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Likewise, in *Landmark National Bank v. Kesler,*[17] the Supreme Court of Kansas affirmed the lower court's ruling that MERS was not a necessary party to a foreclosure in which MERS was designated the nominee-mortgagee for the lender. As in Michigan, the Supreme Court of Kansas determined that MERS did not have any ownership interest in the underlying debt and, therefore, did not have any right to enforce the mortgage. In fact, the Court noted that, in a different jurisdiction[18], MERS had previously argued that it was *not* allowed to enforce the mortgage. Therefore, as a simple nominee-mortgagee, MERS was not a necessary party in the Kansas foreclosure proceeding.

In the most definitive stand against MERS prior to *Silverberg*, the Maine Supreme Judicial Court[19] had held that MERS lacks standing to institute a foreclosure through judicial proceedings. In this case, the mortgage defined MERS as a nominee. The Court found that, in its limited role as nominee, MERS did not have possession of the note or any interest in the debt obligation. The Court held that MERS did not qualify as a mortgagee and lacked the standing required to institute a foreclosure proceeding.

Favorable Decisions to MERS

However, not all states had taken a position against MERS, most notably perhaps, the state of Minnesota. In 2008, Minnesota amended its Recording Act to broaden the authority of nominees. The amendment, commonly referred to as "the MERS statute," allows nominees to record "[a]n assignment, satisfaction, release, or power of attorney to foreclose."[20] Clearly, Minnesota has recognized, for the purposes of recording, MERS's operations as acceptable.

Minnesota's favorable position towards MERS is further detailed in *Jackson v. MERS*[21] where the court had to determine whether a MERS member was required to record the assignment of a promissory note before MERS could commence a foreclosure by advertisement.

Notwithstanding Minnesota's statutory recognition of MERS's authority to record, Minnesota's foreclosure by advertisement statutes require certain assignments to be recorded. The Court had to decide whether the assignment of a promissory note was included in the statutory requirements. The Minnesota Supreme Court found that the assignment of a promissory note was not included and, therefore, held that MERS Members did not have to record a promissory note assignment before MERS could commence a foreclosure by advertisement.

In a 2011 California case[22] in which the borrower challenged MERS's ability, as nominee, to assign the promissory note to the foreclosing party, the California Court of Appeal for the Second District held that, where a deed of trust allows MERS to act on behalf of the lender, MERS has the authority to assign the promissory note. The Court noted that California law regarding nonjudicial foreclosure does not require possession of the note under a deed of trust. This, of course, is the California common law on deeds of trust and is thus clearly distinct from the previously cited national common law on true mortgages.

17 Landmark National Bank v. Kesler, 289 Kan. 528, 216 P.3d 158 (2009).
18 MERS v. Nebraska Department of Banking and Finance, 270 Neb 529; 704 NW2d 784 (2005).
19 MERS v. Saunders, 2 A.3d 289, 295 (Me. 2010).
20 Minn. Stat. § 507.413(a).
21 Jackson v. MERS, 770 NW2d 487, 498 (Minn 2009).
22 Ferguson v. Avelo Mortgage LLC, 195 Cal.App.4th 1618, 126 Cal.Rptr.3d 586 (2011) (as modified on June 20, 2011).

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MERS Reaction

However, seated in the national capital of the financial industry, New York's courts' influence on the national home financing industry is substantially in excess of New York's percentage of the national land area, national population, or even national financial transactions.

So, when New York spoke through *Silverberg*, MERS certainly listened.

On July 22, 2011, MERS officially revoked the authority granted to its Member's Certifying Officers to initiate foreclosures in MERS's name. MERS effectively rescinded the authority of the Certifying Officers through an amendment to Rule 8 of its "Rules of Membership." Rule 8, entitled "Required Assignments for Foreclosure and Bankruptcy", outlines the new steps a Member must take to initiate a foreclosure proceeding. Mainly, the note owner must cause a Certifying Officer to assign the Security Instrument from MERS to the note owner's servicer. Further, the servicer must then record the assignment with the governmental recording office before any foreclosure proceeding can take place.

With the recent changes, members might find it particularly prudent also to become familiar with Rule 7, entitled "Disciplinary Actions". The amendment to Rule 8 provides that, as of September 1, 2011, Members could be sanctioned pursuant to Rule 7 for improper use of MERS's name in a foreclosure proceeding. According to Rule 7, sanctions range from removal as a Member to fines to "any other fitting requirements that may be determined by MERS."[23] Members have an opportunity to respond to the citation for violation and they receive thirty days to correct the violation. In regards to foreclosures, a MERS Member can avoid sanctions by withdrawing the filing of the proceeding within three weeks after bringing the action.

Close analysis of *Silverberg* raises questions whether these steps do anything to cure the infirmity in the MERS tainted transactions or whether these steps are more about trying to keep the *name* of MERS out of the names of cases more than anything else. If, as in *Silverberg*, it was the MERS involvement in the first place that made the mortgage unforeclosable, the courts may well find the MERS taint to be incurable. The question to be presented is simply this: Once a mortgage is impaired by having its ownership separated from the ownership of the note, can that tear in title be repaired by uniting the ownership of the two documents?

In the months leading up to the amendment, MERS had already begun taking steps to withdraw from the foreclosure process. MERS rapidly began to assign deeds of trust to banks that service loans or trustees that oversee mortgage pools. It is likely that some of this change can be attributed to the fact that Fannie Mae, Freddie Mac and other large lenders and loan servicers, such as JP Morgan Chase, had already ceased foreclosing in MERS's name.

The MERS rule changes should successfully remove MERS from the courtroom. However, MERS will not completely disappear from the foreclosure process. MERS will continue to assign the necessary mortgage documents to the various loan servicers and foreclosing parties.

23 MERSCORP, Inc. "Rules of Membership".

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Pending and Proposed Legislation

While the courts have not had major pronouncements after *Silverberg*, State legislatures are also examining the issues it raises. As the various statehouses across the nation see domination by the left and by the right, we can expect red state legislatures to step in, like Minnesota to create legal doctrines shoring up MERS mortgages and blue state legislatures like New York to codify the holdings in cases like *Silverberg*. This is precisely where the problems of Scylla and Charibdis lay.

New York, for example, is considering legislation that would go beyond *Silverberg* and make a homeowner's objection to MERS's involvement in the mortgage transaction an issue that the homeowner can raise far later than the normal deadlines in New York litigation. Some observers regard this legislation with considerable trepidation as it may have the effect of requiring a second suit after the foreclosure action. Moreover, and perhaps an even greater concern, is that the legislation, and its other lender-unfriendly provisions, may scare away lenders from offering mortgage financing on New York properties.

We hear alarm bells on both sides of the aisle: those who fear the economic devastation that could ensue from mass foreclosures and those who fear the economic devastation that could ensue from shutting down the mortgage financing industry. The likely result is that as state leigslatures are left free to forge their own solutions, precisely four categories of those solutions emerge: (1) doing nothing and letting the common law sort things out; (2) reinvigorating the procedures in favor of plaintiffs in foreclosure actions; (3) strengthening the defenses to foreclosure actions; (4) trading off new plaintiff strengths for newly strengthened defenses.

A plurality of states is likely to follow the first of these four courses. The other three will be hotly debated in a few states and will undoubtedly lead to enactments that will move America away from the two-theory stasis it currently has[24] to such a vast array of different variations on these theories, that practice in one state may well ill prepare lawyers for what they can expect to encounter in others. This will lead to multiplied costs to lenders who will need to have individual experts in each jurisdiction where they do business and, even without other factors, will contribute to a greater cost of credit to consumers. Clearly this is a result that benefits no one.

In analyzing any proposed legislation, we must realize that there are two broad categories of financing documents they address: documents issued prior to the passage of the legislation and those entered afterwards. As to the former, there can be constitutional constraints on how far the legislation can go. As to the latter, constraints will come from the marketplace as no State dares to pass legislation that is so lender unfriendly as effectively to require all land purchases in the State to be on a cash only basis.

Yet, in all of this, we need to recall that the entire crisis emerges not from the existence of the MERS system, but from its use. Lenders who use the classic recording methods for new transactions should find those deals as safe and secure as they have been for centuries. But the problem remains that they are simply too slow.[25] Even the MERS advantage of making a mortgage a freely transferable security for

24 The two theories being specifically (1) classic mortgages; and (2) deeds of trust.

25 We note, however, that many recording offices nationwide were under the classical system as much as two years behind in their classical method recording. In order to sustain the kind of vibrant mortgage market there was during the housing boom, classical recording methods would simply have to speed up to carry the load.

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investors can remain in place, provided only that the mortgage or deed in trust always be physically transferred along with the underlying note in each such transfer.

Federal Courts

Many foreclosing banks are already citizens of states other than the state where the property is located. This can trigger for them an entitlement to bring their foreclosure proceeding in federal district court rather than the state courts. Were a court to find the foreclosure law of the State where the property is located to be procedural rather than substantive, the answer for the bank to get a bullet proof foreclosure proceeding might be the simple expedient of starting it in federal court. Indeed, even if the bank is not already a noncitizen of the state where the property is located, it could sell the mortgage to another bank that is or create a bank of a new citizenship for the very purpose.[26]

An Outdated System

No one can seriously dispute that the land title recording system designed in the 1600's is now hopelessly behind the needs of the brisk hour by hour business of the 21st Century. The system is, by law, paper-based across the nation. Even the electronic records are principally photographs of pieces of paper. While optical character recognition technology – a computer reading a document and recognizing the contents as meaningful text in a specific language—has come an amazingly long way since the last quarter of the 20th Century, handwritten notes on real estate transactions remain completely indecipherable to computers. Therefore, as long as there are *any* handwritten notations on real estate records (other than the signature of the grantor and notary), the system remains essentially locked into paper and photographs of paper. And so long as the system is paper-based, electronic indexing would be limited to what the recording clerk sees or believes he or she sees printed on the document. The all-important description, being as it is heavily based on numbers, will continue, at least to some extent, to rely on the accuracy of a clerk transcribing those numbers. Thus, any contemplated upgrade of the system to 21st Century modernity would have to require, at a minimum, that the documents be presented to the recording office both as photographs of paper and as textual electronic files setting forth the contents of the documents as plain text that any computerized word processor could read.

More radical proposals include the elimination of the States' county recording offices and replacing them with single statewide registries. While there is merit to such a proposal, it must be noted that in most of those same recording offices also archive the judicial records that so largely impact on titles, not just judgments, but also things like probate files. The overhaul of the system of *all* of the documents affecting title to any statewide system would be a truly massive undertaking and a good many of *those* documents would indeed require that they be preserved, even in digital format, as mere photographs of paper.[27] We are therefore unprepared to endorse that radical a move in the short term.

26 A bank only has to have one sister bank of diverse citizenship in order to qualify for diversity of citizenship. One bank can handle 49 states and the other bank can handle the single state of which the first bank is a citizen.

27 Although not strictly a "photograph" of paper, we include within the scope of that phrase "pdf" files that are image based rather than text based. Although a 22nd Century system might be content to manipulate images, modern day computers have simply not come that far yet.

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Whatever 21st Century recording system there is, it must have certain characteristics in order to fix the problems that MERS was created to address and solve the problems that MERS created by its existence.[28]

Title records must once again become transparent. MERS creates an entry in the title records that is essentially a place holder and gives the researcher no clue as to who the real parties in interest are and therefore no one to contact with any problems or concerns.

The public has to be able to research title chains without having to pay some private company for its own proprietary records.

The system has to be thoroughly indexed, thoroughly indexable, and amenable to new inventions in indexing techniques. In a modern system, a deed from Leonardo da Vinci should be equally easy to find under "L," "D," or "V." Any truly modern system would automatically compare all instruments offered for recording and flag partial and total overlaps with previous instruments or intrinsic invalidity in the instrument itself.[29]

Creating Modern Systems

Land records should be available as a repository of copies not only of mortgages, but of their underlying promissory notes with legal incentives to the recording of both so as to eliminate the problem of lost paper. A change in substantive law declaring that a recorded assignment of the note and mortgage would serve as prima facie proof of the authority of the assignee with respect to both, would avoid much mischief—provided, as with every recorded instrument, that sufficient safeguards[30] against fraud were imposed as well.[31]

The fundamental flaw in MERS was always that it could come up with creative ways to work around the various laws, but it could never directly influence what those laws would be. If, for example, a legislature were simply to outlaw any MERS-like transactions in its State, all that MERS could do to prevent it would be to lobby. The State, however, is in a position to change the laws, at least for transactions inside the boundaries of that State. With computer storage space being so amazingly cheap nowadays – $100 for a trillion bytes on the open market – there is no amount of data that could be thrown at the recording offices that they would be unable to record in a timely manner, provided only that the data were given to them in pure electronic form, via some kind of upload. Having that data would enable the computerized recorders to index documents by every single word contained in them. While metes and bounds are in some circles regarded as themselves terribly outdated, a properly designed computer system would not only be able to process metes and bounds and compare them to other conveyances to find boundary conflicts,[32]

28 Tanya D. Marsh, Foreclosures and the Failure of the American Land Title Recording System, http://ssrn.com/abstract=1737857 (2011).

29 Truly modern systems would assign some kind of numerical identification tag to every square inch of the earth's surface, including three dimensional cubic inches when necessitated by condominium developments and other vertical conveyancing schemes. However, this article describes only the criteria such systems would need to meet, not how to meet them.

30 See, Bailey, Title Litigation: Expense of Theft Prevention Dwarfed by Cost of Fraud, NYLJ 4/8/09.

31 While beyond the scope of this article, it is worth observing that the current lax laws regarding notaries are themselves hopeless outdated and open invitations to fraud.

32 Modern systems would read metes and bounds descriptions to determine first whether the stated metes and bounds actually do enclose a valid geometrical figure or whether they reflect a surveying error. Truly modern systems would also check any metes and bounds description proffered against all previous ones in the system's database so as to flag overlaps and ascertain whether all or part of the property seemed to be outside of an existing chain of title.

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but would also be able to include any other kind of property identification system that could ever be invented, including section, block, and lot systems, the grantor/grantee system, and anything else.[33]

Private Industry Indexing

MERS was seen as an answer to both the "too slow" and the "too cumbersome," but any State could enact its own system that is neither and, by making the laws sufficiently MERS-unfriendly, could eliminate the other MERS motive, too expensive.[34] The State could decide for itself not only what the market can bear, but what it should.[35] However, in doing so, the State would have to consider the simple fact that institutional lenders are not the only ones to give mortgages. Folks selling their homes to those who cannot or will not get institutional financing also often take back mortgages. Any new law would also have to accommodate their needs. Even without new legislation, title companies can inform the purchaser's attorney that if MERS is involved, the mortgage will be excepted from the title insurance policy. Purchasers' attorneys would have to make sure that the contract of sale protects the purchaser against the consequences of such a refusal.

At the dawn of the 1980's, computers came in two categories: department store sized behemoths suited only for governmental and large corporate use and toys for hobbyists. Into this world quietly slipped the PC with its revolutionary idea of "open architecture," meaning that not only were the thousands of lines of computer code that operated these machines written in a way that any competent computer programmer could read them, but they were so written than any competent computer programmer *could* extend them and make the machine do things the original designer had never dreamed of. Most market analysts credit "open architecture" with the explosive growth of PC's, now numbering some one billion in the world at large. By contrast, our current land records are essentially a closed system. Title companies have invested millions of dollars into reading these documents and figuring out what they mean for title in this State. But with the kind of recording system we described above, all of the data would be instantly open architecture. Title companies could make untold billions of dollars by simply designing computer programs that would log on to the publicly published digital land records, read them, and index them in any variety of creative new ways that could, in effect, produce a rudimentary title report in a matter of seconds.

Obviously, creating a statewide system of uniform multiple electronic indexing input from transactional attorneys' desks would both save the State enormous funds and provide the public with a vastly more secure and useful title recording system. It cannot be denied that such a system would require substantial safeguards against fraud, things like a mechanism to alert overseers that a problem may arise when two deeds are recorded for the same property; signature verification; social security number verification; powers of attorney validated by licensed title professionals; and photographic identification scanned in with the documents offered for recording.[36]

33 See, Bailey and Halpern Weinstein, The Race to Erase Recording Mistakes, NYLJ 4/13/11.

34 Christopher Peterson, Two Faces: Demystifying the Mortgage Electronic Registration System's Land Title Theory, http://ssrn.com/abstract=1684729; Marsh, supra (2010).

35 It is a political, not a legal decision to decide whether policy should or should not encourage mortgages being freely swapped around like stocks and bonds.

36 There are strong arguments to make these fraud prevention devices publicly inaccessible as public accessibility could have these devices foster fraud instead of preventing it.

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Moving Beyond the Mistakes of MERS ...

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Such an enhanced recording system could also handle the recording of promissory notes along with their mortgages, incentivized by a statutory rebuttable presumption that the owner stated on the recording is the current owner unless there is a recorded assignment of the note enjoying the same presumption. Logically, one would prepare any such assignment so as to assign both the note and the mortgage. That kind of recorded note system with ACRIS style indexing and access would make MERS—created chiefly for achieving speed—hopelessly obsolete and provide both lenders and the public with real value for their recording fees pouring once again into government coffers.

Conclusion

Both mortgage recording and foreclosure systems across America are currently broken. Fixing the latter inevitably requires fixing the former. Clearly no federal fix is in the offing, but inspired leadership in state capitals can go a long way, if not in curing the consequences of not having fixed the systems sooner, at least in erecting a system that will sustain commerce and secure titles in the future. ■

Meetings Calendar

2012 Mid-Year Meeting
March 8 - 11, 2012
Four Season Hotel
Las Vegas, NV

2012 Annual Meeting
October 18-21, 2012
Renaissance Hotel
Chicago, IL

2013 Mid-Year Meeting
March 14-17, 2013
Naples Grande Resort
Naples, FL

2013 Annual Meeting
October 17-20, 2013
Four Seasons Hotel
Vancouver, BC, Canada

2014 Mid-Year Meeting
March 27-30, 2014
Grand Hyatt Kauai Resort and Spa
Kauai, HI

2014 Annual Meeting
October 16-19, 2014
InterContinental Hotel
Boston, MA

ACREL Mentoring Program 2011

by Kathy Murphy and Ken Jacobson, Co-Chairs, Orientation and Integration Committee

The ACREL Orientation and Integration Committee was organized to, among other things, facilitate the integration of new Fellows into the College. One of the most important programs that the Committee manages is ACREL's mentoring program. In the mentoring program, current Fellows in the College are matched with new Fellows. The mentors are volunteers who reach out to new Fellows after the new Fellows have accepted their invitation to join ACREL. Mentors act as a resource for the new Fellow to facilitate meeting other Fellows and learning about the opportunities provided by the College. Mentors answer the new Fellows' questions regarding ACREL and its activities, encourage attendance at the annual and mid-year meetings of the College, introduce new Fellows to other Fellows at the College's meetings, and generally make new Fellows feel welcome at meetings and in the College.

The mentoring program was supplemented by an orientation call for new Fellows in advance of the Philadelphia meeting in which members of the Executive Committee, Jill Pace and Orientation and Integration Committee co-chairs, Kathy Murphy and Ken Jacobson, participated.

Many thanks to the following persons who are serving as mentors and helping to integrate Fellows admitted into the College during 2011; namely, Brian C. Rider, Cheryl A. Kelly, Richard C. Mallory, F. DeArmond Sharp, Susan Bryson, Scott Jackson, Caryl B. Welborn, Marilyn C. Maloney, Toni P. Wise, Thomas M. Whelan, Neil S. Kessler, Mark A. Senn, Jonathan Shills, Robert D. Lane, Jr., Gordon Tanner, Robert C. Wright, Elwood F. Cahill, Jr., Mike Swearengen, Jack Fersko, John P. McNearney, Scott B. Osborne, Margaret S. Burnham, Rebecca A. Fischer and Jon F. Leyens, Jr.

Mentors are asked to stay in contact with their mentees following the annual meeting and encourage them to attend the Mid-Year and Annual meetings the following year. We hope all Fellows will consider volunteering to be a mentor at some point in their ACREL careers.

Please contact Marilyn Maloney (mcmaloney@liskow.com) or Angela Christy (AChristy@faegre.com) if you are interested in volunteering to be a mentor. ■

Foreclosure as Stay Violation Where Loan is Guaranteed and Guarantor/ Debtor is Party to the Foreclosure Suit

by David R. Kuney, Sidley Austin LLP

Ordinarily, when a mortgage lender forecloses on real property that is not owned by a debtor in bankruptcy, but the guarantor of the mortgage is in bankruptcy, there is no violation of the automatic stay. This scenario may presents itself in mezzanine structures, where the sponsor and parent entity file for bankruptcy, but some or all of the fee-holding subsidiaries do not file for bankruptcy.

However, in a case described as one of "first impression" a bankruptcy court held that in some circumstances a New York state foreclosure action against real property owned by a borrower who is *not* a debtor in bankruptcy, may nevertheless be a violation of the automatic stay (and hence void). *In re Ebadi*, 448 B.R. 308 (Bankr. E.D.N.Y. March 30, 2011) This unusual result can occur where the mortgage is personally guaranteed, the guarantor is in bankruptcy, and the guarantor is named as a party in the foreclosure action and the foreclosure judgment. Because New York state law requires that a party seeking foreclosure include an *in personam* claim against potential deficiency parties, the case could have wide spread implications. Other states may have similar rules.

The facts are as follows: On September 26, 2001, CBC Media Realty ("CBC") executed a note and mortgage in favor of Fleet National Bank. The Debtor, Madjid Ebadi was the owner of CBC, and executed a guaranty agreement. The borrower defaulted and Bank of America, as successor, initiated a foreclosure action in New York state court. The foreclosure action *named both the borrower (not a debtor) and the debtor* as defendants, because New York requires that a foreclosure action name a potential deficiency party. At the time of the foreclosure action, the debtor had not yet filed for bankruptcy.

A few hours before the foreclosure sale, the guarantor filed for bankruptcy. After the bankruptcy filing, a foreclosure judgment was obtained. The foreclosure judgment itself also contained express language stating that if the proceeds of the sale were insufficient to satisfy the entire debt owed to the lender, then the plaintiffs "shall recover from defendants. . . and [Debtor]" the whole deficiency. . . provided a motion for a deficiency judgment shall be made. . ." *Id*. at 312.

The guarantor moved to have the foreclosure declared void. The court describing its decision as one of first impression, stated that the issue was "whether a foreclosure sale under New York law of real property in which a bankruptcy debtor has no ownership interest is a violation of the automatic stay, where the debtor is a guarantor of the underlying debt *and a named defendant in the foreclosure judgment." Id*. at 313 (emphasis added).

The court ruled that the foreclosure was a stay violation and that the foreclosure was void. The court noted several times that the grounds for finding a stay violation was that the debtor was *named as a defendant* in the state court foreclosure, that the judgment thus was effective as against the debtor, and that the sale was thus part of a process under New York law to determine and obtain a deficiency judgment against the debtor. "[T]he stay violation at issue here is not based upon Debtor having an

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ownership interest in the Property but, rather, on Debtor's being a named defendant in the Foreclosure Action, and in the Foreclosure Judgment, which arose from Debtor's status as a guarantor of the debt owed by [borrower] to [Lender]." *Id*. at 314.

The court noted the general rule that a foreclosure action against real property on debt which is personally guaranteed, is generally not a stay violation. "It is a well established principle of bankruptcy law that a creditor is generally not barred from pursuing collection of a debt from a non-filing co-obligor or guarantor, even if one of the obligors, or the principal obligor, is a debtor in bankruptcy, and is therefore shielded from collection efforts by the automatic stay." *Id*. at 316. However, "this case is distinguishable [from this rule] [and] the stay violation is predicated on [the lenders] actions taken in furtherance of the Foreclosure Judgment *against, inter alia, the Debtor himself.*

Practice tip: The lender could have protected itself by doing one of two things. First, the lender should have sought and obtained relief from the stay. *Id*. at 318. Second, the court specifically noted that a stay violation would not have occurred had the guarantor not been named in the original foreclosure action: "Had [creditor] dismissed Debtor from the Foreclosure Action and removed Debtor from the Foreclosure Judgment prior to the sale going forward, the case would likely have been sufficiently analogous to collecting from a non-filing co-obligor such that [lender]would not have been stayed. . ." *Id*. at 316. However, if the creditor does dismiss the guarantor, then under New York law, the lender cannot later pursue a deficiency claim against such guarantor. ■