

CCM 2012 Testimony

900 CHAPEL STREET, 9th FLOOR, NEW HAVEN, CT 06510-2807 PHONE (203) 498-3000 FAX (203) 562-6314

PLANNING & DEVELOPMENT COMMITTEE

March 16, 2012

The Connecticut Conference of Municipalities (CCM) is Connecticut's statewide association of towns and cities and the voice of local government - your partners in governing Connecticut. Our members represent over 90% of Connecticut's population. We appreciate the opportunity to testify on bills of interest to towns and cities.

S.B. 407 "An Act Concerning the Assignment of Mortgage Debts"

CCM supports this bill.

SB 407 would require the assignment of mortgages to be recorded in municipal land records no later than sixty days after the assignment is made. It also would allow town clerks to impose a surcharge of \$250 for each week late, up to a maximum amount of \$5,000.

Traditionally, mortgage assignments have been recorded in land records -- as a benefit to both municipalities as well as homeowners -- offering clear ownership and title of a particular piece of property. In recent years, however, changes in bank practices have left homeowners and municipalities unaware of who owns a particular mortgage or property. Since the mid-1990's many banks have used the Mortgage Electronic Registration Systems (MERS) to record mortgage assignments. It was designed by several of the large banks within the mortgage industry as an electronic registry to track servicing rights and ownership of mortgage loans rather than recording them in municipal land records. The primary function of MERS has been to act as a document custodian, to simplify the process of transferring mortgages by avoiding the need to re-record liens -- thereby paying municipal recording filing fees -- each time a loan is assigned.

The mortgage industry has argued that MERS has streamlined the assignment process, but they have displaced the more transparent public system for maintaining records. The results has been municipalities' inability to turn to public records to learn the identity of a property owner, and for the homeowner the inability to determine the mortgage owner, who is escrowing for their taxes and insurance and who can foreclose on them.

This practice has become extremely problematic, especially with the rise of foreclosures, which have left many homeowners abandoning their homes. When these homes are abandoned they undergo disrepair and become blight issues for towns and cities.

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National Focus on the Crisis

MERS' murkiness has been under a microscope lately. Last month, New York State's Attorney Eric T. Schneiderman initiated a lawsuit accusing several banks of fraud in their use of MERS. General Schneiderman is quoted as saying "The mortgage industry created MERS to allow financial institutions to evade county recording fees, avoid the need to publicly record mortgage transfers and facilitate the rapid sale and securitization of mortgages en masse." It created this "bizarre and complex end-around of the traditional public recording system". He asserts banks saved \$2 billion in recording fees. He also asserts that "More than 70 million mortgage loans, including millions of subprime loans, have been registered in the MERS system, rather than in local county clerks' offices". A copy of *The New York Times* article is enclosed.

The MERS crisis has been featured on shows such as MSNBC and NPR ("Local Governments File Suits Against MERS"). Also, *60 Minutes* reported on the issue: "NC County Sues Banks...". The piece stated that, according to the lawsuit initiated by Guilford County, "Without available and accurate records, landowners can lose their property to illegal foreclosures, see their ability to buy and sell property restricted, and interests of mortgage lenders and borrowers are jeopardized."

State and Local Fiscal Implications to MERS

There are indeed fiscal implications for Connecticut towns and cities – and the State. Take just one example: West Hartford. The Town estimates a loss of about \$48,336 in revenue -- of which the State would have received \$33,835.

Also, enclosed is the Introduction to a report entitled, "Foreclosure, Subprime Mortgage Lending and the Mortgage Electronic Registration System" by Christopher L. Paterson of the University of Utah Law School.

SB 407 would ensure that municipal land records are accurate and current, and can provide residents with important information regarding their mortgage.

CCM urges the committee to favorably report SB 407.

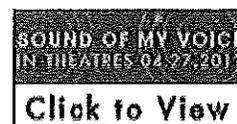
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If you have any questions, please contact Ron Thomas or Mike Muszynski at (203) 498-3000.

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February 3, 2012

New York Sues 3 Big Banks Over Mortgage Database

By REUTERS

Attorney General Eric T. Schneiderman of New York sued three major banks on Friday, accusing them of fraud in their use of an electronic mortgage database that he said resulted in deceptive and illegal practices, including false documents in foreclosure proceedings.

Mr. Schneiderman, co-chairman of a new mortgage crisis unit under President Obama, filed a lawsuit against Bank of America, Wells Fargo and JPMorgan Chase in New York State Supreme Court in Brooklyn.

The database, called the Mortgage Electronic Registration System or MERS, was created in the mid-1990s for tracking mortgage ownership. It is a collaboration of top mortgage servicers, mortgage insurers and Fannie Mae and Freddie Mac, the government entities that hold many of the country's mortgages.

"The mortgage industry created MERS to allow financial institutions to evade county recording fees, avoid the need to publicly record mortgage transfers and facilitate the rapid sale and securitization of mortgages en masse," Mr. Schneiderman said.

"By creating this bizarre and complex end-around of the traditional public recording system," Mr. Schneiderman's lawsuit asserts, the banks saved \$2 billion in recording fees.

More than 70 million mortgage loans, including millions of subprime loans, have been registered in the MERS system, rather than in local county clerks' offices, according to the lawsuit.

The lawsuit asserts the database is inaccurate and seeks to stop the banks from filing foreclosure actions through MERS and executing false or defective mortgage assignments in New York foreclosure proceedings.

Mr. Schneiderman also is seeking all profits obtained through fraudulent and deceptive practices and other damages, including \$5,000 for each violation of general business law.

Patrick Linehan, a JPMorgan spokesman, and Rick Simon, a Bank of America spokesman, declined to comment on the lawsuit. Ancel Martinez, a Wells Fargo spokesman, said the company was reviewing the lawsuit and did not have "anything to add at this time." Janis L. Smith, a spokeswoman for Merscorp and its subsidiary, MERS, said in a statement that the firms complied with the law and mortgage regulations.

"Federal and state courts around the country have repeatedly upheld the MERS business model, and the validity of MERS as legal mortgagee and nominee for lenders," the MERS statement said. "We refute the attorney general's claims and will defend the case vigorously in court."

New York Times
March 5, 2011

MERS? It May Have Swallowed Your Loan

By MICHAEL POWELL and GRETCHEN MORGENSON

¶ FOR more than a decade, the American real estate market resembled an overstuffed novel, which is to say, it was an engrossing piece of fiction.

¶ Mortgage brokers hip deep in profits handed out no-doc mortgages to people with fictional incomes. Wall Street shopped bundles of those loans to investors, no matter how unappetizing the details. And federal regulators gave sleepy nods.

¶ That world largely collapsed under the weight of its improbabilities in 2008.

¶ But a piece of that world survives on Library Street in Reston, Va., where an obscure business, the MERS Corporation, claims to hold title to roughly half of all the home mortgages in the nation — an astonishing 60 million loans.

¶ Never heard of MERS? That's fine with the mortgage banking industry—as MERS is starting to overheat and sputter. If its many detractors are correct, this private corporation, with a full-time staff of fewer than 50 employees, could turn out to be a very public problem for the mortgage industry.

¶ Judges, lawmakers, lawyers and housing experts are raising piercing questions about MERS, which stands for Mortgage Electronic Registration Systems, whose private mortgage registry has all but replaced the nation's public land ownership records. Most questions boil down to this:

¶ How can MERS claim title to those mortgages, and foreclose on homeowners, when it has not invested a dollar in a single loan?

¶ And, more fundamentally: Given the evidence that many banks have cut corners and made colossal foreclosure mistakes, does anyone know who owns what or owes what to whom anymore?

¶ The answers have implications for all American homeowners, but particularly the millions struggling to save their homes from foreclosure. How the MERS story plays out could deal another blow to an ailing real estate market, even as the spring buying season gets under way.

¶ MERS has distanced itself from the dubious behavior of some of its members, and the company itself has not been accused of wrongdoing. But the legal challenges to MERS, its practices and its records are mounting.

¶ The Arkansas Supreme Court ruled last year that MERS could no longer file foreclosure proceedings there, because it does not actually make or service any loans. Last month in Utah, a local judge made the no-less-striking decision to let a homeowner rip up his mortgage and walk away debt-free. MERS had claimed ownership of the mortgage, but the judge did not recognize its legal standing.

¶ “The state court is attracted like a moth to the flame to the legal owner, and that isn’t MERS,” says Walter T. Keane, the Salt Lake City lawyer who represented the homeowner in that case.

¶ And, on Long Island, a federal bankruptcy judge ruled in February that MERS could no longer act as an “agent” for the owners of mortgage notes. He acknowledged that his decision could erode the foundation of the mortgage business.

¶ But this, Judge Robert E. Grossman said, was not his fault.

¶ “This court does not accept the argument that because MERS may be involved with 50 percent of all residential mortgages in the country,” he wrote, “that is reason enough for this court to turn a blind eye to the fact that this process does not comply with the law.”

¶ With MERS under scrutiny, its chief executive, R. K. Arnold, who had been with the company since its founding in 1995, resigned earlier this year.

¶ A BIRTH certificate, a marriage license, a death certificate: these public documents note many life milestones.

¶ For generations of Americans, public mortgage documents, often logged in longhand down at the county records office, provided a clear indication of homeownership.

¶ But by the 1990s, the centuries-old system of land records was showing its age. Many county clerk’s offices looked like something out of Dickens, with mortgage papers stacked high. Some clerks had fallen two years behind in recording mortgages.

¶ For a mortgage banking industry in a hurry, this represented money lost. Most banks no longer hold onto mortgages until loans are paid off. Instead, they sell the loans to Wall Street, which bundles them into investments through a process known as securitization.

¶ MERS, industry executives hoped, would pull record-keeping into the Internet age, even as it privatized it. Streamlining record-keeping, the banks argued, would make mortgages more affordable.

¶ But for the mortgage industry, MERS was mostly about speed — and profits. MERS, founded 16 years ago by Fannie Mae, Freddie Mac and big banks like Bank of America and JPMorgan Chase, cut out the county clerks and became the owner of record, no matter how many times loans were transferred. MERS appears to sell loans to MERS ad infinitum.

¶ This high-speed system made securitization easier and cheaper. But critics say the MERS system made it far more difficult for homeowners to contest foreclosures, as ownership was harder to ascertain.

¶ MERS was flawed at conception, those critics say. The bankers who midwived its birth hired Covington & Burling, a prominent Washington law firm, to research their proposal. Covington produced a memo that offered assurances that MERS could operate legally nationwide. No one, however, conducted a state-by-state study of real estate laws.

¶ “They didn’t do the deep homework,” said an official involved in those discussions who spoke on condition of anonymity because he has clients involved with MERS. “So as far as anyone can tell their real theory was: ‘If we can get everyone on board, no judge will want to upend something that is reasonable and sensible and would screw up 70 percent of loans.’ ”

¶ County officials appealed to Congress, arguing that MERS was of dubious legality. But this was the 1990s, an era of deregulation, and the mortgage industry won.

¶ “We lost our revenue stream, and Americans lost the ability to immediately know who owned a piece of property,” said Mark Monacelli, the St. Louis County recorder in Duluth, Minn.

¶ And so MERS took off. Its board gave its senior vice president, William Hultman, the rather extraordinary power to deputize an unlimited number of “vice presidents” and “assistant secretaries” drawn from the ranks of the mortgage industry.

¶ The “nomination” process was near instantaneous. A bank entered a name into MERS’s Web site, and, in a blink, MERS produced a “certifying resolution,” signed by Mr. Hultman. The corporate seal was available to those deputies for \$25.

¶ As personnel policies go, this was a touch loose. Precisely how loose became clear when a lawyer questioned Mr. Hultman in April 2010 in a lawsuit related to its foreclosure against an Atlantic City cab driver.

¶ How many vice presidents and assistant secretaries have you appointed? the lawyer asked.

¶ “I don’t know that number,” Mr. Hultman replied.

¶ Approximately?

¶ “I wouldn’t even be able to tell you, right now.”

¶ In the thousands?

¶ “Yes.”

¶ Each of those deputies could file loan transfers and foreclosures in MERS’s name. The goal, as with almost everything about the mortgage business at that time, was speed. Speed meant money.

¶ ALAN GRAYSON has seen MERS’s record-keeping up close. From 2009 until this year, he served as the United States representative for Florida’s Eighth Congressional District — in the Orlando area, which was ravaged by foreclosures. Thousands of constituents poured through his office, hoping to fend off foreclosures. Almost all had papers bearing the MERS name.

¶ “In many foreclosures, the MERS paperwork was squirrely,” Mr. Grayson said. With no real legal authority, he says, Fannie and the banks eliminated the old system and replaced it with a privatized one that was unreliable.

¶ A spokeswoman for MERS declined interview requests. In an e-mail, she noted that several state courts have ruled in MERS’s favor of late. She expressed confidence that MERS’s policies complied with state laws, even if MERS’s members occasionally strayed.

¶ “At times, some MERS members have failed to follow those procedures and/or established state foreclosure rules,” the spokeswoman, Karmela Lejarde, wrote, “or to properly explain MERS and document MERS relationships in legal pleadings.”

¶ Such cases, she said, “are outliers, reflecting case-specific problems in process, and did not repudiate the MERS business model.”

¶ MERS’s legal troubles, however, aren’t going away. In August, the Ohio secretary of state referred to federal prosecutors in Cleveland accusations that notaries deputized by MERS were signing hundreds of documents without any personal knowledge of them. The attorney general of Massachusetts is examining a complaint by a county registrar that MERS owes the state tens of millions of dollars in unpaid fees.

¶ As far back as 2001, Ed Romaine, the clerk for Suffolk County, on eastern Long Island, refused to register mortgages in MERS’s name, partly because of complaints that the company’s records didn’t square with public ones. The state Court of Appeals later ruled that he had overstepped his powers.

¶ But Judith S. Kaye, the state’s chief judge at the time, filed a partial dissent. She worried that MERS, by speeding up property transfers, was pouring oil on the subprime fires. The MERS system, she wrote, ill serves “innocent purchasers.”

¶ “I was trying to say something didn’t smell right, feel right or look right,” Ms. Kaye said in a recent interview.

¶ Little about MERS was transparent. Asked as part of a lawsuit against MERS in September 2009 to produce minutes about the formation of the corporation, Mr. Arnold, the former C.E.O., testified that “writing was not one of the characteristics of our meetings.”

¶ MERS officials say they conduct audits, but in testimony could not say how often or what these measured. In 2006, Mr. Arnold stated that original mortgage notes were held in a secure “custodial facility” with “stainless steel vaults.” MERS, he testified, could quickly produce every one of those files.

¶ As for homeowners, Mr. Arnold said they could log on to the MERS system to identify their loan servicer, who, in turn, could identify the true owner of their mortgage note. “The servicer is really the best source for all that information,” Mr. Arnold said.

¶ The reality turns out to be a lot messier. Federal bankruptcy courts and state courts have found that MERS and its member banks often confused and misrepresented who owned mortgage notes. In thousands of cases, they apparently lost or mistakenly destroyed loan documents.

¶ The problems, at MERS and elsewhere, became so severe last fall that many banks temporarily suspended foreclosures.

¶ Some experts in corporate governance say the legal furor over MERS is overstated. Others describe it as a useful corporation nearly drowning in a flood tide of mortgage foreclosures. But not even the mortgage giant Fannie Mae, an investor in MERS, depends on it these days.

¶ “We would never rely on it to find ownership,” says Janis Smith, a Fannie Mae spokeswoman, noting it has its own records.

¶ Apparently with good reason. Alan M. White, a law professor at the Valparaiso University School of Law in Indiana, last year matched MERS’s ownership records against those in the public domain.

¶ The results were not encouraging. “Fewer than 30 percent of the mortgages had an accurate record in MERS,” Mr. White says. “I kind of assumed that MERS at least kept an accurate list of current ownership. They don’t. MERS is going to make solving the foreclosure problem vastly more expensive.”

¶ THE Sarmientos are one of thousands of American families who have tried to pierce the MERS veil.

¶ Several years back, they bought a two-family home in the Greenpoint section of Brooklyn for \$723,000. They financed the purchase with two mortgages from Lend America, a subprime lender that is now defunct.

¶ But when the recession blew in, Jose Sarmiento, a chef, saw his work hours get cut in half. He fell behind on his mortgages, and MERS later assigned the loans to U.S. Bank as a prelude to filing a foreclosure motion.

¶ Then, with the help of a lawyer from South Brooklyn Legal Services, Mr. Sarmiento began turning over some stones. He found that MERS might have violated tax laws by waiting too long before transferring his mortgage. He also found that MERS could not prove that it had transferred both note and mortgage, as required by law.

¶ One might argue that these are just legal nits. But Mr. Sarmiento, 59, shakes his head. He is trying to work out a payment plan through the federal government, but the roadblocks are many. "I'm tired; I've been fighting for two years already to save my house," he says. "I feel like I never know who really owns this home."

¶ Officials at MERS appear to recognize that they are swimming in dangerous waters. Several federal agencies are investigating MERS, and, in response, the company recently sent a note laying out a raft of reforms. It advised members not to foreclose in MERS's name. It also told them to record mortgage transfers in county records, even if state law does not require it.

¶ MERS will no longer accept unverified new officers. If members ignore these rules, MERS says, it will revoke memberships.

¶ That hasn't stopped judges from asking questions of MERS. And few are doing so with more puckish vigor than Arthur M. Schack, a State Supreme Court judge in Brooklyn.

¶ Judge Schack has twice rejected a foreclosure case brought by Countrywide Home Loans, now part of Bank of America. He had particular sport with Keri Selman, who in Countrywide's court filings claimed to hold three jobs: as a foreclosure specialist for Countrywide Home Loans, as a servicing agent for Bank of New York and as an assistant vice president of MERS. Ms. Selman, the judge said, is a "milliner's delight by virtue of the number of hats that she wears."

¶ At heart, Judge Schack is scratching at the notion that MERS is a legal fiction. If MERS owned nothing, how could it bounce mortgages around for more than a decade? And how could it file millions of foreclosure motions?

¶ These cases, Judge Schack wrote in February 2009, "force the court to determine if MERS, as nominee, acted with the utmost good faith and loyalty in the performance of its duties."

¶ The answer, he strongly suggested, was no.

The New York Times (Business Day Section), February 3, 2012

Mortgage Electronic Registration Systems (MERS) Inc.



Joe Raedle/Getty Images

Updated: Feb. 3, 2012

The Mortgage Electronic Registration System, or MERS, is owned by banks and mortgage finance firms. It was created during the housing boom to smooth the process of turning mortgages into complex securities — and to allow lenders to avoid paying registration fees to counties each time the mortgage changed hands. It is the nation's largest electronic mortgage tracking system.

In the fall of 2010, as evidence mounted that many foreclosures may have been mishandled, the system was faulted for sloppiness and questions were raised about whether it was used to sidestep legal requirements. The rising calls for halts to foreclosures suggested that the new approach could in fact have created huge new vulnerabilities for lenders.

In October, on the same day that all 50 state attorneys general announced that they would investigate foreclosure practices, JPMorgan Chase & Company became the first big lender to acknowledge that it had stopped using MERS for foreclosures.

In February 2012, Attorney General Eric T. Schneiderman of New York sued three major banks, accusing them of fraud in their use of MERS, which he said resulted in deceptive and illegal practices, including false documents in foreclosure proceedings. The banks were Bank of America, Wells Fargo and JPMorgan Chase.

“The mortgage industry created MERS to allow financial institutions to evade county recording fees, avoid the need to publicly record mortgage transfers and facilitate the rapid sale and securitization of mortgages en masse,” Mr. Schneiderman said. By creating this “bizarre and complex end-around of the traditional public recording system,” Mr. Schneiderman’s lawsuit asserts, the banks saved \$2 billion in recording fees.

More than 70 million mortgage loans, including millions of subprime loans, have been registered in the MERS system, rather than in local county clerks' offices, according to the lawsuit, which asserts the database.

Background

The registration system is an electronic database meant to replace the reams of paper that were once the cornerstone of the residential mortgage market. The registry was also meant to eliminate the need to record changes in property ownership in local land records.

About 60 percent of mortgages in this country show up in local records as being owned by the service. In fact, none are owned by MERS. It was created to act as an agent for others, whether banks or securitization trusts, which own the actual mortgages — an arrangement that lawyers for homeowners and some judges have called into question.

For centuries, when a property changed hands, the transaction was submitted to county clerks who recorded it and filed it away. These records ensured that the history of a property's ownership was complete and that the priority of multiple liens placed on the property — a mortgage and a home equity loan, for example — was accurate.

During the mortgage lending spree, however, home loans changed hands constantly. Those that ended up packaged inside of mortgage pools, for instance, were often involved in a dizzying series of transactions. So to avoid the costs and complexity of tracking all these exchanges, Fannie Mae, Freddie Mac and the mortgage industry set up MERS to record loan assignments electronically. This company didn't own the mortgages it registered, but it was listed in public records either as a nominee for the actual owner of the note or as the original mortgage holder.

The problems with MERS began to come to light when "vice presidents" of the firm began to submit affidavits in foreclosures, saying the original note had been lost. In some cases those notes were signed by people who signed thousands of such affidavits, and have now admitted they did not actually review the files, as the affidavits said they had. Nor were those people really employees of MERS.

Cost savings to members who joined the registry were meaningful. In 2007, the organization calculated that it had saved the industry \$1 billion during the previous decade. Some 60 million loans are registered in the name of MERS.

When the bottom fell out of the market and delinquencies soared, thousands of foreclosure proceedings began to be filed through MERS. But as cases filed by MERS grew, lawyers representing troubled borrowers began questioning how an electronic registry with no ownership claims had the right to evict people. The system also led to confusion. When MERS was involved, borrowers who hoped to work out their loans couldn't identify who they should turn to.

In September 2010, a number of the nation's largest mortgage lenders suspended evictions after disclosures that employees signed documents without ascertaining the accuracy of the material, a legal requirement. Attorney General Eric H. Holder Jr. said at a news conference on Oct. 6 that

the federal Financial Fraud Enforcement Task Force is looking at the foreclosure issue, while the attorneys general in as many as 40 states are planning a coordinated investigation.

While the outcry has centered on the question of forged or overly rushed reviews of foreclosure documents, figuring out the role of MERS will be important in the federal and state investigations because it acts as a middleman in the mortgage market, allowing the loans to be sold to investors while keeping track of who actually owns them.

The question being raised by many lawyers for homeowners is whether MERS should be allowed to act in court as the owner of the mortgage, when in fact it is not the owner of them, but only represents a bank who owns the note — or a bank who later sold shares of a pool of mortgages to investors, who could themselves have resold the shares.

If it turns out that this new system does not fit properly in the foreclosure process, then the value of the billions of dollars of mortgage-backed securities sold to investors could be called into question. That could lead to even further litigation against the banks and investment firms that sold mortgage securities if the ability to foreclose on home mortgages is not what it was portrayed to be in the documents used to sell the securities.

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FORECLOSURE, SUBPRIME MORTGAGE LENDING, AND THE MORTGAGE ELECTRONIC REGISTRATION SYSTEM

Christopher L. Peterson

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FORECLOSURE, SUBPRIME MORTGAGE LENDING, AND THE MORTGAGE ELECTRONIC REGISTRATION SYSTEM

Christopher L. Peterson *

I. INTRODUCTION

In the past two years, subprime mortgage lending has forced the American economy to the brink of a depression and fundamentally undermined world faith in American consumer financial markets.¹ A host of dubiously underwritten mortgage loans helped inflate a bubble in residential real estate values.² As it has become clear that millions of Americans are not capable of repaying loans crafted for them by commission-hungry brokers, the liquidity of securities drawn from those loans froze.³ Currently about 25% of all subprime home mortgages are delinquent, with millions more likely to follow.⁴ One rating agency predicts that between 40% and 50% of all subprime mortgages originated since 2006 will eventually end in foreclosure.⁵ As the volume of foreclosures increased, it put downward pressure on home prices, creating the first decline in the national median price for previously owned homes since the Great Depression of the 1930s.⁶ According to one estimate, over a quarter of all American households currently have negative equity—they owe more on their home mortgage than their home is worth.⁷ About half of all subprime borrowers are

* Associate Dean of 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: Richard Aaron, April Charney, Prentis Cox, Ron Fuller, Michael Kent, Kathleen Keest, Tera Peterson, Diane Thompson, and Michael Wolf. I am also grateful for helpful comments and questions posed by faculty, students, and other participants attending presentations related to this project at Seton Hall University, the University of Houston Law Center, Ohio State University, and Harvard Law School.

1. Compare Paul Krugman, *Crisis of Confidence*, N.Y. TIMES, Apr. 14, 2008, at A23, with Robert J. Samuelson, *How This Crisis is Different*, WASH. POST., Mar. 18, 2008, at A19.

2. Kareem Fahim & Janet Roberts, *Foreclosures, With No End in Sight*, N.Y. TIMES, May 17, 2009, at NJ1.

3. Joshua Boak, *IMF Puts Subprime Loss Near \$1 Trillion*, CHI. TRIB., Apr. 9, 2008, at C1.

4. Paul Gores, *Trouble at Home*, MILWAUKEE J. SENTINEL, Aug. 21, 2009, at D1; E. Scott Reckard, *State's Mortgage Woes Forecast to Rise*, L.A. TIMES, Aug. 25, 2009, at B2.

5. GRANT BAILY ET AL. FITCH RATINGS, REVISED LOSS EXPECTATIONS FOR 2006 AND 2007 SUBPRIME VINTAGE COLLATERAL 2 (2008).

6. *Banks Collect Houses Amid Subprime Fallout*, INT'L HERALD TRIB., July 3, 2007, at 10.

7. Jody Shenn, *'Underwater' Mortgages to Hit 48%, Deutsche Bank Says*, BLOOMBERG, Aug. 5, 2009, <http://www.bloomberg.com/apps/news?pid=20601110&sid=ac9y1xr7yNhQ>.

underwater on their loans.⁸ Thousands of financial “foreclosure rescue” predators and con artists are openly stalking desperate families looking for a financial lifeline.⁹ County and municipal governments in the Los Angeles area have begun campaigns to exterminate a scourge of mosquitoes breeding in the rotten water of swimming pools behind thousands of abandoned suburban homes.¹⁰ In Cleveland, Ohio an estimated 15,000 of the area’s 84,000 single-family homes are sitting vacant and deteriorating into urban blight with squatters and scavengers taking over entire neighborhoods.¹¹ America lost friends in places as far off as Norway and Australia when municipal pension funds bottomed out on investments in American subprime mortgage securities.¹² The International Monetary Fund estimates subprime losses at nearly a trillion dollars; about \$143 for every person on the planet.¹³

Reckless overleveraging on Wall Street combined with losses in mortgage securities to squeeze the investment banking establishment. Two of the nation’s formerly most reputable investment houses, Bear Sterns and Lehman Brothers, collapsed when it became clear that billions of dollars of their subprime mortgage assets were virtually worthless.¹⁴ For its part, the Federal Reserve Board of Governors (Fed) slashed interest rates on loans offered to member banks, keeping the economy afloat, but fueling concerns of a return to 1970s-style stagflation.¹⁵ Teetering on the edge of financial abyss, the Fed opened up new credit lines to Wall Street investment firms, creating financial arrangements not unlike deposit insurance, but chillingly devoid of traditional deposit insurance regulatory oversight—without any explicit

8. Les Christie, *Half of Mortgage Borrowers Will be ‘Underwater’*, CNNMONEY, Aug. 6, 2009, http://money.cnn.com/2009/08/06/real_estate/underwaterworld/.

9. Donna Leinwand, *Foreclosure Rescue Scams Multiply*, USA TODAY, Aug. 4, 2008, at 3A.

10. Steve Chawkins, *A Magical Misery Tour in Stockton*, L.A. TIMES, Dec. 13, 2007, at A1; David Streitfeld, *Blight Moves in After Foreclosures*, L.A. TIMES, Aug. 28, 2007, at A1.

11. Erik Eckholm, *Foreclosures Force Suburbs to Fight Blight*, N.Y. TIMES, Mar. 3, 2007, at A1 (“Many of the houses are filled with smelly trash and mattresses used by vagrants. They have been stripped of aluminum siding, appliances, pipes and anything else that scavengers can sell to scrap dealers.”); Alex Kotlowitz, *All Boarded Up*, N.Y. TIMES, Mar. 8, 2009, at MM28 (“The city estimates that 10,000 houses, or 1 in 13, are vacant. The county treasurer says it’s more likely 15,000. Most of the vacant houses are owned by lenders who foreclosed on the properties and by the wholesalers who are now sweeping in to pick up houses in bulk, as if they were trading in baseball cards.”).

12. Julia Werdigier, *Wall St.’s Pullback on Financing Creates Openings for Europe’s Smaller Banks*, N.Y. TIMES, Mar. 22, 2008, at C3.

13. Boak, *supra* note 3.

14. WILLIAM D. COHAN, *HOUSE OF CARDS; A TALE OF HUBRIS AND WRETCHED EXCESS ON WALL STREET 4* (2009); Devin Leonard, *How Lehman Got Its Real Estate Fix*, N.Y. TIMES, May 3, 2009, at BU 1.

15. Tom Lauricella, *Quarterly Markets Review: Trying to Get Up Off the Mat*, WALL ST. J., Apr. 1, 2008, at C1.

prior approval from Congress.¹⁶ In addition to the crumpled Wall Street investment houses and hedge funds, smaller subprime mortgage loan originators folded up their tents like the Bedouin—over 100 different subprime mortgage origination companies systematically collapsed.¹⁷ Currently over 400 banks are on the FDIC's "problem list."¹⁸

With so many fundamental changes, opportunities for moral hazard, agency cost problems, consumer abuses, and impending lawsuits, perhaps the only group with a plethora of opportunities are law professors looking for salient article topics. Indeed, the academy has responded with a new crop of scholarship exploring the role of investment bankers, rating agencies, hedge funds, mortgage brokers, mortgage originators, and loan servicers. It is, however, somewhat ironic that virtually no academic attention has been paid to the one particular company that has been a party in more subprime mortgage loans than any other. Mortgage Electronic Registration Systems, Inc., commonly known as MERS, is a corporation registered in Delaware and headquartered in the Virginia suburbs of Washington, D.C.¹⁹ MERS operates a computer database designed to track servicing and ownership rights of mortgage loans anywhere in the United States.²⁰ Originators and secondary market players pay membership dues and per-transaction fees to MERS in exchange for the right to use and access MERS records.²¹

But, in addition to tracking ownership and servicing rights, MERS has attempted to take on a different, more aggressive, legal role. When closing on home mortgages, mortgage lenders now often list MERS as the "mortgagee of record" on the paper mortgage—rather than the lender that is the actual mortgagee.²² The mortgage is then recorded with the county property recorder's office under MERS, Inc.'s name, rather than the lender's name—even though MERS does not solicit, fund, service, or actually own any mortgage loans. MERS then purports to remain the mortgagee for the life of a mortgage loan even after the original lender or a subsequent assignee transfers the loan into a pool of loans that are

16. *Top Officials: Bear Rescue was not a Bailout*, CHI. TRIB., Apr. 4, 2008, at C1.

17. Steve Stecklow, *Subprime Lender's Failure Sparks Lawsuit Against Wall Street Banks*, WALL. ST. J., Apr. 9, 2008, at A1.

18. Damian Paletta & David Enrich, *Banks on Sick List Top 400*, WALL. ST. J., Aug. 28, 2009, at A1.

19. Carson Mullen, *MERS: Tracking Loans Electronically*, MORTGAGE BANKING, May 31, 2000, at 63.

20. Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, Jan. 1, 1997, at 42.

21. *Id.*

22. *See infra* note 64 and accompanying text.

ultimately sold to investors—a process known as securitization. Although MERS is a young company, 60 million mortgage loans are registered on its system.²³ Indeed, today MERS is legally involved in the origination of approximately 60% of all mortgage loans in the United States.²⁴ In past generations, employees of county recording offices kept records of each individual company that recorded mortgage loans and mortgage loan assignments. But today, recording officials increasingly carry on something of a bizarre puppet show, dutifully filing away records of the name of one company repeated over, and over again: MERS.

MERS justifies its role in mortgage loan closings and securitization deals by explaining that it is acting as a “nominee” for the parties.²⁵ The mortgage lending industry obtains two principal benefits from attempting to use MERS as a “mortgagee of record in nominee capacity.” First, under state secured credit laws, when a mortgage is assigned, the assignee must record the assignment with the county recording office, or risk losing priority vis-à-vis other creditors, buyers, or lienors. Most counties charge a fee, ranging from \$25 to \$50, to record the assignment, and use these fees to cover the cost of maintaining the real property records.²⁶ Some counties also use recording fees to fund their court systems, legal aid organizations, low-income housing programs, or schools.²⁷ In this respect, MERS’s role in acting as a mortgagee of record in nominee capacity is simply a tax evasion tool.²⁸ By paying MERS a fee, the parties to a securitization lower their operating costs. The second advantage MERS offers comes later, when homeowners fall behind on their monthly payments. In addition to its roles as a document custodian and tax evasion broker, MERS also frequently attempts to bring home foreclosure proceedings in its own name, rather than the name of the actual owner of the loan, which is often a trust owned by investors.²⁹ This eliminates the need for the trust—a purely legal business entity with no employees, offices, or assets other than its loans—to foreclose in its own name, or to reassign

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

24. *Id.*

25. See *infra* note 81 and accompanying text.

26. ANDREW LIPTON, MOODY’S INVESTORS SERVICE, MORTGAGE ELECTRONIC REGISTRATION SYSTEMS, INC. (MERS): ITS IMPACT ON THE CREDIT QUALITY OF FIRST-MORTGAGE JUMBO MBS TRANSACTIONS 2 (1999).

27. See, e.g., Chelan County Auditor, Fee List, http://www.co.chelan.wa.us/ad/adr_fees.htm, (last visited Sept. 2, 2009) (illustrating distribution of county recording fees in the State of Washington).

28. See *infra* note 57 and accompanying text.

29. Christopher L. Peterson, *Predatory Structured Finance*, 28 CARDOZO L. REV. 2185, 2208–12 (2007).

the loan to a loan servicing company to bring the foreclosure.³⁰ Throughout history, executioners have always worn masks. In the American mortgage lending industry, MERS has become the veiled man wielding the home foreclosure axe.

This Article explores the legal and public policy foundations of the MERS system. Part II briefly explains the origins of the county real property recording systems and the law governing real property liens. Part III explains how MERS works, why mortgage bankers created the company, and what MERS has done to transform the underlying assumptions of state real property recording law. Part IV explores three controversial legal issues confronting MERS and the companies that have relied on it. In particular, this Part queries whether MERS actually has standing to bring foreclosure actions; whether MERS should be considered a debt collector under the federal Fair Debt Collection Practices Act; and whether loans recorded in MERS's name should have priority in various collateral competitions under state law and the federal bankruptcy code. Next, Part V explores whether MERS bears some responsibility for the current mortgage foreclosure crisis and what the long-term effects of privatized land title records will have on our public information infrastructure. Part V also considers the deeper question of whether the mortgage banking industry, in creating and embracing MERS, has subverted the democratic governance of the nation's real property recording system.

II. THE AMERICAN REAL PROPERTY RECORDING SYSTEM

Public land title records have been a fundamental feature of American law since before the founding of the Republic. Unlike feudal Europe, where most real property was tied-up in successive generations of aristocratic families, most early colonists came to America seeking new opportunities.³¹ Relatively wide availability and lack of ancestral estates facilitated more frequent transfers of real property among businesses and families.³² Moreover, the American entrepreneurial spirit combined with the modest means of most colonists to create great demand for loans secured by the one widely available asset: land.³³

Perhaps then, it is not surprising that in the early seventeenth century, Americans began experimenting with laws requiring that parties create

30. *Id.*

31. 14 POWELL ON REAL PROPERTY § 82.01[1][b] (Michael Allan Wolf ed., 2007)

32. *Id.*

33. SYDNEY HOMER & RICHARD SYLLA, A HISTORY OF INTEREST RATES 28-81 (3d ed. 1996).