

# ROBO SIGNERS: The Legal Quagmire of Invalid Residential Foreclosure Proceedings and the Resultant Potential Impact upon Stakeholders

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## INTRODUCTION

Reports began erupting through the press during the latter half of 2010 exposing a potentially virulent financial mishap in the banking and mortgage related industry wherein some of the largest mortgage companies in this country used the same document processor to process foreclosure paperwork.<sup>1</sup> This document processor, Ally Financial, admitted to

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<sup>1</sup> See Ariana Eunjung Cha, *Ally Financial Legal Issue with Foreclosures May Affect Other Mortgage Companies*, WASH. POST (Sept. 22, 2010, 5:37 AM), <http://www.washingtonpost.com/wp-dyn/content/article/2010/09/21/>

AR2010092105872.html (asserting that because some of the largest mortgage companies used the same document processor as Ally Financial, they may have some of the same document processing problems as Ally Financial).

processing (or signing off on) the foreclosure paperwork without reading the documents.<sup>2</sup> Indeed, Ally Financial had to stop evictions of homeowners in a number of states.<sup>3</sup> It was reported at that time that many hundreds of other companies, including Fannie Mae and Freddie Mac, also used Ally Financial to service their loans.<sup>4</sup> In addition to Ally Financial, there have been revelations involving other document processors acting as what have been termed “robo-signers.”<sup>5</sup>

A *New York Times* article dated February 4, 2012, entitled: “A Mortgage Tornado Warning, Unheeded,”<sup>6</sup> brought to light an internal confidential Fannie Mae document forewarning of the practice of “robosigning.” This report was in direct response to a personal investigation conducted by an individual who lost his family home to foreclosure.

[A]fter losing a family home to foreclosure, under what he thought were fishy circumstances, Mr. Lavallo, founder of a consulting firm called the Sports Marketing Group, began a new life as a mortgage sleuth. In 2003, when home prices were flying high, he compiled a dossier of improprieties on one of the giants of the business, Fannie Mae.

In hindsight, what he found looks like a blueprint of today’s foreclosure crisis. Even then, Mr. Lavallo discovered, some loan-servicing companies that worked for Fannie Mae routinely filed false foreclosure documents, not unlike the fraudulent paperwork that has since made “robo-signing” a household term. Even then, he found, the nation’s electronic mortgage registry was playing fast and loose with the law—something that courts have belatedly recognized, too.

You might wonder why Mr. Lavallo didn’t speak up. But he did. For two years, he corresponded with Fannie Mae executives and lawyers. Fannie Mae later hired a Washington law firm to investigate his claims. In May 2006, that firm, using some of Mr. Lavallo’s research, issued a confidential, 147-page report

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<sup>2</sup> See Deposition of Jeffrey Stephan at 5, 7, 10, GMAC Mortgage, L.L.C. v. Neu, No. 50-2008-CA-040805XXXX-MB (Fla. Cir. Ct. Dec. 10, 2009), available at <http://www.tinyurl.com/yz6jgsj> (showing that Jeffrey Stephan admitted to signing approximately 10,000 foreclosure documents per month under oath that he had personally reviewed the foreclosure documents when he had, in fact, not personally reviewed the foreclosure documents).

<sup>3</sup> See Cha, *supra* note 1 (asserting that Ally Financial halted evictions of mortgagors in twenty-three states in order to investigate possible document signing irregularities).

<sup>4</sup> See *id.* (asserting that hundreds of mortgage companies, including some of the largest, used the same document processing service as Ally).

<sup>5</sup> See Deposition of Beth Ann Cottrell at 10–11, Chase Home Finance, L.L.C. v. Koren, No. 50-2008-CA-016857 (Fla. Cir. Ct. May 17, 2010), available at <http://www.propublica.org/documents/item/may-2010-deposition-by-beth-ann-cottrell-of-chase-home-finance> (showing that Beth Ann Cottrell admitted that she and others signed foreclosure documents attesting to personal knowledge of said document closures); see also Marian Wang, *GMAC’s ‘Robo-Signers’ Draw Concerns About Faulty Process, Mistaken Foreclosures*, PRO PUBLICA (Sept. 29, 2010, 12:49 PM), <http://www.propublica.org/blog/item/gmacs-robo-signers-draw-concerns-about-faulty-process-mistaken-foreclosures>.

<sup>6</sup> Gretchen Morgenson, *A Mortgage Tornado Warning, Unheeded*, N.Y. TIMES, Feb. 5, 2012, at BU1, available at <http://www.nytimes.com/2012/02/05/business/mortgage-tornado-warning-unheeded.html>.

corroborating many of his findings.

And there, apparently, is where it ended. There is little evidence that Fannie Mae's management or board ever took serious action.<sup>7</sup>

"Robo-signing" has become a term of art. One court has defined robo-signing as "complet[ing] affidavits and other essential foreclosure documents without personal knowledge of the documents' veracity and without verification of the documents' contents."<sup>8</sup> Attorneys General in all fifty states investigated these improper foreclosure practices, and entered into a settlement agreement with the five largest banks in America that is estimated to be worth between twenty-six and thirty-nine billion dollars.<sup>9</sup> Further, in light of these practices, courts have gone to the extent of dismissing foreclosure cases.<sup>10</sup> For a time, various financial institutions had even placed a moratorium on foreclosures.<sup>11</sup> However, these moratoria were gradually lifted.<sup>12</sup> A report of the Special Master regarding Bank of America filed on August 15, 2011 concluded with a determination that:

[Bank of America Home Loans] has shown, on a Prima Facie basis, that it has processes and procedures in place which, if adhered to, will ensure that the information set forth in affidavits or certifications submitted in foreclosure proceedings is . . . properly executed and is based upon knowledge gained through a personal review of relevant records which were made in the regular course of business as part of BAC Servicing's regular practice to make such records.<sup>13</sup>

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<sup>7</sup> *Id.*

<sup>8</sup> *Beals v. Bank of America, N.A.*, No. 10-5427, 2011 WL 5415174, at \*3 (D.N.J. Nov. 4, 2011).

<sup>9</sup> This \$26 to \$39 billion settlement is estimated to affect approximately two million homeowners and primarily is to cover the liability sustained by the five largest banks (Bank of America, JP Morgan Chase, Wells Fargo, Citigroup and Ally Financial) in their failure to use due diligence in monitoring the signing of documents related to foreclosure proceedings. *See* Nelson D. Schwartz & Shaila Dewan, *States Negotiate \$26 Billion Settlement for Homeowners*, N.Y. TIMES (Feb. 9, 2012), <http://www.nytimes.com/2012/02/09/business/states-negotiate-25-billion-deal-for-homeowners.html?pagewanted=all>. The settlement is not designed to cover any criminal liability, fraud in the securitization and selling of mortgages, or insurance or tax fraud. Further, the settlement covers only the loans owned by the banks and, therefore, excludes loans owned by government mortgage companies, Fannie Mae and Freddie Mac, which own over half the mortgages in the United States. *See id.* In addition, this settlement does not cover the activities of the Mortgage Electronic Registration System (MERS) and its alleged robo-signing abuses. *Id.* The \$39 billion upper estimate could grow if other banks sign on. *See id.*

<sup>10</sup> *See, e.g., infra* notes 144–46 (showing Ohio and New York cases that were dismissed because of document signing irregularities).

<sup>11</sup> Charles Riley, *Bank of America Halts All Foreclosure Sales*, CNN MONEY (Oct. 8, 2010), [http://www.money.cnn.com/2010/10/08/real\\_estate/bank\\_america\\_50/index.htm](http://www.money.cnn.com/2010/10/08/real_estate/bank_america_50/index.htm).

<sup>12</sup> Alejandro Lazo, *Bank of America Ramps Up Foreclosure Proceedings*, L.A. TIMES BLOG (Sept. 14, 2011, 6:30 PM), [http://latimesblogs.latimes.com/money\\_co/2011/09/bank-of-america-ramps-up-foreclosure-proceedings.html](http://latimesblogs.latimes.com/money_co/2011/09/bank-of-america-ramps-up-foreclosure-proceedings.html).

<sup>13</sup> Report of the Special Master Concerning Bank of America d/b/a BAC Home Loan Servicing, LP, at 28, *In re Residential Mortgage Foreclosure Pleading and Document Irregularities*, No. F-059553-10 (N.J. Super. Ct. Ch. Div. Aug. 15, 2011), *available at* [http://www.judiciary.state.nj.us/superior/report\\_bank\\_of\\_america.pdf](http://www.judiciary.state.nj.us/superior/report_bank_of_america.pdf).

Yet, financial institutions appear to be proceeding cautiously to assure compliance with foreclosure requirements.<sup>14</sup> Such caution may be warranted because some companies and at least one executive have been indicted on criminal charges as a consequence of the practice of robo-signing.<sup>15</sup>

In the midst of this controversy federal lawmakers fashioned a short bill to address some of the issues raised by this burgeoning foreclosure crisis.<sup>16</sup> The bill would have required courts to accept all out-of-state notarizations, including those stamped en masse by computers in a practice that critics say has been improperly used to expedite foreclosure orders.<sup>17</sup> However, President Obama refused to sign the bill after realizing that certain foreclosure documentation standards would actually be loosened by this proposed legislation.<sup>18</sup>

This paper explores the impact of the use of robo-signers and the resulting effect this practice may have upon the stakeholders. A closely related issue explored in this article, albeit on a limited basis, is the use of the Mortgage Electronic Registration Systems (“MERS”). MERS considered itself both a servicer for millions of loans in this country, and a proper party in both foreclosure proceedings and motions for relief from the stay in bankruptcy cases.<sup>19</sup> Due to the sheer volume of foreclosures

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<sup>14</sup> See Nick Timiraos & Alan Zibel, *Reviews Begin for Borrowers Disputing Foreclosures*, WALL ST. J. (Nov. 2, 2011), <http://online.wsj.com/article/SB10001424052970203707504577012130274478996.html>.

<sup>15</sup> While a discussion of the criminal charges is beyond the scope of this article, it is worth noting because the threat of jail time to an individual generally leads to more cooperation and the exposure of new facts. See Roger Bull, *Nevada Indicts 2 LPS Employees on 606 Counts in Robo-Signing Scandal*, FLA. TIMES-UNION (Nov. 17, 2011), <http://jacksonville.com/news/crime/2011-11-17/story/nevada-indicts-2-lps-employees-606-counts-robo-signing-scandal>. In Nevada, two title officers employed by Lender Processing Service, a Jacksonville, Florida-based company, were indicted on multiple felony charges. See *id.* Both were indicted on charges of offering false documents for recording and false certification on certain instruments. Missouri indicted both DocX, a large foreclosure servicing company, and its founder and former president, Lorraine O. Brown, on charges of forgery. See Gretchen Morgenson, *Company Faces Forgery Charges in Mo. Foreclosures*, N.Y. TIMES (Feb. 6, 2012), <http://www.nytimes.com/2012/02/07/business/docx-faces-foreclosure-fraud-charges-in-missouri.html>. Further, the City of San Francisco commissioned an audit of the foreclosures conducted between January 2009 and November 2011 and found that eighty-four percent of said foreclosures contained apparent violations of law. OFFICE OF THE ASSESSOR-RECORDER S.F., FORECLOSURE IN CALIFORNIA: A CRISIS OF COMPLIANCE I (2012).

<sup>16</sup> H.R. 3808, 111th Cong. (2010).

<sup>17</sup> *Id.*

<sup>18</sup> See Jia Lynn Yang & Ariana Eunjung Cha, *Obama Won't Sign Bill that Would Affect Foreclosure Proceedings*, WASH. POST (Oct. 7, 2010, 11:31 PM), <http://www.washingtonpost.com/wp-dyn/content/article/2010/10/07/AR2010100704254.html> (stating that President Obama vetoed legislation concerning the foreclosure crisis).

<sup>19</sup> The issue of standing, which has been the subject of litigation in numerous cases where MERS asserts itself as a proper party in these proceedings, is not within the scope of this paper. In motions for relief from the stay in bankruptcy cases, MERS is seeking to be allowed to proceed with a foreclosure, which has been stayed due to the filing of a bankruptcy proceeding by the mortgagor/borrower. See generally 11 U.S.C. § 362 (2010).

processed through MERS, mass processing of documents seems inherently problematic absent adequate controls—the solution for which may be as simple as increased staffing along with other controls.

We begin with a general discussion of foreclosure law to provide the framework for the discussion including types of foreclosures, redemption of property rights, and state and federal statutory/regulatory requirements. We then discuss how courts have dealt with the failures to comply with foreclosure procedures, looking at the types of defects that may have existed in those cases, and particularly where those legal deficits result from the use of robo-signers. This paper emphasizes the legal implications of such deficits, whose negative implications are exacerbated by the passage of time, unraveling transactions that have a direct impact upon people's lives. That is, we explore the impact upon the stakeholders in this system, from the lenders, to the title insurers, to a possible lessor of premises whose legal underpinnings have unraveled. Or, like a stack of cards, each standing precariously and leaning upon the other—when one falls, a total collapse results.

## I. THE LAW OF FORECLOSURE

### A. Types of Foreclosure Proceedings<sup>20</sup>

Real estate law is primarily state-law specific, particularly with respect to foreclosure proceedings.<sup>21</sup> The two main types of foreclosure

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<sup>20</sup> It is noteworthy to refer to the history of foreclosure discussed by Justice Scalia:

The history of foreclosure law also begins in England, where courts of chancery developed the “equity of redemption”—the equitable right of a borrower to buy back, or redeem, property conveyed as security by paying the secured debt on a later date than “law day,” the original due date. The courts’ continued expansion of the period of redemption left lenders in a quandary, since title to forfeited property could remain clouded for years after law day. To meet this problem, courts created the equitable remedy of foreclosure: after a certain date the borrower would be forever foreclosed from exercising his equity of redemption. This remedy was called strict foreclosure because the borrower’s entire interest in the property was forfeited, regardless of any accumulated equity. The next major change took place in 19th-century America, with the development of foreclosure by sale (with the surplus over the debt refunded to the debtor) as a means of avoiding the draconian consequences of strict foreclosure. Since then, the States have created diverse networks of judicially and legislatively crafted rules governing the foreclosure process, to achieve what each of them considers the proper balance between the needs of lenders and borrowers. All States permit judicial foreclosure, conducted under direct judicial oversight; about half of the States also permit foreclosure by exercising a private power of sale provided in the mortgage documents. Foreclosure laws typically require notice to the defaulting borrower, a substantial lead time before the commencement of foreclosure proceedings, publication of a notice of sale, and strict adherence to prescribed bidding rules and auction procedures. Many States require that the auction be conducted by a government official, and some forbid the property to be sold for less than a specified fraction of a mandatory presale fair-market-value appraisal.

*BFP v. Resolution Trust Corp.*, 511 U.S. 531, 541–42 (1994) (citations omitted).

<sup>21</sup> See Prentiss Cox, *Foreclosure Reform Amid Mortgage Lending Turmoil: A Public Purpose Approach*, 45 HOUS. L. REV. 683, 698 (2008) (stating that “[s]tate law . . . controls the overwhelming

proceedings can be categorized as either judicial or non-judicial.<sup>22</sup> Twenty states allow only judicial foreclosures,<sup>23</sup> five states allow only non-judicial foreclosures,<sup>24</sup> with the remaining states allowing for both procedures.<sup>25</sup> States nevertheless each may have distinct procedural requirements.<sup>26</sup>

Judicial foreclosures are generally far more time consuming since court hearings may be scheduled, and other court notification processes are involved. Yet, the procedures from state to state can vary significantly.<sup>27</sup> The process may occur generally as follows:

the filing of a foreclosure complaint and *lis pendens* notice; the service of process on all parties whose interests may be prejudiced by the proceedings; a hearing before a judge or a master in chancery who reports to the court; the entry of a decree or judgment; the notice of sale; a public sale, usually conducted by a sheriff; the post sale adjudication as to the disposition of the foreclosure

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majority of foreclosures”).

<sup>22</sup> See *id.* at 699. A third type of foreclosure proceeding, which is actually a sub- category of a judicial foreclosure, is “strict foreclosure.” Only two states, New Hampshire and Vermont, currently allow strict foreclosures. For strict foreclosure proceedings, the lender uses the judicial process to bring an action against the defaulting borrower. If the borrower does not pay the mortgage within a court ordered specified time, the property goes directly back to the lender, without necessity of a sale. See *id.* at 700; see also *BFP*, 511 U.S. at 541.

<sup>23</sup> See *Foreclosure Laws and Procedure by State*, REALTYTRAC, <http://www.realtytrac.com/foreclosure-laws/foreclosure-laws-comparison.asp> (last visited Feb. 13, 2012) (giving a state-by-state synopsis of foreclosure procedures).

<sup>24</sup> *Id.*

<sup>25</sup> *Id.*

<sup>26</sup> See, for example, *supra* note 22, where the differences in the judicial foreclosure statutes are discussed.

<sup>27</sup> For example, in New York the foreclosure process takes an average of 900 days. See *Foreclosure Activity at 40-Month Low*, REALTYTRAC (May 12, 2011), <http://www.realtytrac.com/content/press-releases/foreclosures-activity-at-40-month-low-6578>. In contrast, in Texas, the process typically can be completed in as little as twenty-seven days. See *Texas Foreclosure Laws*, REALTYTRAC, <http://www.realtytrac.com/foreclosure-laws/texas-foreclosure-laws.asp> (last visited June 3, 2011) (stating that the foreclosure process in Texas can take as little as twenty-seven days but the process generally takes about three months). New York does not allow non-judicial foreclosures. See *supra* note 23. New York had provided for non-judicial foreclosures under limited conditions, however, this provision was repealed in 2009; the automatic repeal of this non-judicial foreclosure provision was included in a 1998 law and apparently had nothing to do with the current financial crisis. Act of July 7, 1998, ch. 231, § 2, 1998 N.Y. Sess. Laws 701 (McKinney). On the other hand, Texas allows non-judicial foreclosures where there is a “power of sale” clause in the mortgage document. See TEX. PROP. CODE ANN. § 51.002 (West Supp. 2012); see also Brandon Bennett, *Secured Financing in Russia: Risks, Legal Incentives, and Policy Concerns*, 77 TEX. L. REV. 1443, 1466 (1999) (stating that power of sale clauses are required for non-judicial foreclosures). Commentators suggest that much of the backlog in New York likely relates to the backlog in the court system since only judicial foreclosures are normally conducted in New York due to the intricacies of the prior non-judicial foreclosure process. Yuki Nogichi, *Foreclosure Influx Causes Backlog in Some States*, NPR (March 16, 2012), <http://www.npr.org/2012/03/16/148685887/foreclosure-influx-causes-backlog-in-some-states>. In addition, in October of 2010, New York courts began imposing an “affirmation rule” as a result of the concerns, which are the subject of this paper, requiring attorneys to affirmatively attest to the accuracy of their court submissions. See Andrew Keshner, *Foreclosures Plunge as Lawyers Adjust to New Affirmation Rule*, N.Y. L.J. (Dec. 16, 2010), available at <http://vaughnweberlaw.com/2010/12/16/foreclosures-plunge/> (reviewing the changes in foreclosure filing because of the affirmation rule).

proceeds; and if appropriate, the entry of a deficiency judgment.<sup>28</sup>

Non-judicial foreclosures, on the other hand, tend to be less involved and time consuming.<sup>29</sup> Normally, if there is a “power of sale” clause<sup>30</sup> contained in the deed of trust or mortgage instrument, this clause provides the authority for the lender to proceed with foreclosure through a streamlined auction process.<sup>31</sup> “After varying degrees of notice, the mortgaged property is sold at a public sale by a third party, such as a sheriff or a trustee, or by the mortgagee.”<sup>32</sup>

Nevertheless, even non-judicial foreclosures can be involved and complex.<sup>33</sup> Furthermore, in all states there are additional time periods involved where the debtor is allowed opportunities for redeeming the property prior to,<sup>34</sup> and in some cases even after, the date of the scheduled foreclosure.<sup>35</sup>

### B. Equity of Redemption and Statutory Redemption Periods

States that allow the debtor an opportunity to redeem the property prior to foreclosure through what is termed the “equity of redemption,” give the debtor an opportunity to become current on the payments in arrears before the date and time scheduled for the foreclosure.<sup>36</sup> Once the foreclosure sale is completed the debtor’s “equity of redemption” is extinguished.<sup>37</sup>

<sup>28</sup> Grant S. Nelson & Dale A. Whitman, *Reforming Foreclosure: The Uniform Nonjudicial Foreclosure Act*, 53 DUKE L.J. 1399, 1403 (2004).

<sup>29</sup> See Brian M. Heaton, Note, *Hoosier Inhospitability: Examining Excessive Foreclosure Rates in Indiana*, 39 IND. L. REV. 87, 91 (2005) (asserting that the “power of sale” clause allows for the sale of the defaulted property without going through a court proceeding, and instead only requires the proper advertising of the property before a foreclosure sale).

<sup>30</sup> See Melissa B. Jacoby, Essay, *Home Ownership Risk Beyond a Subprime Crisis: The Role of Delinquency Management*, 76 FORDHAM L. REV. 2261, 2271 (2008) (asserting that a non-judicial foreclosure is allowed when a “power of sale” clause is in the original loan agreement).

<sup>31</sup> See Nelson & Whitman, *supra* note 28, at 1403 (stating that non-judicial foreclosures are generally less complicated and less costly than judicial foreclosures).

<sup>32</sup> See *id.* at 1403–04 (giving the general steps to non-judicial foreclosure proceedings).

<sup>33</sup> The previous non-judicial foreclosure process in New York was so complex that it was rarely utilized. See *Q&A: Foreclosing Outside of Court*, N.Y. TIMES, Aug. 9, 1998, <http://www.nytimes.com/1998/08/09/realestate/q-a-230251.html>.

<sup>34</sup> This is typically referred to as the “equity of redemption.” See Morris G. Shanker, *Will Mortgage Law Survive? A Commentary and Critique on Mortgage Law's Birth, Long Life, and Current Proposals for Its Demise*, 54 CASE W. RES. L. REV. 69, 75 (2003) (stating that equity of redemption is the debtor’s absolute right to pay the underlying debt prior to foreclosure and keep the property).

<sup>35</sup> This is commonly known as the “statutory redemption” period. See Dale A. Whitman, *Chinese Mortgage Law: An American Perspective*, 15 COLUM. J. ASIAN L. 35, 72 (2001) (asserting that statutory redemption is a debtor’s statutory right to redeem property after foreclosure and is available in about twenty states).

<sup>36</sup> All states allow the debtor to become current on the mortgage prior to the date and time scheduled for foreclosure, so long as the full payment is tendered in a form acceptable to the lender (usually certified funds). See Shanker, *supra* note 34, at 74–81 (giving a thorough discussion of the history of the equity of redemption). The mortgage instrument then becomes reinstated and is in full force and effect as if the debtor had not fallen behind in the payments. See *id.*

<sup>37</sup> *Id.* at 76 (explaining that once the debtor defaulted by failing to pay the mortgage debt by the

In addition to the additional time frame allowed by the “equity of redemption,” about twenty states afford the debtor the opportunity to redeem the property after the foreclosure has actually been completed.<sup>38</sup> This is known as “statutory redemption.”<sup>39</sup> Through the statutory redemption process there is an established timeframe within which the debtor must cure any default by tendering payment to the lender in an acceptable form.<sup>40</sup> Usually certified funds will be required.

### C. Federal Governmental Requirements

In addition to these state-defined foreclosure processes, there may also be federal governmentally-prescribed requirements affecting the foreclosure of mortgages. For example, for loans insured by the Federal Housing Administration (“FHA”) lenders are required to mail a booklet to borrowers entitled “How to Avoid Foreclosure,” and offer the debtor an opportunity for an interview.<sup>41</sup>

In addition to FHA requirements, for the extra protection of debtors who may be on active duty in the military, the Service Members Civil Relief Act<sup>42</sup> requires the filing of an affidavit averring that the affected mortgagor is not on active duty.<sup>43</sup> If the mortgagor is on active duty at the time of the default, then a court hearing may be conducted and other protective provisions apply as well.<sup>44</sup>

legal terms of the mortgage, the creditor had the right to foreclose but the debtor could still retain the property by paying the mortgage debt in full prior to the effective foreclosure).

<sup>38</sup> See Whitman, *supra* note 35, at 72.

<sup>39</sup> See *id.*

<sup>40</sup> See Nelson & Whitman, *supra* note 28, at 1438–39 (stating that the statutory periods of redemption commonly range from six months to two years).

<sup>41</sup> 24 C.F.R. § 203.602 (2011) (requiring the mortgagee to send the mortgagor a delinquency notice on an HUD form or a form approved by HUD no later than two months after any delinquency).

<sup>42</sup> Servicemembers Civil Relief Act, Pub. L. No. 108–189, 117 Stat. 2835 (codified as amended at 50 U.S.C.A. § 501–596(b) (West 1990)).

<sup>43</sup> 50 U.S.C.A. app. § 521 (West Supp. 2012).

<sup>44</sup> § 533. Mortgages and trust deeds

(a) Mortgage as security. This section applies only to an obligation on real or personal property owned by a servicemember that—

- (1) originated before the period of the servicemember's military service and for which the servicemember is still obligated; and
- (2) is secured by a mortgage, trust deed, or other security in the nature of a mortgage.

(b) Stay of proceedings and adjustment of obligation. In an action filed during, or within 9 months after, a servicemember's period of military service to enforce an obligation described in subsection (a), the court may after a hearing and on its own motion and shall upon application by a servicemember when the servicemember's ability to comply with the obligation is materially affected by military service—

- (1) stay the proceedings for a period of time as justice and equity require, or
- (2) adjust the obligation to preserve the interests of all parties.

(c) Sale or foreclosure. A sale, foreclosure, or seizure of property for a breach of an obligation described in subsection (a) shall not be valid if made during, or within 9 months after, the period of the servicemember's military service except—

- (1) upon a court order granted before such sale, foreclosure, or seizure with a return

Finally, one of the most powerful federal governmental requirements that impacts foreclosures is Title 11 of the U.S. Bankruptcy Code<sup>45</sup> (“the Code”). Specifically, section 362(a) of the Code contains a provision for automatically staying a foreclosure proceeding (among numerous other creditor actions).<sup>46</sup> Note, however, that there are exceptions and limitations to the automatic stay such that it does not apply in every case.<sup>47</sup> In addition, after notice and a hearing, a creditor can request that the stay be lifted, annulled, modified, or conditioned under certain defined circumstances,<sup>48</sup>

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made and approved by the court; or

(2) if made pursuant to an agreement as provided in section 107 [section 517 of this Appendix].

(d) Misdemeanor. A person who knowingly makes or causes to be made a sale, foreclosure, or seizure of property that is prohibited by subsection (c), or who knowingly attempts to do so, shall be fined as provided in title 18, United States Code, or imprisoned for not more than one year, or both.

50 U.S.C.A. app. § 533 (West Supp. 2012).

<sup>45</sup> 11 U.S.C. §§ 101–1532 (2006).

<sup>46</sup> Section 362 states (in pertinent part):

a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of—

(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title.

11 U.S.C.A. § 362(a)(1) (West 2012).

<sup>47</sup> 11 U.S.C.A. § 362(a) (West 2012).

<sup>48</sup> Section 362(d) states that:

On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay—

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest;

(2) with respect to a stay of an act against property under subsection (a) of this section, if—

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization;

(3) with respect to a stay of an act against single asset real estate under subsection (a), by a creditor whose claim is secured by an interest in such real estate, unless, not later than the date that is 90 days after the entry of the order for relief (or such later date as the court may determine for cause by order entered within that 90-day period) or 30 days after the court determines that the debtor is subject to this paragraph, whichever is later—

(A) the debtor has filed a plan of reorganization that has a reasonable possibility of being confirmed within a reasonable time; or

(B) the debtor has commenced monthly payments that—

(i) may, in the debtor's sole discretion, notwithstanding section 363(c)(2) [11 USCS § 363(c)(2)], be made from rents or other income generated before, on, or after the date of the commencement of the case by or from the property to each creditor whose claim is secured by such real estate

including where the creditor's interest is not adequately protected.<sup>49</sup> Most pertinent to this discourse is that disputes regarding the validity of the foreclosure process often arise in the context of a bankruptcy proceeding, particularly where MERS is the party seeking relief from the automatic stay, and there is a challenge on the basis of "standing."<sup>50</sup>

## II. DEFECTS IN THE FORECLOSURE PROCESS

As has been discussed, the procedures required to be performed in connection with effectuating a valid foreclosure can be complex in many jurisdictions. These procedures reflect the need to assure that rights to property ownership are neither extinguished nor created in an environment with inadequate legal circumscriptions. It is not difficult to perceive that there may be inexorable consequences where faulty attendance to mandated requirements results in a foreclosure done in error. And, unfortunately, as the scenarios in Part IV depict, these consequences can be viral if they are not remedied before spreading from the borrower to other parties having an interest in the subject property.<sup>51</sup>

### A. Exercising Due Diligence

Mortgage lenders and their servicers have a general responsibility to exercise due diligence when initiating and processing documentation for foreclosures.<sup>52</sup> However, there are a myriad of opportunities to fail to diligently comply with, or fail to conform to, processes requisite to a valid

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(other than a claim secured by a judgment lien or by an unmatured statutory lien); and

(ii) are in an amount equal to interest at the then applicable nondefault contract rate of interest on the value of the creditor's interest in the real estate; or

(4) with respect to a stay of an act against real property under subsection (a), by a creditor whose claim is secured by an interest in such real property, if the court finds that the filing of the petition was part of a scheme to delay, hinder, or defraud creditors that involved either—

(A) transfer of all or part ownership of, or other interest in, such real property without the consent of the secured creditor or court approval; or

(B) multiple bankruptcy filings affecting such real property. If recorded in compliance with applicable State laws governing notices of interests or liens in real property, an order entered under paragraph (4) shall be binding in any other case under this title purporting to affect such real property filed not later than 2 years after the date of the entry of such order by the court, except that a debtor in a subsequent case under this title may move for relief from such order based upon changed circumstances or for good cause shown, after notice and a hearing. Any Federal, State, or local governmental unit that accepts notices of interests or liens in real property shall accept any certified copy of an order described in this subsection for indexing and recording.

11 U.S.C.A. 362(d) (West Supp. 2012).

<sup>49</sup> 11 U.S.C.A. 362(d)(1) (West 2012).

<sup>50</sup> See *supra* note 19.

<sup>51</sup> See *infra* Part IV.

<sup>52</sup> See *Jones v. Flowers*, 547 U.S. 220, 225, 239 (2006).

foreclosure proceeding. Generally, proper parties must be established;<sup>53</sup> the property description must be accurate;<sup>54</sup> financial information must be analyzed and validated;<sup>55</sup> the circumstances adherent to justifying the foreclosure process itself must be assessed and confirmed;<sup>56</sup> parties must be notified;<sup>57</sup> and the person(s) assuring all requirements have been met must indeed do those things, and aver through a notarization process that all was done as stated.<sup>58</sup>

It is difficult to believe that due diligence has been consistently achieved when some mortgage companies employ only one person to sign up to 10,000 foreclosure affidavits per month.<sup>59</sup>

#### B. Relevant Causes of Action Against Defective Foreclosure Proceedings

A person alleging a foreclosure was conducted improperly may do so based upon various legal theories, regardless of whether the foreclosure process is judicial or non-judicial. For one, a borrower may claim lack of due process of law because the lender failed to send proper notice of the foreclosure proceeding to the borrower.<sup>60</sup> In the case of *Jones v. Flowers*,<sup>61</sup> the borrower alleged that the lender failed to send proper notice of the borrower's redemption rights. However, notice had been mailed, but the certified mail notice was returned unclaimed.<sup>62</sup> The court held that since the notice was returned unclaimed, other reasonable steps should be taken to notify the owner in order for the notice to comport with the requirements of the Due Process Clause of the Fourteenth Amendment.<sup>63</sup>

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<sup>53</sup> See *In re Maisel*, 378 B.R. 19, 21 (Bankr. D. Mass. 2007) (filing motion for relief from automatic stay because documents showed that the creditor had no interest in the property until four days after the filing of the motion for relief of the automatic stay).

<sup>54</sup> See generally Christopher L. Peterson, *Foreclosure, Subprime Mortgage Lending, and the Mortgage Electronic Registration System*, 78 U. CIN. L. REV. 1359, 1395 (2010) (stating that there are many cases where a faulty property description has rendered a mortgage invalid).

<sup>55</sup> See generally *Mielke v. Bank of Am. Home Loans Servicing, LP*, No. 2:10-cv-11576, 2011 U.S. Dist. LEXIS 41617, at \*21–22 (E.D. Mich. 2011).

<sup>56</sup> See generally *U.S. Bank Nat'l Ass'n v. Spencer*, No. BER-F-10591, 2011 N.J. Super. LEXIS 746, at \*35–36 (N.J. Super. Ct. Ch. Div. Mar. 22, 2011).

<sup>57</sup> See generally *Jones*, 547 U.S. at 234, 238 (showing that proper notice to interested parties is crucial).

<sup>58</sup> See generally Peterson, *supra* note 54, at 1394–95.

<sup>59</sup> See Cha, *supra* note 1 (reporting that the head of the Ally Financial foreclosure document processing team hand-signed 10,000 affidavits per month, not in the presence of a notary).

<sup>60</sup> See *United States v. Ford*, 551 F. Supp. 1101, 1102–05 (N.D. Miss. 1982) (alleging that lender failed to provide personal notice of foreclosure proceedings which court notes is a due process claim); *Small Engine Shop, Inc. v. Cascio*, 878 F.2d 883, 886 (5th Cir. 1989) (alleging that lender foreclosed without actual notice after borrower's request for notice which amounted to lack of due process of law).

<sup>61</sup> 547 U.S. 220 (2006).

<sup>62</sup> *Id.* at 224.

<sup>63</sup> See *id.* at 234–35.

Proper notice is of prime importance in foreclosure actions. Notice of both the foreclosure action and any rights of redemption, along with other types of notices are required in varying degrees in different jurisdictions.<sup>64</sup>

Another claim available to borrowers pertains to unfair<sup>65</sup> and deceptive trade practices.<sup>66</sup> Violations of state laws that prohibit unfair and deceptive trade practices fall within the purview of different regulatory bodies and the states' attorneys general offices.<sup>67</sup> In light of the existence of the various regulating bodies, those who service mortgage loans in a manner that is considered unfair and deceptive—for instance, by not verifying defaults sufficiently or failing to adequately notify borrowers of a looming foreclosure—may face the possibility of impending legal action.<sup>68</sup>

An action closely related to the concept of unfair and deceptive trade practices is an action for fraud.<sup>69</sup> Although more difficult to prove since intent to defraud would have to be shown,<sup>70</sup> fraud is among the causes of action for which such claims are being brought, particularly by individual borrowers.<sup>71</sup> In addition to these claims, negligence is a cause of action individual claimants use as a basis in these types of cases.

<sup>64</sup> See *id.* at 225–27.

<sup>65</sup> See Henry N. Butler & Jason S. Johnson, *Reforming State Consumer Protection Liability: An Economic Approach*, 2010 COLUM. BUS. L. REV. 1, 74 (2010) (“The current FTC definition of an unfair act is one that ‘causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or competition.’”) (citing Federal Trade Commission Act Amendments of 2006, Pub. L. No. 109-455, § 3, 120 Stat. 3372 (codified at 15 U.S.C. § 45(n))).

<sup>66</sup> See *id.*

The definition of a deceptive act currently involves the examination of a series of factors: “First, there must be a representation, omission or practice that is likely to mislead the consumer. . . . Second, we examine the practice from the perspective of a consumer acting reasonably in the circumstances. . . . Third, the representation, omission, or practice must be a ‘material’ one.”

(citing Letter from James C. Miller III, Chairman, to Rep. John D. Dingell, Chairman of House Comm'n on Energy & Commerce, FTC Policy Statement on Deception (Oct. 14, 1983), available at <http://www.ftc.gov/bcp/policystmt/ad-decept.htm>).

<sup>67</sup> See Bob Cohen, Annotation, *Right to Private Action Under State Consumer Protection Act—Preconditions to Action*, 117 A.L.R. 5th 155, at \*2a (2004) (acknowledging the existence of various regulating bodies that attempt to address unfair or deceptive business practices, including the FTC, the legislature through enactment of laws, and the attorney general).

<sup>68</sup> See Press Release, Attorney General Tom Miller, Miller Statement on 50 State Mortgage Foreclosure Group (Oct. 13, 2010), [http://www.state.ia.us/government/ag/latest\\_news/releases/oct\\_2010/robo\\_signing.html](http://www.state.ia.us/government/ag/latest_news/releases/oct_2010/robo_signing.html) (“Attorney General Tom Miller is leading a 50-state bipartisan mortgage foreclosure working group, as part of a coordinated national effort by states to review the practice of so-called ‘robo-signing’ within the mortgage servicing industry.”).

<sup>69</sup> See Miriam H. Baer, *Linkage and the Deterrence of Corporate Fraud*, 94 VA. L. REV. 1295, 1323 n.103 (“That the defendant has made a representation in regard to a material fact . . . [t]hat such representation is false; . . . [t]hat such representation was not actually believed by the defendant, on reasonable grounds, to be true; . . . [t]hat it was made with intent that it should be acted on[;] . . . that it was acted on by [the plaintiff] to his damage; and . . . [t]hat in so acting on it the [plaintiff] was ignorant of its falsity, and reasonably believed it to be true.”) (emphasis added) (quoting *Dev. Co. v. Silva*, 125 U.S. 247, 250 (1888)).

<sup>70</sup> See *id.*

<sup>71</sup> See *GMAC Mortg. v. McKeever*, No. 08-459-JBC, 2011 U.S. Dist. LEXIS 53983, at \*6 (E.D.

The case of *Beals v. Bank of America*<sup>72</sup> concerns, in part, systemic flaws in the country's mortgage foreclosure practice relating to alleged instances of robo-signing.<sup>73</sup> The plaintiffs' claims arose out of allegations that the defendant bank and loan servicer did not fulfill a contractual agreement to modify the payment schedule as it had agreed.<sup>74</sup> In this case, the plaintiffs raised seven counts as a basis of the claim for relief, including

- (1) breach of contract[;]
- (2) breach of the covenant of good faith and fair dealing[;]
- (3) fraud and intentional misrepresentation[;]
- (4) constructive fraud and negligent misrepresentation[;]
- (5) negligent processing of loan modifications and foreclosure[;]
- (6) violation of the New Jersey Consumer Fraud Act . . . and
- (7) violation of the Fair Debt Collection Practices Act ("FDCPA").<sup>75</sup>

The *Beal* court made several rulings in connection with the motion to dismiss filed by the defendants. Significantly, the court concluded that plaintiffs had not stated a claim for negligence, and that defendants "owe[d] plaintiffs no duty independent of the contract."<sup>76</sup> The court stated that "even if defendants were negligent, plaintiffs' damages 'do not arise from any duty imposed by law but rather result from [the] alleged breach of contract.'"<sup>77</sup> Plaintiffs had asserted that the defendant's duty

emanate[d] from the testimony of Bank of America executives before Congress, in which one stated that Bank of America ha[d] a responsibility to be fair . . . and [that] those who work[ed] with [the company] in connection with foreclosure proceedings, also ha[d] an obligation to do [their] best to protect the integrity of those proceedings.<sup>78</sup>

The court did not agree with plaintiff's contention that the statement created a duty and, thereby, a basis for a cause of action in negligence.<sup>79</sup>

With respect to the causes of action for breach of contract and breach of the covenant of good faith and fair dealing, the court denied the motion to dismiss where it had found a contract actually existed.<sup>80</sup> In addition, with respect to all claims for fraud the court denied the motion to dismiss.<sup>81</sup> The basis for the court's denial was that the plaintiffs put forth a sufficient claim for fraudulent and negligent misrepresentations in connection with actions by the defendants to modify the loan agreement.<sup>82</sup>

Ky. May 19, 2011) (pleading that MERS committed fraud in forging a foreclosure document but failing to prove that MERS possessed the document with intent to defraud).

<sup>72</sup> *Beals v. Bank of Am., N.A.*, No. 10-5427 KSH, 2011 WL 5415174 (D.N.J. Nov. 4, 2011).

<sup>73</sup> *See id.* at \*3.

<sup>74</sup> *Id.* at \*2.

<sup>75</sup> *Id.* at \*4.

<sup>76</sup> *Id.* at \*16.

<sup>77</sup> *Id.* (quoting *Saltiel v. GSI Consultants*, 788 A.2d 268, 281 (2002)).

<sup>78</sup> *Id.* at \*15.

<sup>79</sup> *Id.* at \*16.

<sup>80</sup> *Id.* at \*19.

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* at \*14–15.

With respect to allegations by one of the plaintiffs that the assignment of the plaintiff's mortgage involved a known robo-signer, the court noted that the plaintiff did not allege that the assignment was substantively defective.<sup>83</sup> Nonetheless, the court acknowledged that "the validity and legitimacy of assignment documents are an important part of the foreclosure process . . . ."<sup>84</sup> From the plaintiff's perspective, the court viewed this defect essentially as part and parcel of causing the plaintiff to be "led down a path to believe that he was subject to foreclosure but that defendants would agree to (or at least seriously consider) a modification."<sup>85</sup> Further, as pertains to the specific cause of action for misrepresentation, the court found sufficient basis for the plaintiff's claims that he was led to believe that a modification of the loan terms would be agreed to.<sup>86</sup> With respect to the claim for violation of the Fair Debt Collection Practices Act, the court determined that the defendants were not "debt collectors" within the meaning of the FDCPA<sup>87</sup> since the mortgage was not in default at the time it was assigned to defendant bank or at the time the mortgage servicer began servicing the loan.<sup>88</sup>

In a Florida foreclosure case, the District Court of Appeals reversed an order of summary judgment in favor of the lender, finding that the evidence was insufficient to support a judgment of the amount due and owing on the note and mortgage.<sup>89</sup> In this case the court found that the affidavit of the "specialist" for the loan servicer was inadmissible hearsay since the servicer had no personal knowledge regarding the veracity or accuracy of the data which was obtained from the bank computer.<sup>90</sup> This case puts loan servicers on notice that courts are closely scrutinizing the processes these servicers use to verify loan foreclosure documents.

It must also be noted that several courts have dismissed claims by homeowners bringing actions against lenders in connection with robo-signing.<sup>91</sup> In a class action suit in Maine, the district court dismissed three

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<sup>83</sup> *Id.* at \*14.

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> *Id.*

<sup>87</sup> *Id.* at \*18.

<sup>88</sup> *Id.*

<sup>89</sup> *See* Glarum v. LaSalle Bank Nat'l Ass'n, 83 So. 3d 780, 783 (Fla. Dist. Ct. App. 2011).

<sup>90</sup> *Id.* at 782.

<sup>91</sup> *See* Bass v. Ameriquest Mortg. Co., 2011 U.S. Dist. LEXIS 148729 (D. Haw. Dec. 27, 2011) (granting defendant lenders summary judgment for plaintiff's claims for breach of contract, negligent infliction of emotional distress, and mortgage fraud related to alleged robo-signing); Cerecedes v. U.S. Bankcorp, 2011 U.S. Dist. LEXIS 75559 (C.D. Cal. July 11, 2011) (granting defendant's motion to dismiss plaintiff's claims that defendant was negligent and committed unfair business practices in connection with unsubstantiated allegations of robo-signing); Davis v. Countrywide Home Loans, 2011 U.S. Dist. LEXIS 22270 (S.D. Ind. March 4, 2011) (dismissing the plaintiff's claim—that defendant violated the Racketeer Influenced and Corrupt Organizations Act by using robo-signers—for lack of subject matter jurisdiction); Wells Fargo Bank v. Kosar, 2011 Pa. Dist. & Cnty. Dec. LEXIS 244 (Pa. Cnty. Ct. Sept. 15, 2011) (allowing lender to cure the defect in a verification form upon which

of the four claims against GMAC Mortgage.<sup>92</sup> GMAC Mortgage filed affidavits in foreclosure cases without personal knowledge of the facts contained in the affidavits. The court ruled that the proper method of attacking an existing judgment is to seek a reversal.<sup>93</sup> The court did allow a fourth claim, which is based upon the Maine Unfair Trade Practices Act.<sup>94</sup>

And in Florida, the first robo-signing case that was scheduled to go to court was settled.<sup>95</sup>

The first robo-signing case scheduled to get to the Florida Supreme Court for oral arguments has been settled out of court by Bank of New York Mellon and the homeowner.

The settlement comes as a disappointment to homeowners in foreclosure who have been trying to challenge the use of fraudulent documents used by banks to expedite foreclosure orders for Florida circuit courts.

Enrique Nieves III of Ice Legal in Royal Palm Beach had been preparing for oral arguments in *Roman Pino v. BNY Mellon* after the Fourth District Court of Appeal upheld the bank's right to voluntarily dismiss the case . . . .

With the settlement, the Fourth District Court of Appeal ruling remains the law in every court in Florida. In *Pino v. BNY Mellon*, the homeowner requested an evidentiary hearing when the bank tried to re-initiate a foreclosure that had been stalled because of a questionable assignment of mortgage documents.

The bank was trying to go forward with a cured document and Nieves was arguing they could not proceed until the original fraud allegation was aired on its merits.

Palm Beach Circuit Judge Meenu Sasser noted the bank had voluntarily dismissed the original foreclosure petition and that case could not be reopened. She treated the second foreclosure petition as an entirely separate matter, and Nieves appealed.

The Fourth District Court of Appeal sided with Sasser in an *en banc* decision. But there was a dissent, mainly on grounds that an attempt to perpetrate a fraud on the court was still actionable. The majority panel acknowledged the issue was of great public importance due to the rampant use of questionable documents; that certification helped Nieves put the case before the Supreme Court.<sup>96</sup>

These cases illustrate the kinds of issues courts are facing in regard to systemic flaws in the robo-signing debacle. Although robo-signing per se may not always be directly related to the cause of action arising in each case, it certainly has a tangential impact. As was stated by the *Beals* court,

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plaintiff's sued over an instance of robo-signing).

<sup>92</sup> *Bradbury v. GMAC Mortgage*, 780 F. Supp. 2d 108, 111 (D. Me. 2011) (ruling that the proper way to attack an existing judgment is get the existing judgment reversed).

<sup>93</sup> *Id.* at 111.

<sup>94</sup> *Id.* at 112.

<sup>95</sup> Adolfo Pesquera, *Key Robo-signing Case Ends With Settlement*, FLA. BUS. REV., July 29, 2011, available at LEXIS, Doc. No. 1202508929895.

<sup>96</sup> *Id.*

“the validity and legitimacy of assignment documents are an important part of the foreclosure process.”<sup>97</sup>

### C. MERS

It is a common practice in the mortgage industry for mortgages to be assigned to multiple, successive parties.<sup>98</sup> More often than not, the assigned mortgage becomes but a segment of a bundled package of usually homogenous mortgage documents in which investors take a shared interest. This process is known as securitization.<sup>99</sup>

The Mortgage Electronic Registration Systems, Inc. (“MERS”) was created as a vehicle to track mortgage securitization transactions.<sup>100</sup> MERS was created because many of the state recording systems were deemed by the major lenders as slow, costly, and antiquated.<sup>101</sup> The problem with state recording systems is not new. Many title insurance companies have maintained their own private records of real estate transactions since the 1960s to combat foreseeable problems with the state systems.<sup>102</sup> Lenders saw an opportunity to speed up recording procedures with MERS while at the same time reducing the cost of each transaction; costs were reduced by computerizing the tracking of each assignment transaction, and MERS eliminated the need to pay recording fees for each assignment transaction since the “recording” is accomplished within the computerized system instead of within the public land records.<sup>103</sup> MERS was also supposed to make foreclosures more efficient.<sup>104</sup> However, ultimately, MERS may have made the foreclosure process more inefficient by sacrificing reasonable documentation for increased speed of the transaction.<sup>105</sup> Originally,

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<sup>97</sup> *Beals v. Bank of America*, No. 10-5427, 2011 U.S. Dist. LEXIS 128376, at \*42 (D. N.J. Nov. 4, 2011).

<sup>98</sup> See Tanya Marsh, *Foreclosures and the Failure of the American Land Title Recording System*, 111 COLUM. L. REV. SIDEBAR 19, 23 (2011) (asserting that the great volume of mortgage assignments caused the county recording systems to become too untimely and costly; therefore, failing to meet the needs of mortgage banking).

<sup>99</sup> Robin S. Golden & Sameera Fazili, *Raising the Roof: Addressing the Mortgage Foreclosure Crisis Through a Collaboration Between City Government and a Law School Clinic*, 2 ALB. GOV'T L. REV. 29, 37–38 (2009) (“The mortgage backed securities are extremely sophisticated financial instruments governed primarily through contractual arrangements, known as pooling and servicing agreements (PSAs), negotiated between all the parties to the transaction.”).

<sup>100</sup> See Peterson, *supra* note 54, at 1361 (describing the purpose for the creation of MERS).

<sup>101</sup> See Marsh, *supra* note 98, at 20 (citing the perceived deficiencies of land title recording procedures).

<sup>102</sup> Peterson, *supra* note 54, at 1366 (explaining the historical problems with the state recording systems).

<sup>103</sup> *Id.* at 1368–69; see also Gerald Korngold, *Proposed Regulatory Solution: Legal and Policy Choices in the Aftermath of the Subprime and Mortgage Financing Crisis*, 60 S.C. L. REV. 727, 741–43 (2009) (discussing some of the benefits of MERS).

<sup>104</sup> See Peterson, *supra* note 54, at 1362.

<sup>105</sup> See *id.* at 1361–62. Compounded with the concern regarding robo-signing is the issue of whether MERS is a proper party in a foreclosure action. One major line of attack being used in cases attacking the validity of foreclosures is whether the party bringing the foreclosure action is indeed a proper party. That is, does the entity whose name the foreclosure is brought under have standing to

mortgages were recorded with public land records in the names of the lenders and then assigned to MERS to make all subsequent assignments within the MERS system. However, later lenders decided they could save even more money by making the first public record recording in the name of MERS as the mortgagee.<sup>106</sup> Probably no one took a really serious look at the speed versus reasonable documentation problem in the early 1990s when MERS was being conceived. However, now many courts are closely analyzing the dichotomy and flaws that are being exposed, and due to this scrutiny, MERS now prohibits members from filing foreclosures in the name of MERS.<sup>107</sup>

The problem of reasonable documentation became more exacerbated in the mid-1990s when lenders and brokers began the securitization of subprime loans.<sup>108</sup> No one could have predicted in the mid-1990s the magnitude of the financial meltdown in 2007, which would precipitate the need to foreclose on 8.1 million loans.<sup>109</sup> Because there may be multiple assignments on each loan, there are tens of millions of unrecorded assignments on the potential foreclosures. These unrecorded assignments can cause problems because of a lack of transparency, especially for the borrower. The nonpublic MERS records make it extremely difficult, if not impossible, for distressed borrowers to know whom to deal with in order to work out their problems.<sup>110</sup>

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bring the action? The problem is this: MERS considers itself both a “nominee of the lender,” although they never actually lent money, and “their successors and assigns,” although they have not entered into a formal assignment agreement, and a “beneficiary,” even though MERS does not have any interest in the underlying note. *See id.* at 1375–87 (discussing the issue of standing relative to the issues of being a nominee and a successor and assigns). MERS also normally assigns the deed of trust and note to a securitized loan trust which argues that it is the owner of the loan. *See In re Vargus*, 396 B.R. 511, 515–16 (Bankr. C.D. Cal. 2008).

Courts have grappled with the issue of whether MERS has standing to foreclose. Some courts in interpreting state statutes have ruled that MERS was not a proper party. In *In re Salazar*, the U.S. Bankruptcy Court for the Southern District of California determined that MERS was only a nominal beneficiary and was not the beneficiary at the time of the foreclosure sale and thus did not satisfy the requirement that the bank have a recorded beneficial interest in the property. *In re Salazar*, 448 B.R. 814, 819–22 (Bankr. S.D. Cal. 2011), *rev'd*, *In re Salazar*, 470 B.R. 557 (S.D. Cal. 2012) (finding that both U.S. Bank and MERS are entitled to invoke the power of sale). Other courts have validated MERS as a proper party. In *Gomez vs. Countrywide*, the U.S. District Court held that MERS as a nominee was essentially an agent and thus gave MERS the right to foreclose on the deed of trust. *See Gomez v. Countrywide*, No. 2:09-cv-01489-RJ-LRL, 2009 U.S. Dist. LEXIS 108292, at \*6, \*7 (D. Nev. Oct. 26, 2009).

<sup>106</sup> *See* Peterson, *supra* note 54, at 1371.

<sup>107</sup> *Foreclosures and Bankruptcies*, MERS, <http://www.mersinc.org/foreclosures/index.aspx> (last visited Feb. 11, 2012) (stating that “MERS System Membership Rule 8 prohibits Members from initiating foreclosure proceedings in the name of Mortgage Electronic Registration Systems, Inc. (‘MERS’)”).

<sup>108</sup> *See* Peterson, *supra* note 54, at 1367–68 (showing the typical process of securitizing a subprime loan).

<sup>109</sup> *See* David R. Greenberg, Comment, *Neglected Formalities in the Mortgage Assignment Process and the Resulting Effects on Residential Foreclosures*, 83 TEMP. L. REV. 253, 253 (2010) (commenting on the vast number of potential foreclosures created by the economic meltdown).

<sup>110</sup> *See* Korngold, *supra* note 103, at 743–46 (discussing transparency and efficiency problems

By 2007, MERS had sixty million loans and sixty percent of new loan originations.<sup>111</sup> With this high volume of new loan originations and 8.1 million potential foreclosures, coupled with tens of millions of unrecorded assignments, it is a small wonder that MERS, and mortgage service companies in the name of MERS, had to resort to an assembly line process whereby agents of MERS signed affidavits regarding the propriety of foreclosure documentation without reviewing the loan file.

Two Ohio cases brought to the forefront some serious problems with how some financial institutions dealt with the documentation of assignments in foreclosure actions.<sup>112</sup> These cases were dismissed without prejudice because the lenders could not document that the assignments of the notes and mortgages were executed prior to the filing of the foreclosure actions as required by law.<sup>113</sup> A more troubling problem was an appearance of a cavalier attitude of the mortgage lending industry toward compliance with foreclosure procedures.<sup>114</sup> As Judge Boyko stated, “[t]he [financial] institutions seem to adopt the attitude that since they have been doing this for so long, unchallenged, this practice equates with legal compliance. Finally put to the test, their weak legal arguments compel the Court to stop them at the gate.”<sup>115</sup>

The furor created by the robo-signing put the spotlight on MERS and the practices of its members, which have been characterized as shoddy workmanship.<sup>116</sup> In *Bank of New York v. Mulligan*,<sup>117</sup> the court ordered the bank to provide three documents as follows:

(1) [A]n affidavit of facts either by an officer of plaintiff BNY or someone with a valid power of attorney from plaintiff BNY and personal knowledge of the facts; (2) an affidavit from Ely Harless describing his employment history for the past three years, because Mr. Harless assigned the instant mortgage as Vice President of MORTGAGE ELECTRONIC REGISTRATION SYSTEMS, INC. (MERS) and then executed an affidavit of merit for assignee BNY as Vice President of BNY’s alleged attorney-in-fact without any power of attorney; and, (3) an affidavit from an officer of plaintiff BNY explaining why it purchased the instant nonperforming loan from MERS, as nominee for DECISION ONE

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with MERS); *see also* Peterson, *supra* note 54, at 1398–99 (discussing the problem of identifying the proper note holders and the actual amount of the debt owed).

<sup>111</sup> Peterson, *supra* note 54, at 1373–74.

<sup>112</sup> *See In re Foreclosure Cases*, Nos. 1:07CV2282, 07CV2532, 07CV2560, 07CV2602, 07CV2631, 07CV2638, 07CV2681, 07CV2695, 07CV2920, 07CV2930, 07CV2949, 07CV2950, 07CV3000, 07CV3029, 2007 WL 3232430 (N.D. Ohio Oct. 31, 2007); *see also In re Foreclosure Cases*, Nos. 07-cv-166, 07-cv-190, 07-cv-226, 07-cv-279, 07-cv-423, 07-cv-534, 07-cv-536, 07-cv-642, 07-cv-670, 07-cv-706, 07-cv-714, 07-cv-727, 07-cv-731, 07-cv-963, 07-cv-999, 07-cv-1047, 07-cv-1091, 07-cv-1119, 07-cv-1150, 2007 U.S. Dist. LEXIS 90812 (S.D. Ohio Nov. 27, 2007).

<sup>113</sup> *In re Foreclosure Cases*, Nos. 1:07CV2282, 07CV2532, 07CV2560, 07CV2602, 07CV2631, 07CV2638, 07CV2681, 07CV2695, 07CV2920, 07CV2930, 07CV2949, 07CV2950, 07CV3000, 07CV3029, 2007 WL 3232430, at \*3 (N.D. Ohio Oct. 31, 2007).

<sup>114</sup> Judge Boyko opined, “[p]laintiff’s, ‘Judge, you just don’t understand how things work,’ argument reveals a condescending mindset and quasi-monopolistic system where financial institutions have traditionally controlled, and still control, the foreclosure process.” *Id.* at \*3 n.3.

<sup>115</sup> *Id.*

<sup>116</sup> *See* Marsh, *supra* note 98, at 24.

<sup>117</sup> *Bank of N.Y. v. Mulligan*, 28 Misc. 3d 1226A (N.Y. Sup. Ct. 2010).

MORTGAGE COMPANY, LLC [ ].<sup>118</sup>

The court dismissed the foreclosure action, with prejudice, in response to the bank's failure to provide proper documentation of an assignment.<sup>119</sup>

Thus, the MERS system presents a potentially infectious issue. With such vast numbers of documents being processed through this system in an abbreviated period of time, is it endemic to such a system that summary and shallow controls will be employed? And if the aforementioned defect causes a loosening of the threads, to what consequence? To determine the answers to these and other questions, Eric T. Schneiderman, Attorney General of New York, recently filed suit against MERS, banks, and lending servicing companies.<sup>120</sup> This suit is not affected by the landmark settlement reached by the states and the five large mortgage services.<sup>121</sup> The suit avers that MERS, in conjunction with the banks, filed foreclosures with no legal right to do so, and indiscriminately used "certifying officers" to execute and file with courts defective documents which rendered said documents false, deceptive, and/or invalid.<sup>122</sup> The suit asks the court to declare said practices illegal, to enjoin said practices, to mandate that the parties correct all defects in title caused by said practices, and for money damages.<sup>123</sup> Furthermore, the states of Massachusetts and Delaware have filed deceptive practices suits, which are not affected by the settlement.<sup>124</sup>

### III. THE STAKEHOLDERS

Barbara Borrower, recently widowed, has been thrust into the role of being not only the sole breadwinner but the family financier as well. Finances befuddle her simply because she is untrained and inexperienced. Her focus had always been on raising her and her deceased husband's two children and making sure they were properly educated. She lived in her home with her family for more than 20 years. Mr. Borrower had recently

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<sup>118</sup> *Id.* at \*1–2.

<sup>119</sup> *Id.* at \*25.

<sup>120</sup> Press Release, N.Y. Att'y Gen. Eric T. Schneiderman, A.G. Schneiderman Announces Major Lawsuit Against Nation's Largest Banks For Deceptive & Fraudulent Use Of Electronic Mortgage Registry (Feb. 03, 2012), <http://www.ag.ny.gov/press-release/ag-schneiderman-announces-major-lawsuit-against-nation%E2%80%99s-largest-banks-deceptive> (last visited Feb. 11, 2012) (delineating the legal and factual bases for said suit).

<sup>121</sup> See Schwartz & Dewan, *supra* note 9.

<sup>122</sup> See *A.G. Schneiderman Announces Major Lawsuit Against Nation's Largest Banks For Deceptive & Fraudulent Use Of Electronic Mortgage Registry*, *supra* note 120.

<sup>123</sup> *Id.*

<sup>124</sup> Press Release, Att'y Gen. Martha Coakley, Five National Banks Sued by AG Coakley in Connection with Illegal Foreclosures and Loan Servicing (Dec. 01, 2011), <http://www.mass.gov/ago/news-and-updates/press-releases/2011/five-national-banks-sued-by-ag-coakley.html> (last visited Feb. 12, 2012) (announcing a comprehensive suit against large banks due to the mortgage crisis alleging robo-signing); Press Release, Att'y Gen. Joseph R. "Beau" Biden, III, Biden: Private National Mortgage Registry Violates Delaware Law (Oct. 27, 2011), <http://attorneygeneral.delaware.gov/media/releases/2011/law10-27.pdf> (announcing a suit against MERS for deceptive trade practices).

refinanced the mortgage loan and used the equity they had built up in the family home, Greenacres, to purchase his long desired cabin cruiser. Unfortunately, as fate would have it, he only got to use it a few times before expiring from a massive heart attack while out on the cabin cruiser. Mrs. Borrower sold the cabin cruiser but lacking the sophistication to negotiate beneficial terms, she received far less for it than they paid.

Mrs. Borrower has decided to move out of Greenacres and into an apartment, signing a one-year lease. She has realized that she can rent Greenacres for more than the cost to rent the apartment. And besides, Greenacres is more house than she needs since her children are now grown. However, sentimentality and the current market conditions restrain her from selling. With her low paying clerical job, combined with the rent she will receive, she is able to continue making the mortgage payments on the home. Mrs. Borrower rented Greenacres to Lisa Lessee and her family of three children. Unfortunately, due to the market downturn, the tenant, Lisa Lessee, lost her job. Because tenants were difficult to find in the existing market climate, and out of sympathy, Mrs. Borrower decided to let Lisa Lessee stay in Greenacres for a reduced rent. As one might expect, Mrs. Borrower found herself struggling to make her mortgage payments.

Mrs. Borrower received a notice from a bank whose name she did not recognize, initiating a non-judicial foreclosure process. After fretting for many weeks with no apparent solution, Mrs. Borrower contacted her children and they agreed to help. Mrs. Borrower sent the funds to Big Bank to stop the foreclosure process. To her shock and horror, Mrs. Borrower received a notice in the mail stating that the foreclosure process had been completed and that any opportunity to redeem the property had long since expired. She tried to contact Big Bank but was told her mortgage was sold to another bank (for various reasons much of her mail did not get forwarded to her new apartment). When she finally reached the bank to whom her note and mortgage had been sold, she was informed that the funds she sent were insufficient to cure the default and that the funds were not received on time.

Bob and Betty Buyer purchased Greenacres at the foreclosure proceeding, taking out a loan with American Bank.<sup>125</sup> The Buyers evict Lisa Lessee and her family. Confident that they will prevail in a pending action to quiet title, Mr. and Mrs. Buyer, with their three children in tow, move in to Greenacres as their primary residence.

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<sup>125</sup> An empirical study done in 1985 of foreclosure sales in Onondaga County, New York, during 1979, gives us a factual backdrop of who buys at the actual foreclosure sale, what happens to the proceeds and who benefits from a foreclosure. See generally Steven Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure—An Empirical Study of Mortgage Foreclosure and Subsequent Resale*, 70 CORNELL L. REV. 850 (1985).

There are numerous stakeholders whose interests can be affected by the unraveling of the cords that once seemed tightly woven and enmeshed to construct and complete a real estate transaction. A primary purpose of the legal process for completing a real estate transaction in this country is to provide societal stability and durability.<sup>126</sup> It is unlikely that the resulting impact of “undoing what has been done” in these matters will be a positive one for all of the parties involved. Indeed, there can be a direct, far reaching and consequential negative impact upon a variety of parties and positions. Metaphorically, once the cords are unconstrained, they quickly whip out, or with determined and minimal effort steadily unravel, until the cord becomes nothing more than a loose conglomeration of bare thread—weakened and fragile.

Arguably, but not necessarily, the most affected by such a calamitous event is the borrower/homeowner. The borrower presumably precipitated the process by failing to meet her contractual obligations. Yet the borrower may shift from being the victimizer, i.e. the naughty debtor who apparently failed to meet her contractual obligations, to the victim of an illegal ousting from what is, in most cases, one’s most vital and inestimable material possession—the place of residence.<sup>127</sup> On the other hand, the pre-eviction, foreclosed-upon homeowner may rejoice in the extra time allowed by the legal deficits exposed in the foreclosure process. For the homeowner who has indeed caused a default in his or her contractual obligations, time can be a coveted commodity—allowing that extra breathing space to make necessary arrangements and adjust to the trauma of being dispossessed of his or her abode.

#### Barbara Borrower

In the case of Barbara Borrower, she no longer resides at Greenacres. Thus, she does not have to suffer the consequence of no longer having a place to live. Nonetheless, she will suffer repercussions. First of all, she loses Greenacres and the tangible reminders of the cherished memories it holds. Secondly, she will no longer be the beneficiary of any equity that might have remained or been recovered when market conditions possibly

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<sup>126</sup> See *Social Benefits of Homeownership and Stable Housing*, NAT. ASS’N OF REALTORS (Aug. 2010), <http://www.realtor.org/sites/default/files/social-benefits-of-stable-housing-2012-04.pdf> (studying and assessing the social benefits of stability within the housing market).

<sup>127</sup> The Washington Post reported that a study by the University of Pennsylvania’s School of Medicine found that forty-seven percent of the homeowners going through foreclosure showed signs of depression, and thirty-seven percent showed signs of severe depression. *Study Centers on Foreclosure’s Stress on Family Life*, WASH. POST (Feb. 16, 2010), available at <http://www.washingtonpost.com/wp-dyn/content/article/2010/02/12/AR2010021204156.html>. Anecdotally, *USA Today* reported a tragic event in Prineville, Oregon, where an elderly couple, faced with the prospect of post foreclosure eviction, closed themselves and their four retriever dogs up in their home, allowing it to be filled with toxic fumes from their car. See Stephanie Armour, *Foreclosures Take an Emotional Toll on Many Homeowners*, USA TODAY (May 16, 2008), [http://www.usatoday.com/money/economy/housing/2008-05-14-mortgage-foreclosures-mental-health\\_N.htm](http://www.usatoday.com/money/economy/housing/2008-05-14-mortgage-foreclosures-mental-health_N.htm).

improved in the future. In this case, however, any equity that existed was quickly consumed by transaction costs involved with the foreclosure process. Thirdly, although the landlord-tenant relationship between Mrs. Borrower and Lisa Lessee has been terminated upon foreclosure, Mrs. Borrower may be liable to Ms. Lessee for breach of contract and for the return of any security deposit she may have obtained.<sup>128</sup>

#### Lisa Lessee and Her Children

Lisa Lessee and her three children moved in with her sister. Lacking a substantial source of income, she had no alternative. The sporadic child support she receives from her ex-husband is insufficient to pay a normal rent. As a victim of a foreclosed-upon landlord, Ms. Lessee is not alone.<sup>129</sup> Professor Rodriguez-Dod states, “[r]eportedly, approximately 40% of families being evicted—about 70,000 renters—have been displaced because their landlords’ properties were foreclosed. It is estimated that in the northeastern United States up to 50% of foreclosures involve renters. And in the Chicago area, foreclosure-related tenant evictions tripled from 2007 to 2008.”<sup>130</sup>

But Ms. Lessee, and others similarly situated, are not without rights. On May 20, 2009, President Obama signed into law the Protecting Tenants at Foreclosure Act of 2009 (“PTFA”).<sup>131</sup> By this law, Ms. Lessee, as a bona fide tenant, would be entitled to ninety days notice prior to being evicted from the foreclosed upon property; however, in this case since the Buyer family will be living on the property as their primary residence, Ms. Lessee is not entitled to remain in possession of the premises after the ninety-day period.<sup>132</sup> In addition to the PTFA, the foreclosure crisis has spawned other laws, both federal and state, to ameliorate the impact upon tenants in varying degrees of forcefulness.<sup>133</sup>

#### The Buyer Family

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<sup>128</sup> If Lisa Lessee had been a tenant at the time Barbara Borrower had executed the mortgage, such as where Borrower refinanced the property while Lessee was a tenant, then Lessee’s right would have priority over the mortgagee. See Vicki Been & Allegra Glashauser, *Tenants: Innocent Victims of the Nation’s Foreclosure Crisis*, 2 ALB. GOV’T L. REV. 1, 10–11 (2009) (giving an overview of parties’ priorities in foreclosure).

<sup>129</sup> See generally Eloisa Rodriguez-Dod, *Stop Shutting the Door on Renters: Protecting Tenants from Foreclosure Evictions*, 20 CORNELL J. L. & PUB. POL’Y 243 (2010).

<sup>130</sup> *Id.* at 245. Professor Rodriguez-Dod further notes:

Anecdotes abound about foreclosures and consequent evictions of renters. Tenants dutifully paying their monthly rent have found themselves forced out of their rental homes because landlords defaulted on their mortgages. Many have been low-income tenants who receive little notice before being uprooted and have little savings to afford a move to new housing.

*Id.* at 245.

<sup>130</sup> *Id.*

<sup>131</sup> Protecting Tenants at Foreclosure Act, Pub. L. No. 111-22, 123 Stat. 1632 (2009).

<sup>132</sup> § 702(a)(2)(A).

<sup>133</sup> See generally Rodriguez-Dod, *supra* note 129, at 248–65 (reviewing the environment of federal and state eviction laws).

Although not quite the untainted purchaser, since the pungent reflux from the agitated foreclosure process cannot reasonably escape notice of one so intricately involved, the purchaser of the foreclosed-upon property nonetheless has a reasonable expectation that correct legal processes were complied with, particularly in a court-ordained foreclosure proceeding. Furthermore, the Buyers have been assured that title has been quieted through that separate judicial process. Mr. and Mrs. Buyer realized that they must give the Lessee family ninety-days notice.<sup>134</sup> They did so with some reluctance and marginal compunction, being fully aware of the circumstances surrounding the underlying default by Mrs. Borrower and the impact upon her tenant. Yet they too had a family to provide for and needed Greenacres since it was within walking distance of the school they preferred for their children, and was just a few blocks from the city subway system to facilitate both of them getting to and from work. Greenacres was perfect.

#### Big Bank and its Assignees

Mrs. Borrower was foreclosed upon through a non-judicial foreclosure process based upon a power of sale clause in the deed of trust between the Borrowers and Big Bank. Big Bank, consistent with its recapitalization model, assigned the note and mortgage to an assignee. Because of the volume of mortgage loans Big Bank makes, it had subscribed to MERS soon after it was established in the mid 1990s, thus minimizing the transaction costs involved in the assignments. As the nominee for Big Bank and its assigns, MERS was responsible for assuring that all the necessary documents relating to foreclosure are processed and that the affidavits averred to by its document processors are properly done. Because of the age of the original loan from the Borrowers, the loan originated in the name of Big Bank and was later assigned to MERS. Since MERS was the mortgagee of record in the county land records, the foreclosure proceedings were commenced on behalf of Big Bank's assignee by MERS.

Big Bank's assignee was thankful that the Buyers purchased the property since they had a bulging inventory of bank-owned properties. The assignee was not interested in being in the real estate business. The homes they owned barely sold for the outstanding balance on the mortgage loan.

#### The Title Insurance Companies

WeGotYourBack Title Insurers provided title insurance to the Buyers in connection with the mortgage loan they used to purchase Greenacres. However, the title insurance policy contained an exception for anything pertaining to defects in the foreclosure process itself.

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<sup>134</sup> Protecting Tenants at Foreclosure Act § 702(a)(1).

Guaranty Title Insurers provided title insurance to American Bank, the Buyers' lenders. The policy specifically covered any defects in connection with the foreclosure process.

American Bank

American Bank provided a loan to the Buyers to purchase the property at foreclosure.

IV. THE CORD UNRAVELS: DEFECTIVE FORECLOSURES AND THEIR  
IMPACT UPON STAKEHOLDERS

It has been discovered through testimony made by a document processor for MERS in connection with the action to quiet title that the affidavits in connection with the foreclosure on Greenacres were not actually verified in the presence of a notary. Far more significantly, after this revelation, a careful review of the documentation was made and the assignee realized that indeed the payments sent by Mrs. Borrower from the funds her children gave her were not timely recorded to her account, causing invalid late fees to accrue. Had they been properly recorded, Mrs. Borrower clearly would have cured the default on her loan prior to the expiration of the statutory period for redemption. In spite of the fact that Mrs. Borrower did not contest the foreclosure, due to the egregious behavior of both MERS and the assignee for Big Bank, the court denies the action to quiet title, deeming the foreclosure process defective. The threads rapidly begin to whip apart.

Who ends up in actual possession of Greenacres depends upon the law of the jurisdiction in which the property is located. In a case where it is a "technical" defect, such as failure to properly notarize an affidavit or obtain proper service as well as underlying facts justifying a foreclosure, it is likely the court will allow a party to re-foreclose with any necessary damages being paid by the offending party.<sup>135</sup> In these cases the foreclosure action might be dismissed without prejudice.<sup>136</sup> However, as in the facts of this case, where the homeowner actually was not in default of the mortgage obligation, a court may reinstate her status as the owner of Greenacres in a suit to set aside the foreclosure action, and void the mortgage on Greenacres obtained by the Buyers in favor of American Bank.<sup>137</sup>

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<sup>135</sup> See Marvin N. Bagwell & Robert F. Bedford, *What Is the Probable Effect of Defective Foreclosure Documents Under New York Law?*, ONE ON ONE, Summer 2011, at 26 (asserting that the courts will most likely not return the property to the former property owner).

<sup>136</sup> See Chris Markus, Ron Taylor & Blake Vogt, *From Main Street to Wall Street: Mortgage Loan Securitization and New Challenges Facing Foreclosure Plaintiffs in Kentucky*, 36 N. KY. L. REV. 395, 397 (2009) (discussing the circumstances under which Judge Boyko dismissed Ohio cases without prejudice, e.g. failing to provide proper documentation of the assignment); see also Boyko cases cited *supra* note 113.

<sup>137</sup> See *Lona v. Citibank, N.A.*, 202 Cal. App. 4th 89, 106 (2011) ("Other grounds for setting aside a trustee's sale in the case law include assertions that . . . the borrower was not in default . . ."); see also *Bank of N.Y. v. Mulligan*, No. 51509U, slip op., 2010 N.Y. Misc. LEXIS 4056, at \*1-2, \*8, \*12-

If the foreclosure action is set aside, American Bank might seek recourse from Guaranty Title Insurance Company, which in turn might seek recourse from Big Bank, the original lender. Or American Bank can seek relief directly from Big Bank and its assigns for the monies these institutions received to pay off the debt owed by Mrs. Borrower.

The Buyers might suffer the greatest hardship of all since they may be forced to leave Greenacres. Also, since their title policy excluded defects in the foreclosure process itself, they lack that protection. Of course, since American Bank may obtain satisfaction from Guaranty Title for the amount of the loan it extended to the Buyers, they may be free from that debt obligation (assuming there is no deficiency). The Buyers may also be able to bring an action for unjust enrichment against Big Bank and its assigns for the monies received in the foreclosure action, which might include any down payment made by Buyers to purchase the property.<sup>138</sup> Nevertheless, the Buyers must endure the hardship of relocating and finding a new home. There are a variety of causes of action, rights to subrogation, indemnification and defenses thereto that the various parties may have, and this article does not portend to address them. Rather, its purpose is to highlight the complexities that can result when the cord begins to unravel.

#### V. THE TIE THAT BINDS: REMEDIES AND ENFORCEMENT ACTION

Certainly it would benefit most stakeholders, and, generally, the country's economy as a whole to have a real estate foreclosure system with ingrained stability—a system where due process is given its greatest opportunity to thrive, and where trade practices promote fairness and full disclosure—or at least one which minimizes the opportunity for structural disintegration.<sup>139</sup>

Recent changes have been made in the court system, by state statute, and internally by financial institutions in response to the practice of robo-signing that would have a positive impact on the system. For example, North Carolina passed the Mortgage Debt Collection and Servicing Act in April of 2008<sup>140</sup> to improve mortgage servicing. In Nevada, the State Assembly enacted a law on October 1, 2011, to prevent robo-signing.<sup>141</sup>

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13 (N.Y. Sup. Ct. Aug. 25, 2010) (denying the bank's application for an order of reference with prejudice and cancelling the notice of pendency because of the repeated failure of the bank to provide proper and timely documentation of the loan).

<sup>138</sup> See *Rankin v. Satir*, 171 P.2d 78, 80–81 (Cal. Ct. App. 1946) (holding that constructive trusts are based on the equitable principle that one should not benefit from his own wrongdoing and that this equitable principle should apply to any case where such wrongful benefit is had). Under the equitable unjust enrichment discussed in *Rankin*, the court may impose a constructive trust, which would hold that Big Bank possesses the monies for the benefit of Buyers.

<sup>139</sup> See generally Marsh, *supra* note 98 (giving an overview of the problems within the land title recording system which may have led to a lack of confidence in the land title recording system and contributed to the mortgage companies deciding to create another system).

<sup>140</sup> N.C. GEN. STAT. §§ 45-90–95 (2011).

<sup>141</sup> A.B. 284, 76th Leg., Reg. Sess. (Nev. 2011). According to a *Wall Street Journal* blog,

The law imposes both civil and criminal penalties for misrepresentations regarding real estate titles.<sup>142</sup>

Two title officers in Nevada employed by Lender Processing Service, a Jacksonville, Florida-based company, were indicted on multiple criminal charges.<sup>143</sup> Both were indicted on charges of offering false documents for recording and false certification on certain instruments.<sup>144</sup> The Michigan Attorney General filed criminal subpoenas to out-of-state mortgage processing companies in June 2011 after twenty-three county registers of deeds filed a criminal complaint in connection with robo-signed documents.<sup>145</sup> And the New York Attorney General is conducting a banking probe against certain financial executives that could lead to criminal charges.<sup>146</sup> In Missouri, both DocX, a large foreclosure servicing company, and its founder and former president, Lorraine O. Brown, were indicted on charges of forgery.<sup>147</sup> The California, Delaware and Illinois Attorneys General are also conducting similar investigations.<sup>148</sup>

The New Jersey court system promulgated what have been termed “anti robo-signing” rules to better ensure that a foreclosure is effectuated properly, and in an environment that lessens the opportunity for defects.<sup>149</sup> These rules place heightened responsibilities upon both the financial institutions and the attorneys who represent the financial institutions. In announcing this administrative order, the New Jersey court stated:

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foreclosure filings plummeted by 88% the month after the new law went into effect. See Nick Timiraos, *Nevada Foreclosure Filings Dry Up After ‘Robo-Signing’ Law*, WALL ST. J. BLOG (Nov. 7, 2011, 2:24 PM), <http://blogs.wsj.com/developments/2011/11/07/nevada-foreclosure-filings-dry-up-after-robo-signing-law/>.

<sup>142</sup> A.B. 284, 76th Leg., Reg. Sess., §§ 6, 9, 13, 14 (Nev. 2011).

<sup>143</sup> See Roger Bull, *Nevada Indicts 2 LPS Employees on 606 Counts in Robo-Signing Scandal*, FLA. TIMES-UNION JACKSONVILLE (Nov. 17, 2011, 7:41 PM), <http://jacksonville.com/news/crime/2011-11-17/story/nevada-indicts-2-lps-employees-606-counts-robo-signing-scandal>.

<sup>144</sup> *Id.*

<sup>145</sup> See “*Robo-signing*” of Mortgages Still a Problem, CBS NEWS (July 18, 2011, 8:54 PM), [www.cbsnews.com/2100-201\\_162-20080533.html](http://www.cbsnews.com/2100-201_162-20080533.html).

<sup>146</sup> *Id.*

<sup>147</sup> See Gretchen Morgenson, *Company Faces Forgery Charges in Mo. Foreclosures*, N.Y. TIMES (Feb. 6, 2012), <http://www.nytimes.com/2012/02/07/business/docx-faces-foreclosure-fraud-charges-in-missouri.html>.

<sup>148</sup> See “*Robo-signing*” of Mortgages Still a Problem, *supra* note 145.

<sup>149</sup> Residential Mortgage Foreclosure Pleading and Document Irregularities, Admin. Order 01-2010 (N.J. Dec. 20, 2010) (Glenn, Judge); see N.J. CT. R. 4:64-1(2)

In all residential foreclosure actions, plaintiff’s attorney shall annex to the complaint a certification of diligent inquiry: (a) that the attorney has communicated with an employee or employees of the plaintiff who (i) personally reviewed the documents being submitted and (ii) confirmed their accuracy; and (b) the name(s), title(s) and responsibilities in those titles of the plaintiff’s employee(s) with whom the attorney communicated pursuant to paragraph (2)(A) of this rule.

See also Andrew Keshner, *New Rule Says Attorneys Must Verify Foreclosure Papers*, N.Y. L.J., (Oct. 21, 2010), available at LEXIS (doc-id #1202473628860#) (showing similar requirements now exist in New York).

This order addresses several steps taken by the Judiciary today in an effort to ensure the integrity of the residential mortgage foreclosure process: (1) Judge Jacobson's order directing six lenders and service providers who have been implicated in irregularities in connection with their foreclosure practices to show cause why the processing of uncontested residential mortgage foreclosure actions they have filed should not be suspended; (2) administrative action directing twenty-four lenders and service providers who have filed more than 200 residential foreclosure actions in 2010 to demonstrate affirmatively that there are no irregularities in their handling of foreclosure proceedings, via submissions to retired Superior Court Judge Walter R. Barisonek, who has been recalled to temporary judicial service and assigned as a Special Master; and (3) the adoption of amendments to the Rules of Court and a Notice to the Bar which require plaintiff's counsel in all residential foreclosure actions to file certifications confirming that they have communicated with plaintiff's employees who have (a) personally reviewed documents and (b) confirmed the accuracy of all court filings, and which remind all counsel of their obligations under the New Jersey Rules of Professional Conduct.<sup>150</sup>

In addition, in September 2011, a settlement agreement was reached between the New York State Department of Financial Services and New York Banking Department and Goldman Sachs ("Goldman"), owner of Litton Loan Servicing ("Litton"), providing conditions by which Goldman could sell Litton to Ocwen Financial Corp., a mortgage servicing company.<sup>151</sup> The purpose of the settlement was to make changes in the mortgage servicing industry, such as the practice of robo-signing.<sup>152</sup> The settlement agreement specifically calls for an end to the practice of robo-signing and requires services to withdraw any pending foreclosure action where affidavits may have been robo-signed.<sup>153</sup>

New court rules, statutes, and other efforts are essentially creating a means by which the lack of due process in such situations can be measured. Although there cannot be a perfect solution in an imperfect world (and courts most assuredly will have to continue in their role of determining failures to comply with the system), these efforts may aid in binding the transactional cord of the foreclosure process.

MERS itself will no doubt need to revise its procedures so that its role in the foreclosure process is of a less menacing nature. As stated earlier, MERS is ending the practice of allowing its members to file foreclosure actions in the name of MERS in cases involving assignments.<sup>154</sup> In the future, the lenders are to record mortgage assignments with the county

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<sup>150</sup> See Residential Mortgage Foreclosure Pleading and Document Irregularities, *supra* note 149.

<sup>151</sup> See Agreement on Mortgage Servicing Practices, State of N.Y., Dep't of Fin. Serv., Banking Dep't, available at [www.banking.state.ny.us/clocwen.pdf](http://www.banking.state.ny.us/clocwen.pdf).

<sup>152</sup> *Id.* at 1.

<sup>153</sup> *Id.* at 2.

<sup>154</sup> See *supra* note 113.

clerks responsible for recordation of mortgage instruments before bringing an action for foreclosure.<sup>155</sup>

It seems MERS is having to reinvent itself. Will these changes be adequate? Robo-signing, as it has come to be known, surely will have to cease.

#### CONCLUSION

We refer to the well-known maxim: “if it ain’t broke, don’t fix it.” We apply the converse: “if something’s bad wrong, fix it.” If the reader will excuse the colloquialisms, there is something “bad wrong” with a system that would allow a document processor to review, sign, and verify the voluminous documents necessary to document a foreclosure process in an average of 1.5 minutes. The stability and security of our real estate system demands better. There can be no valid argument against the fact that the numbers of real estate transactions occurring daily have outpaced the historical mechanisms designed to accommodate them. Technological advances should be fully exploited to promote efficiency. Yet, the system should not be allowed to advance at a pace that loosens the threads of its existence.<sup>156</sup>

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<sup>155</sup> Martha Neil, *MERS Changes Rules, Says Mortgage Servicers Must File Assignments with County Before Foreclosing*, A.B.A. J. (July 27, 2011, 6:36 PM), [http://www.abajournal.com/news/article/mers\\_changes\\_rules\\_says\\_mortgage\\_servicers/](http://www.abajournal.com/news/article/mers_changes_rules_says_mortgage_servicers/).

<sup>156</sup> See *Massachusetts Supreme Judicial Court Unanimously Voids Foreclosure Sales Because Securitization Trusts Could Not Demonstrate Clear Chains of Title to Mortgages*.—U.S. Bank National Ass'n v. Ibanez, 941 N.E.2d 40 (Mass. 2011), 125 HARV. L. REV. 827, 834 (2011).

But perhaps the most important lesson of *Ibanez* is that even in an age of rapid innovation in mortgage lending and securitization, mortgage lenders and other participants in the mortgage loan market must still comply with state property law, even if that law has been infrequently examined for over a century and no longer corresponds with widespread mortgage lending industry practices.

See also U.S. Bank Nat. Ass'n v. Ibanez, 941 N.E.2d 40, 55 (2011) (“The legal principles and requirements we set forth are well established in our case law and our statutes. All that has changed is the plaintiffs’ apparent failure to abide by those principles and requirements in the rush to sell mortgage-backed securities.”)