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Shaky Standing

Foreclosure cases identify shoddy record-keeping in mortgage industry

By DOUGLAS S. MALAN

In a rush to collect on home loans turned sour, some companies foreclosing on home owners are overlooking one small detail—the companies can't prove that they have standing in the case.

The frequency with which securities, such as bonds backed by mortgages and notes promising to pay back mortgages, are traded in the financial market can make it difficult to identify the entity that is actually in possession of the note or the mortgage. Thus, when challenged in courts throughout the country, lenders recently have seen lawsuits dismissed for failing to ascertain a basic element of litigation.

It's yet another wrinkle in the fallout of the housing market, in which homes have lost their value, homeowners can't pay their bills and those who banked on the financial security of residential real estate have seen wealth dry up.

New Haven Superior Court Judge Juliet L. Crawford dismissed such a foreclosure case in late April when she concluded that Virginia-based Mortgage Electronic Registration Systems Inc. (MERS) "failed to establish that it held either the mortgage or the note at the time" it filed its lawsuit against Madison homeowner Anna M. Miller, who defaulted on her mortgage in 2004 before she ever made a payment.

"It may sound like a simple idea, but as far as I know, it's the first time a Connecticut court has dismissed a foreclosure for this reason," said Christopher G. Brown, who represented Miller through Begos, Horgan & Brown of Westport. "It is



David W. Hamble

Westport attorney Christopher G. Brown said because the ownership of a mortgage note 'may change many times very quickly, the lenders may lose track of the actual owner at any point.' At that point, he said, the lender may not have standing to bring a foreclosure action.

likely that the same defect that was fatal to the lender in this case exists in many, many other mortgage foreclosure cases."

Miller declined comment.

Securities trading includes constant, high-volume transactions of mortgage-backed bonds on the secondary market, and after repeated transactions, the institution attempting to foreclose typically is not the institution that initially made the loan.

But in Connecticut, whoever holds the note has the right to receive the payments the borrower makes, Brown said.

"Because the ownership of the note may change many times very quickly, the lenders may lose track of the actual owner at any point," he added. "Sometimes the note itself gets lost."

He argued that to foreclose in Connecticut, the plaintiff must have an interest in the note, not just an interest in the mortgage. And because MERS separates the note from the mortgage in its computer system, it cannot foreclose in the state, he said.

The Miller case "gives you the impression that the secondary mortgage market has made a mess of who owns what," he added.

Tracking System

Mortgages often are registered with MERS, which serves as the party listed in the land records for the mortgage lender and servicer. The lender and the servicer (the latter is the company that accepts the mortgage payment) often are separate companies.

MERS's status as original mortgagee is

approved by Fannie Mae, Freddie Mac, Ginnie Mae, the Federal Housing Administration, Veterans Affairs, California and Utah Housing Finance Agencies, “as well as all of the major Wall Street rating agencies,” according to its web site.

The company also contends that ownership information about any loan registered with it does not need to be altered when it is later sold on the secondary market “because MERS remains the nominal mortgagee no matter how many times servicing is traded.”

One Connecticut attorney, who requested anonymity because of a conflict with MERS, said that with respect to non-MERS mortgages traded on the secondary market, “the recording of the assignments of mortgage on the land records to reflect the same is sometimes delayed,” which potentially creates problems in determining standing.

Despite some flaws in the system, “I don’t think this case will have any impact on future foreclosures,” he said. “Connecticut case law and statutory law are clear that the holder of the promissory note is a proper plaintiff in a foreclosure action. The owner of the note and the holder of the note do not necessarily have to be the same person, as the Uniform Commercial Code as adopted in Connecticut makes clear.”

He said his firm makes certain that the note-holder is the party named plaintiff in foreclosure cases.

As of late last month, Brown was preparing to draft his opposition to MERS’s motion to reargue, which was filed by their lawyers at Hunt Leibert Jacobson in Hartford. The firm did not return telephone calls seeking comment.

To further complicate these matters, the right to receive repayment of the principal on the loan can be sold to one party, and the right to receive interest repayment sold to another.

Foreclosure actions sometimes are filed under the belief that the paperwork will be sorted out later in the process to determine who is the note holder, Brown added.

Often, borrowers do not challenge allegations of ownership. In fact, many foreclosure actions throughout the state have been uncontested. When borrowers do appear, they increasingly represent themselves because of their financial troubles, and, Brown said, they may not know what questions to ask about ownership.

“Foreclosure firms are so used to actions just going through unopposed,” said Andrew Pizor, senior loan policy counsel for the



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Connecticut Fair Housing Association. “Now people are paying attention and pointing out the gaps. This is a hot legal issue right now.

“When I raise these defenses in foreclosure proceedings, the stock response [from creditors’ attorneys] is that it’s just a technicality. Well, not paying the mortgage is just a technicality, too.”

Pizor also is an attorney with The Consumer Law Group in Rocky Hill, which is handling several similar cases in Chicago involving Ameriquest, he said.

Borrowers Affected

Other jurisdictions are more familiar with these matters.

One of the well-known opinions emanated from *In re Foreclosure Cases* in the Northern District of Ohio last October when a federal judge dismissed 14 foreclosure actions in one fell swoop because the plaintiffs failed to show standing.

And in late April, a bankruptcy court judge in Massachusetts issued \$650,000 in sanctions against Ameriquest Mortgage Co., Wells Fargo and lawyers in Massachusetts and California for misrepresenting Ameriquest’s status as the holder of a note and mortgage in a Chapter 13 bankruptcy case.

“Unfortunately, the parties’ confusion and lack of knowledge, or perhaps sloppiness, as to their roles is not unique in the residential mortgage industry,” Judge Joel B. Rosenthal



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wrote. “Nor are ‘mistakes’ and misrepresentations limited to the identification of roles played by various entities in this industry.”

While the mortgage industry’s poor record keeping may provide a defense for some home owners, the “find-the-holder” game also has its drawbacks. Trying to find the note holder in order to work out a loan modification agreement also can be a difficult proposition. “It’s a big problem,” said a second Connecticut attorney who requested anonymity because of a conflict with MERS.

“For borrowers trying to work out a loan, maybe they get the runaround from the servicer, the attorney said. “Then when they identify the lender and agree on a modification. Sometimes that modification isn’t honored by the next holder of the loan after it is sold.”

Brown, the Westport attorney who represented Anna Miller, said that he already has been contacted by a New York lawyer seeking advice on how to handle two cases with similar issues of untraceable note/mortgage ownership. He doubts, though, that many troubled homeowners will roll the dice thinking their mortgage can’t be tracked and thereby file applicable defenses in their foreclosure actions.

But the cases have brought to light an important point, in his opinion: “If you’re going to take someone’s house, the least you can do is get your ducks in a row.” ■