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REMARKS AND TESTIMONY OF

R.K. ARNOLD

PRESIDENT AND CEO OF MERSCORP, INC.

BEFORE THE

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

HOUSE FINANCIAL SERVICES COMMITTEE

NOVEMBER 18, 2010

**Remarks of R.K. Arnold
President and CEO of MERSCORP, Inc.
Before the
Subcommittee on Housing and Community Opportunity
House Financial Services Committee**

November 18, 2010

Chairman Waters, Ranking Member Capito and members of the Subcommittee, my name is R.K. Arnold. I am President and CEO of MERSCORP, Inc. Thank you for this opportunity to appear today.

MERS is a member-based organization made up of about 3,000 mortgage lenders. It maintains a nationwide database that tracks changes in servicing rights and ownership interests in mortgage loans. Today MERS is keeping track of 31 million active loans.

The MERS database is important to the mortgage industry because it is the only centralized registry in the industry that uniquely identifies each mortgage loan.

The MERS database is important to individual borrowers because it provides a free and accessible resource where borrowers can locate their servicers, and in many cases, learn who their note-owner is as they change over time.

The MERS database is important to communities because housing code enforcement officers use it to identify who is responsible for maintaining vacant properties.

The MERS database aids law enforcement in the detection of mortgage fraud by tracking liens taken out utilizing the same borrower name, social security number, or property.

MERS also performs another key function: It serves as the mortgagee of record, or the holder of mortgage liens, on behalf of its members as a common agent. MERS is designated as the mortgagee in the mortgage document, and this designation is approved by the borrower at loan closing and then recorded in the appropriate local land records. Serving as the mortgagee enables MERS to receive and maintain updated information as loan servicers and noteholders change over time because we are the central clearinghouse for receipt of mail as mortgagee.

One thing that is always clear in a mortgage document is that if the borrower defaults on his obligation, the lender can foreclose. If MERS holds the mortgage lien, foreclosures can occur in two ways: Either the MERS mortgage interest is reassigned in the land records to the lender holding the note and the lender initiates the action on its own, or MERS initiates the action as the mortgagee of record in the land records.

To do this, MERS relies on specially designated employees of its members, called certifying officers, to handle the foreclosure. To be a MERS certifying officer, one must be an officer of the member institution who is familiar with the functions to be performed, and who has passed an examination administered by MERS. Generally, these are the same individuals who would handle the foreclosure if the lender was involved without MERS. The loan file remains with the servicer as it did before MERS. MERS is not a repository for mortgage documents or promissory notes.

MERS derives its revenues entirely from fees charged to its members—it makes no money from foreclosures. And MERS does not decide when to foreclose. Foreclosure must be authorized by the note-owner (or noteholder), and it must be done in accordance with our strict rules and procedures, which we regularly enforce and refine.

For example, it is a key MERS rule that the note must be presented in a foreclosure, which some states do not require. And we prohibited the use of lost note affidavits in foreclosures done by MERS once we learned they were being used as an excuse to not produce the note.

Earlier this year, when we became aware of acceleration in foreclosure document processing, we grew concerned that some certifying officers might have been pressured to perform their responsibilities in a manner inconsistent with our rules. When we did not get the assurances we thought were appropriate to keep this from happening, we suspended our relationships with those companies.

When we discovered that some so-called “robo-signers” were MERS certifying officers, we suspended their authority until they could be retrained and retested. We are asking our members to provide us with specific plans outlining how they intend to prevent such actions in the future.

Mr. Chairman, all of us at MERS keenly understand that while owning your own home is a dream, losing that home is a nightmare. As professionals who have dedicated ourselves to helping people realize their dream, we are deeply dismayed by the current foreclosure crisis. We take our role as a mortgagee very seriously and we see our database as a key to moving toward better access to information and transparency for consumers.

I am hopeful that as people understand more about MERS and the role we play, they will see that MERS adds great value to our nation’s system of housing finance in ways that benefit not just financial institutions, the broader economy and the government, but—most of all—real people.

Thank you for holding these hearings and inviting MERS to participate.

Your invitation letter contained a number of specific questions that you wished to have addressed. For ease of reference, I have appended them to this short statement.

**Testimony of R.K. Arnold
President and CEO of MERSCORP, Inc.
Before the
Subcommittee on Housing and Community Opportunity
House Financial Services Committee**

November 18, 2010

Chairman Waters, Ranking Member Capito and members of the Subcommittee, my name is R.K. Arnold. I am President and CEO of MERSCORP, Inc. and its subsidiary, Mortgage Electronic Registration Systems, Inc. I appreciate the opportunity to appear before the Committee today to explain what MERS is and isn't, its critical role in our nation's housing finance system, and how MERS has been affected by the current foreclosure crisis.

I have written testimony and an oral statement that has already been delivered to the committee that I would request be made part of the record.

BACKGROUND

MERS is owned by the mortgage industry¹ and operated as a membership organization. Almost all mortgage lenders (about 3,000) are members of MERS, though not all members register all the loans they originate on the MERS® System.² MERS derives its revenue solely

¹ MERSCORP, Inc. is structured as a privately held stock company. Its principal owners are the Mortgage Bankers Association, Fannie Mae, Freddie Mac, Bank of America, Chase, HSBC, CitiMortgage, GMAC, American Land Title Association, and Wells Fargo. MERS is headquartered in Reston VA.

² Members tend to register only loans they plan to sell. Wells Fargo and JP Morgan Chase are the principal members in this regard. They service most of the loans they originate themselves, so registering their retail business on the MERS® System is of less practical value to them. However, when these institutions purchase loans from others, known as their correspondent business, they do require that those loans be registered on the MERS® System.

from its members.³ MERS charges no fees and makes no money from mortgages, from the securitization or transfer of mortgages, or from foreclosures done in its name.

MERS serves two important functions. First, it maintains a database or registry of mortgage loans, keeping track of changes in servicing rights and beneficial ownership interests over the life of the loan. Second, it can be designated by its members to serve as the mortgagee, or the holder of the mortgage lien, in the public land records. This designation is what enables MERS to maintain its accurate database.

MERS AND YOUR MORTGAGE

The mortgage loan process can be confusing and complex to consumers. There is a lot of paperwork generated and many documents to be signed. However, two pieces of paper stand out from the rest as the most important pieces needed so that the consumer can get a mortgage loan. They are: (1) the promissory note, which is a promise by the borrower to repay the loan amount to the lender or noteholder; and (2) the mortgage (also referred to as the “deed of trust” in some states), which establishes a lien against the property as collateral for the loan and allows the lender (or noteholder) to foreclose on the property if the borrower does not repay the loan according to the terms of the promissory note. The person who borrows the money is called the “mortgagor” and the holder of the mortgage is called the “mortgagee.” Once the borrower signs both pieces of paper, the borrower receives the money

³ MERS makes its money through an annual membership fee (ranging from \$264 to \$7,500) based on organizational size, and through loan registration and servicing transfer fees. MERS charges a one-time \$6.95 fee to register a loan and have Mortgage Electronic Registration Systems, Inc. serve as the common agent (mortgagee) in the land records. For loans where Mortgage Electronic Registration Systems, Inc. will not act as the mortgagee, there is only a small one-time registration fee (\$0.97). This is known as an iRegistration. Transactional fees (ranging from \$1.00 to \$7.95) are charged to update the database when servicing rights on the loan are sold from one member to another.

to buy the house. To obtain a mortgage loan, the borrower must agree that the mortgagee has the right to foreclose in the event of a default.

Another important party in the life of a mortgage loan is the loan servicer. The servicer is a company named (by the note-owner) to be the interface between the note-owner and the borrower to collect payments and remit them to the note-owner. It may become the noteholder for purposes of enforcing the terms of the note on behalf of the note-owner.⁴

MERS acts as the designated “common agent” for the MERS member institutions in the land records, which means that MERS holds the mortgage lien on behalf of its members and acts on their behalf as mortgagee. To accomplish this, at the time of the closing, the borrower and lender appoint MERS to be the mortgagee. The designation of MERS is prominently displayed on the mortgage document and is affirmatively approved by the borrower at closing.⁵ After the borrower executes the mortgage document, it is recorded in the public land records with Mortgage Electronic Registration Systems, Inc. noted in the index prepared by the recorder (or clerk) as the mortgagee. Mortgage loan information is then registered on the MERS database.

These two key pieces of paper in a mortgage transaction follow very different paths after they are signed. The mortgage (or deed of trust) is recorded in the county land records where an imaged copy is stored.⁶ The original mortgage document, with recording data added by the county recorder, is returned to the servicer and goes into the servicer’s master loan file.

⁴ The originating lender may be the servicer in some cases.

⁵ A copy of a sample mortgage document can be found in Attachment One. A short summary of MERS prepared by the Mortgage Bankers Association can be found in Attachment Two.

⁶ This action tells the world that there is a lien against the property. This is done to protect the lender’s interest. The recording of the mortgage puts future purchasers on notice of any outstanding claims against the property.

The note is sent to a custodian (usually a regulated depository institution) and is typically bought and sold (and thus trades hands) in the normal course of financial activity.⁷ The servicer undertakes the obligations to service the loan, but servicing rights also may move from one servicing business to another because servicing rights are contract rights, which are bought and sold independent of any sale of the promissory note. MERS does not receive or maintain either the mortgage or the promissory note.

Every time a note or servicer changes hands, a notation of that change is made (electronically) on the MERS[®] System by the members involved in the sale. In this way, changes in servicing rights and beneficial ownership interest in the promissory note are tracked over the life of the loan.⁸

A fundamental legal principle is that the mortgage follows the note, which means that as the note changes hands, the mortgage remains connected to it legally even though it is not physically attached. In other words, the promissory note is enforceable against the property because of the mortgage, but the mortgage instrument itself is not independently enforceable as a debt. This principle is not changed when MERS is the mortgagee because of the agency relationship between MERS and the lender. An agency relationship arises where one party is specifically authorized to act on behalf of another in dealings with third persons, and the legal definition of a “nominee” is a “party who holds bare legal title for the benefit of others.” Here,

⁷ The promissory note is not (and never has been) recorded or stored with the county land records office. The note is a negotiable instrument that can be bought and sold by endorsement and delivery from the seller to the note purchaser. This activity is governed in all fifty states by the Uniform Commercial Code (UCC) Article 3.

⁸ The MERS[®] System is the database; MERSCORP, Inc is the operating company that owns the database; and Mortgage Electronic Registration Systems, Inc (“MERS”) a subsidiary of MERSCORP, Inc., which serves as mortgagee in the land records for loans registered on the MERS[®] System. For discussion purposes, “MERS” may be used in this testimony to refer to all three entities unless specifically stated otherwise.

the language of the mortgage appoints MERS as nominee, or agent, for the lender and its successors and assigns for the purposes set forth therein. The mortgage also grants MERS broad rights, again as nominee for the lender and the lender's successors and assigns, "to exercise any or all" of the interests granted by the borrower under the mortgage, "including but not limited to, the right to foreclose and sell the property; and to take any action required of the lender." Thus, the language of the recorded mortgage authorizes MERS to act on behalf of the lender in serving as the legal titleholder under the mortgage and exercising any of the rights granted to the lender there under.

MERS members affirm this agency relationship with MERS in their membership agreements, which provide that MERS "shall serve as mortgagee of record" with respect to each mortgage loan that the MERS member registers on the MERS[®] System and provide that "MERS shall at all times comply with the instructions of the holder of mortgage loan promissory notes."

THE MECHANICS OF MERS

MERS tracks mortgage loans through an 18-digit identification number called the Mortgage Identification Number (MIN). With one notable exception, the MIN is to a specific home loan what the VIN (Vehicle Identification Number) is to an individual automobile. Like the VIN, the MIN can be assigned at the earliest stage of the product's creation and stays with it for its entire life. However, unlike cars which all get a VIN, not all loans get MINs and are registered on the MERS[®] System. This is because some loan originators do not use MERS when

they do not intend to sell the servicing rights. About half of all loans active in the United States are registered on the MERS® System.

As the mortgagee of record, MERS receives all notices including legal pleadings on actions pertaining to the property such as foreclosure notices and complaints, tax sales and eminent domain actions, among the many other types of mail. MERS forwards those documents electronically to the relevant servicer who will then take the appropriate action to respond on behalf of the note-owner and MERS.

MERS plays an important role for borrowers as the permanent link between borrowers and their servicers. If servicers change or if they declare bankruptcy, the borrower always has a knowledgeable point of contact in MERS. A toll free number, the unique Mortgage Identification Number (MIN) and mailing address are prominently included on the first page of the mortgage document. MERS also maintains a website, which serves as another resource for borrowers. MERS is also a means by which the borrower can easily identify the note-owner.⁹

MERS is not part of the decision-making process as to which mortgage loans the lenders make to borrowers, nor is MERS part of how mortgage loans get securitized. It is the note-owner who decides whether a note should be sold, or transferred to a trust, or ultimately securitized with a pool of other loans.¹⁰ Loans were securitized long before MERS became

⁹ The design of the MERS® System always anticipated and required that borrowers would be able to access the system to determine the servicer of their loans. Providing such information to MERS is a requirement of membership and loan registration. When Congress acted last year to require that borrowers be told when their note is sold and the identity of the new note-owner, MERS established, within a matter of weeks, a new service called Investor ID. Of the 3,000 members of MERS, 97% agreed to disclose the identity of the note-owner through the MERS® System. Fannie Mae opted to be disclosed. Freddie Mac chose not to be disclosed.

¹⁰ The issue of whether transfers of residential mortgage loans made in connection with securitizations are sufficient to transfer title and foreclosure rights is the subject of a "View Point" article entitled "Title Transfer Law 101" by Karen Gelernt that appeared in the October 19, 2010 edition of the *American Banker*. A copy can be found in Attachment Three.

operational, and in fact, there are loans in securities today that do not name Mortgage Electronic Registration Systems, Inc. as the mortgagee. What MERS does is eliminate the expense of repeated assignments, resulting in lower cost for lenders when they sell the loans (represented by the promissory note) to investors. When the note is sold, MERS continues to act as the mortgagee for the new noteholder because the mortgage interest follows the note when it changes hands.

OTHER FACTS ABOUT MERS

The number of loans registered on the MERS® System is substantial. Since its establishment in 1997, about 66 million loans have been registered and tracked on the MERS® System. About half of those loans (about 31 million) are active mortgage loans.

Measured by direct employment, MERS is a relatively small organization. About 50 people work for MERSCORP, Inc. in our Reston, Va. office. Hewlett-Packard is the MERS technology partner and runs the database with an additional 150 people.

In significant ways, MERS is analogous to the Depository Trust and Clearing Corporation (DTCC) that electronically records the assignment of stock and bond certificates, thus eliminating the need to create a new certificate each time a security is bought or sold. The benefit of MERS is similar to that of the DTCC: It reduces the errors associated with paper processes and increases system efficiency.¹¹ Also like the DTCC, MERS is adjacent to the systems that create the data it tracks; it is integrated with, but independent of, its member

¹¹ A 1993, 36-page white paper entitled "Whole Loan Book Entry Concept for the Mortgage Finance Industry" addresses the concepts underlying MERS and the problems it was designed to address. It is available upon request.

organizations. The two primary differences between the organizations are that the DTCC holds title to the financial instrument and that it clears trades between its participants (including the exchange of funds between the counter-parties).

MERS CERTIFYING OFFICERS

Mortgage Electronic Registration Systems, Inc. takes the majority of its actions as the mortgagee through the use of officers commonly referred to as “certifying officers.” From inception, the concept of certifying officers has always been fundamental to the operations of MERS. In the white paper calling for the creation of MERS (referenced in footnote 11), it was recognized that members would need to have a form of authority to act on behalf of MERS when MERS is the mortgagee on their behalf. That authority took the form of electing persons (designated by the member) as officers with limited authority to take certain actions. The offices to which each of these individuals are officially appointed are vice president and assistant secretary. The authority granted to these officers is limited to: (1) executing lien releases, (2) executing mortgage assignments, (3) initiating foreclosures, (4) executing proofs of claims and other bankruptcy related documents (e.g., motions for relief of the automatic stay), (5) executing modification and subordination agreements needed for refinancing activities, (6) endorsing over mortgage payment checks made payable to MERS (in error) by borrowers, and (7) taking such other actions and executing documents necessary to fulfill the member’s servicing duties.

It is important to note that the certifying officers are the same officers whom the lenders and servicers use to carry out these functions even when MERS is not the mortgagee.

MERS has specific controls over who can be identified by its members as a certifying officer. To be a MERS certifying officer, one must be a company officer of the member institution, have basic knowledge of MERS, and pass a certifying examination administered by MERS.

Under the corporate law in Delaware (where MERS is incorporated), there is no requirement that an officer of a corporation also be an employee of that corporation. A corporation is allowed to appoint individuals to be officers without having to employ those individuals or even pay them. This concept is not limited to MERS. Corporations cannot operate without officers; they can and often do operate without employees. It is not uncommon for large organizations to have all its employees employed by an operating company and for those employees to be elected as officers of affiliated companies that are created for other purposes (all corporations are required by law to have officers to act for it). Even for loans where MERS is not the mortgagee, employees of the servicer are generally delegated the power to take actions (e.g., initiate foreclosures) and execute documents (e.g., lien releases and assignments) on behalf of the owner of the loan (and the servicer, in turn, may further delegate such authority to a third-party vendor).

MERS AND FORECLOSURE

When Mortgage Electronic Registration Systems, Inc. is the mortgagee of record, and the borrower is in default on the mortgage, and the note-owner decides to foreclose, foreclosure can be undertaken in one of two ways: Either in the name of MERS, or in the name of the noteholder (which is usually the servicer).

If the noteholder chooses to foreclose in its own name, under the MERS rules, it must be named as mortgagee in the land records. MERS, through the MERS member's designated certifying officer, will execute an assignment to the foreclosing company and the assignment will be recorded in the land records. At this point, MERS no longer holds any legal interest in the mortgage, and it plays no further role in the foreclosure process. Most loans are assigned out of MERS in this way and not foreclosed in the name of MERS.

If the note-owner chooses to have Mortgage Electronic Registration Systems, Inc. foreclose, then the note-owner endorses the note in blank (if it has not already done so), making it bearer paper, and grants possession of the note to a MERS certifying officer. This makes MERS the noteholder. Since MERS is already the mortgagee in the land records, MERS is now able to legally begin the foreclosure process on behalf of the note-owner. The foreclosure is managed entirely by the member institution's MERS certifying officer. This person typically works in the default department within the MERS member institution so they are familiar with the various state foreclosure requirements. The member manages the relationship with the law firm that is handling the foreclosure. The member retains the law firm on behalf of MERS and the member provides the necessary documents and information to the law firm. The member obtains these documents and information from the servicing files and system, which are maintained by the member.

As noted earlier, the MERS certifying officers are the same employee officers who handle foreclosure functions for the MERS member institutions. Whether a foreclosure is initiated in the name of MERS and handled by the certifying officers, or by the lender in its own name, the same people would be doing the work. Likewise, the loan file remains with the

servicer as it did before MERS existed. MERS is not a repository for mortgage documents or promissory notes.

It is important to note that Mortgage Electronic Registration Systems, Inc. only initiates foreclosure when it has been instructed to do so by the servicer (acting on behalf of the note-owner) or directly by the note-owner. MERS has strict rules and procedures governing foreclosure, most notably a requirement that the certifying officer be in possession of the mortgage note when foreclosing in the name of MERS. In addition, pursuant to a 2006 MERS membership rule, no foreclosures in the name of MERS are allowed in the State of Florida. In the event a MERS member contracts out foreclosure operations to a vendor or a law firm, a separate contract is entered into by MERS, the MERS member and the contracted firm for the purpose of establishing our understanding of the obligations of the parties and for the purposes of designating certifying officers. The specific, authorized functions of MERS certifying officers are enumerated in a corporate resolution by which MERS makes the appointment.

Because there is a choice whether a foreclosure is done in the name of the servicer, note-owner or MERS, one might wonder if there is an advantage in choosing one way or the other. The advantage to institutions by foreclosing in the name of MERS is that they do not need to record an assignment from MERS to themselves, saving them time and money. The advantage that some lenders see in not foreclosing in the name of MERS is that the MERS rules are strict and require that the note be produced. If the lender does not want to do this, the MERS member cannot commence a foreclosure action in the name of MERS, but must assign the mortgage out of MERS. This is a major reason why most loans are not foreclosed in the name of MERS.

In 2005, when it became apparent to us that foreclosures undertaken in Florida were relying excessively on lost note affidavits, MERS adopted a rule forbidding the use of lost note affidavits when foreclosures were done in the name of MERS in Florida. That rule was extended nationally in 2006 and is still in effect today. MERS believes that borrowers are entitled to know that the company foreclosing has all of the necessary paperwork and rights to do so. Showing up with the original note provides the borrower and the court with proof that the foreclosing company is the proper party to foreclose.

COMMON QUESTIONS ABOUT MERS STRUCTURE AND ROLE IN MORTGAGE MARKETS

When servicing rights or promissory notes are sold for loans where MERS is not the mortgagee, the usual practice is for the seller to execute and record an instrument assigning the mortgage lien to the purchaser (commonly referred to as an “assignment”). Assignments are not required by law to be recorded in the land records. The primary reason assignments are recorded (in cases where MERS is not the mortgagee), stems from the appointment of servicers to administer the loan on behalf of the mortgage loan owner. In which case, the servicer will be assigned the mortgage lien (thus becoming the mortgagee) in order to receive the service of process related to that mortgage loan. When Mortgage Electronic Registration Systems, Inc. is the mortgagee (i.e., holds the legal title to the mortgage lien), there is no need for an assignment between its members because MERS is the common agent for them. It is not the case that the assignments are now being done electronically through the MERS® System instead of being recorded in the land records. The need for an assignment is eliminated because title to the mortgage lien has been grounded in MERS. Moreover, transfers of

mortgage notes and servicing rights are not recordable transactions (and have never been reflected in the land records) because they are not a conveyance of an interest in real property that is entitled to be recorded; only the transfer of the lien is a conveyance. A promissory note is sold by endorsing the note, and delivering it to the purchasers. Servicing rights are non-recordable contracts rights. Mortgage Electronic Registration Systems, Inc. remains the mortgagee regardless of the number of these non-recordable transfers that may occur during the life of the loan. Upon such sales, the seller and purchaser update the MERS® System of the transfer with an “electronic handshake.” If the purchaser does not confirm the transaction, it is flagged by the MERS® System for follow-up. MERS also audits its members for the accuracy of the information they provide to the MERS® System.

The only reason servicers needed to appear in the county land records before MERS was so they could receive legal notices pertaining to the property. That role is now played by MERS as their common agent. MERS runs a massive mailroom and help desk operation to handle millions of legal notices for its members, which makes it far more efficient and certain that mail will go to the correct place. Today, if a servicer “boxes up” in the middle of the night and disappears, the homeowner can have confidence that legal notices will be delivered to the correct successor company without delay.

The chain of title starts and stops with Mortgage Electronic Registration Systems, Inc. as the mortgagee. MERS, as the agent for the note-owner, can hold legal title for the note-owner in the land records.¹² The basic concept of a recording statute is that a person or company

¹² The essential elements of the legal principles underlying MERS can be found in “MERS Under Attack: Perspective on Recent Decisions from Kansas and Minnesota,” an article by Barkley and Barbara Clark in the February 2010 edition of *Clark’s Secured*

claiming an interest in land protects its interest by recording that interest at the county recorder of deeds office. The recorded document provides constructive notice to the world of the claim. In many states, there is no requirement that a conveyance of real estate must be recorded in the land records. The concept of nominees appearing in the land records on behalf of the true owner has long been recognized. It has never been the case that the true owners of interests in real estate could be determined using the land records.

The use of MERS is in compliance with the statutory intent of the state recording acts. When MERS is the mortgagee, the mortgage is recorded at the county land records, thereby putting the public on notice that there is a lien on the property. As the 1993 white paper describing MERS makes clear, at certain time periods, the flow of assignments were overwhelming the county recorder system, resulting in long backlogs, and in some cases, taking the county recorder over a year to record an assignment. Now that assignments are eliminated because a common agent like MERS is holding the mortgage lien, the land records can operate more efficiently. Multiple assignments can lead to errors and uncertainty in the chain of title because assignments were often missing, incomplete, inaccurate, or misfiled. In situations where the recorded assignment identified the wrong property, the lender had not perfected its lien on the right property but had clouded the title for some unrelated third party.

The MERS® System also complements the county land records by providing additional information that was never intended to be recorded at the county level, namely the information about the mortgage loan servicer, and now, with the addition of MERS® InvestorID, the name of the investor.

Some have raised questions about the reduction of recording fees that has accompanied the elimination of the need to record assignments, and there have been suggestions that these fees are somehow owed or outstanding. Fees are paid for a service performed, and if a document is eliminated because it is no longer legally necessary, no fee is due and owing because there is nothing to record. Another way to look at it is that, because MERS greatly reduces the workload of county recorders, the lower operating expenses of the county recorder's office offsets the loss in fee income. Moreover, it would be the borrower, and not the lender, who ultimately pays the costs of recording assignments, either directly or indirectly.¹³

The use of MERS is based on sound legal principles. Its legal validity has been upheld as it was in the Cervantes, Jackson and In re Tucker cases, to just name a few. While there is much support by courts for the MERS role as a common agent, there have been cases where there have been evidentiary issues, which have resulted in outcomes that do not always let MERS, or its members, foreclose without going back and proving up the right to take action. States have laws that govern foreclosures¹⁴ and when the process is not followed, it can, and should result in a court not allowing it to go forward. In some of these cases, judges wanting more evidence or information about MERS have made comments about MERS. In light of the recent foreclosure crisis, it is probable that MERS will continue to be challenged. But we are confident

¹³ On loans originated by correspondent lenders or brokers (where MERS is not the mortgagee), the costs of preparing assignments and the associated filing fees are listed on the HUD-1 and paid directly by the borrower.

¹⁴ Individual states handle real estate foreclosures differently. In some states the foreclosure process is judicial, and in some states it is non-judicial. Under both systems, time frames and terms vary widely from state to state. A brief, general, description of both processes prepared by the Mortgage Bankers Association can be found in Attachment Five.

that when courts are provided with all of the facts, MERS will continue to prevail.¹⁵ A MERS case law outline (current through October 20, 2010) is available upon request.¹⁶

MERS CONTINUES TO IMPROVE ITS PROCESSES

In 2009, when it came to our attention that some employees designated by member institutions to serve as MERS certifying officers were not entrusted by their own institutions with signing authority, MERS enhanced its procedures to require that each MERS certifying officer be a company officer of the member institution. In addition, MERS has developed a primer containing information to be reviewed by each prospective MERS certifying officer. To test this knowledge, MERS instituted an online examination to make sure prospective certifying officers had a basic knowledge of MERS and of their roles and responsibilities as MERS certifying officers. MERS requires that these certifications be renewed annually, and we also instituted a recertification process for current certifying officers who had been designated prior

¹⁵ Some important recent cases upholding the rights of MERS include:

- **IN RE Mortgage Electronic Registration Systems (MERS) Litigation**, a multi-district litigation case in federal court in Arizona where the court issued a favorable opinion, stating that “The MERS System is not fraudulent, and MERS has not committed any fraud.”
- **In re Tucker** (9/20/2010), where a Missouri bankruptcy judge found that the language of the deed of trust clearly authorizes MERS to act on behalf of the lender in serving as the legal title holder.
- **Mortgage Electronic Registration Systems, Inc. v. Bellistri**, 2010 WL 2720802 (E.D. Mo. 2010), where the court held that Bellistri’s failure to provide notice to MERS violated MERS’ constitutional due process rights.
- **Taylor v. Deutsche Bank Nat’l Trust Co.**, So. 3d, 2010 WL 3056612 (Fla. 5th DCA 2010), where the court held the MERS mortgage to be valid under Florida law, and held that MERS may assign its rights in the mortgage to the foreclosing company who holds the note. The Florida court also held that where MERS is described as the “mortgagee under the Security Instrument” the document grants to MERS legal status under the UCC, which MERS can assign to the foreclosing bank.
- **Deutsche Bank Natl. Trust Co. v. Traxler**, 2010-Ohio-3940, where the Ohio Court of Appeals recognizes MERS’ authority to assign a mortgage when designated as both a nominee and mortgagee.
- **King v. American Mortgage Network, et al.**, United States District Court, District of Utah, Northern Division (Case No. 1:09-CV-125 TS), where the court, interpreting the language of the deed of trust, held that MERS had the authority to initiate foreclosure proceedings, appoint a trustee, and to foreclose and sell the property.

¹⁶ A review of the use of MERS in all fifty states was done by Covington and Burling in 1996 and 1997 as part of the due diligence associated with the creation of MERS. It is available upon request.

to establishment of the online examination. MERS will continue to enforce these policies and refine its testing and certification program in recognition of the responsibility involved in initiating a foreclosure on someone's home.

When we saw actions were being undertaken to accelerate foreclosure document processing, we became concerned that certifying officers might be pressured to perform their responsibilities in a manner inconsistent with the MERS rules. When we did not receive the assurances we thought appropriate that this would not happen, we suspended relationships with some prominent players involved in the foreclosure process.

When we discovered that some "robo-signers" were MERS certifying officers, we contacted those certifying officers and suspended their authority. They will not be recertified until they retrain and submit to reexamination, and the members who employed them provide MERS with a plan on what will be changed within their companies to prevent this from happening again.

The MERS management team is committed to the highest standards; we believe that MERS adds great value to our nation's system of housing finance in a way that benefits financial institutions, borrowers and the government. There are many benefits derived from the MERS database:

- The MERS database is available to borrowers to locate their servicers, and in many cases, to identify note-owners.
- For local communities, MERS has become a much-needed link between code enforcement officers and the servicing community to help combat the blight that vacant

properties bring to neighborhoods. Over 600 government institutions (cities, municipalities and states) utilize the MERS® System for free to look up the property preservation contacts for loans registered on the system. This helps save the code enforcement officers much needed time in searching for the company directly responsible for the upkeep of that vacant property.

- For law enforcement agencies, MERS aids in combating mortgage fraud through the detection of undisclosed multiple liens taken out by fraudsters for the same social security number or property.

Also, with MERS, lien releases occur quickly at the time of payoff for borrowers because there can be no break in the chain of title with MERS. And finally, foreclosures in the name of MERS are not allowed without the note.

IDEAS FOR THE FUTURE

The MERS database, coupled with the Mortgage Identification Number, is a powerful tool that can be harnessed by the Congress and the industry to improve the mortgage finance system. There are a number of ideas that are worth considering so that when we emerge from this current crisis we have a housing finance system that meets our needs.

1. All residential home loans should be uniquely identified and tracked on a national database, which should include:
 - a. Who is the borrower?
 - b. What/Where is the property?

- c. Who is the owner of the loan's promissory note (the originator/investor)?
 - d. Who is the servicer of the loan (the mortgage company)?
2. The cost of registration for the loan should be included with the other origination fees and disclosed on the HUD -1 at closing.
3. The national database should also track who has physical custody of the original promissory note (the mortgages are always available in the county land records).
4. The database should reflect both current and historical information regarding the home loan.
5. The national unique identifier should be a full life-of-loan identifier, from origination through final satisfaction (payoff) and lien release.
6. All federal data systems that deal with home loans should be required to integrate the unique national identification number, so that information regarding loans can be linked across multiple data sources, e.g., the FHA should be able to look at HUD data, and FDIC should be able to look at SEC information, always knowing that they are comparing apples to apples. State and local government agencies should also be encouraged to adopt the number.

Mr. Chairman, all of us at MERS keenly understand that while owning your own home is a dream, losing that home is a nightmare. As professionals who have dedicated ourselves to helping people realize their dream, we are deeply dismayed by the current foreclosure crisis. We take our role as a mortgagee very seriously and we see our database as a key to moving toward better access to information and transparency for consumers.

I am hopeful that as people understand more about MERS and the role we play, they will see that MERS adds great value to our nation's system of housing finance in ways that benefit not just financial institutions, the broader economy and the government, but—most of all—real people.

Thank you for holding these hearings and inviting MERS to participate.

ATTACHMENTS:

- 1) Sample mortgage document
- 2) MBA Fact Sheet on MERS
- 3) "Title Transfer Law 101," by Karen Gelernt, *American Banker*, October 19, 2010
- 4) "MERS Under Attack: Perspective on Recent Decisions from Kansas and Minnesota," by Barkley and Barbara Clark, *Clark's Secured Transactions Monthly*, February 2010
- 5) "Judicial Versus Non-Judicial Foreclosure," Mortgage Bankers Association, October 2010

ATTACHMENT 1:
SAMPLE MORTGAGE DOCUMENT

This is an Example of a Mortgage which names MERS as the Original Mortgagee (MOM Document).

Prepared by or under the supervision of:

[Name of Natural Person]

[Street Address]

[City, State Zip Code]

_____ [Space Above This Line For Recording Data]

The MERS 18-digit MIN must be visible on the Security Instrument. Place the MIN to the right of the form title, but not within the top recording margin or on the right margin.

MORTGAGE MIN: 1000XXX-XXXXXXXXXX-X

DEFINITIONS

Words used in multiple sections of this document are defined below and other words are defined in Sections 3, 11, 13, 18, 20 and 21. Certain rules regarding the usage of words used in this document are also provided in Section 16.

(A) "Security Instrument" means this document, which is dated _____, together with all Riders to this document.

(B) "Borrower" is _____

MERS as the Original Mortgagee language. See page 3 of this document to note further reference to MERS as Mortgagee.

_____. Borrower is the mortgagor under this Security Instrument.

(C) "MERS" is Mortgage Electronic Registration Systems, Inc. MERS is a separate corporation that is acting solely as a nominee for Lender and Lender's successors and assigns. **MERS is the mortgagee under this Security Instrument.** MERS is organized and existing under the laws of Delaware, and has an address and telephone number of P.O. Box 2026, Flint, MI 48501-2026, tel. (888) 679-MERS.

(D) "Lender" is _____

Lender is a _____ organized and existing under the laws of _____
_____. Lender's address is _____

(E) "Note" means the promissory note signed by Borrower and dated _____
The Note states that Borrower owes Lender _____

_____ Dollars (U.S. \$ _____)
plus interest. Borrower has promised to pay this debt in regular Periodic Payments and to pay the debt in full not later than _____

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(F) **“Property”** means the property that is described below under the heading “Transfer of Rights in the Property.”

(G) **“Loan”** means the debt evidenced by the Note, plus interest, any prepayment charges and late charges due under the Note, and all sums due under this Security Instrument, plus interest.

(H) **“Riders”** means all Riders to this Security Instrument that are executed by Borrower. The following Riders are to be executed by Borrower *[check box as applicable]*:

- | | | |
|--|---|---|
| <input type="checkbox"/> Adjustable Rate Rider | <input type="checkbox"/> Condominium Rider | <input type="checkbox"/> Second Home Rider |
| <input type="checkbox"/> Balloon Rider | <input type="checkbox"/> Planned Unit Development Rider | <input type="checkbox"/> Biweekly Payment Rider |
| <input type="checkbox"/> 1-4 Family Rider | <input type="checkbox"/> Revocable Trust Rider | |
| <input type="checkbox"/> Other(s) <i>[specify]</i> | | |

(I) **“Applicable Law”** means all controlling applicable federal, state and local statutes, regulations, ordinances and administrative rules and orders (that have the effect of law) as well as all applicable final, non-appealable judicial opinions.

(J) **“Community Association Dues, Fees, and Assessments”** means all dues, fees, assessments and other charges that are imposed on Borrower or the Property by a condominium association, homeowners association or similar organization.

(K) **“Electronic Funds Transfer”** means any transfer of funds, other than a transaction originated by check, draft, or similar paper instrument, which is initiated through an electronic terminal, telephonic instrument, computer, or magnetic tape so as to order, instruct, or authorize a financial institution to debit or credit an account. Such term includes, but is not limited to, point-of-sale transfers, automated teller machine transactions, transfers initiated by telephone, wire transfers, and automated clearinghouse transfers.

(L) **“Escrow Items”** means those items that are described in Section 3.

(M) **“Miscellaneous Proceeds”** means any compensation, settlement, award of damages, or proceeds paid by any third party (other than insurance proceeds paid under the coverages described in Section 5) for: (i) damage to, or destruction of, the Property; (ii) condemnation or other taking of all or any part of the Property; (iii) conveyance in lieu of condemnation; or (iv) misrepresentations of, or omissions as to, the value and/or condition of the Property.

(N) **“Mortgage Insurance”** means insurance protecting Lender against the nonpayment of, or default on, the Loan.

(O) **“Periodic Payment”** means the regularly scheduled amount due for (i) principal and interest under the Note, plus (ii) any amounts under Section 3 of this Security Instrument.

(P) **“RESPA”** means the Real Estate Settlement Procedures Act (12 U.S.C. §2601 et seq.) and its implementing regulation, Regulation X (24 C.F.R. Part 3500), as they might be amended from time to time, or any additional or successor legislation or regulation that governs the same subject matter. As used in this Security

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Instrument, “RESPA” refers to all requirements and restrictions that are imposed in regard to a “federally related mortgage loan” even if the Loan does not qualify as a “federally related mortgage loan” under RESPA.

(Q) “Successor in Interest of Borrower” means any party that has taken title to the Property, whether or not that party has assumed Borrower’s obligations under the Note and/or this Security Instrument.

TRANSFER OF RIGHTS IN THE PROPERTY

This Security Instrument secures to Lender: (i) the repayment of the Loan, and all renewals, extensions and modifications of the Note; and (ii) the performance of Borrower’s covenants and agreements under this Security Instrument and the Note. For this purpose, Borrower does hereby mortgage, grant and convey to **MERS (solely as nominee for Lender and Lender’s successors and assigns) and to the successors and assigns of MERS, the following described property located in the**

of _____ : _____
[Name of Recording Jurisdiction] [Type of Recording Jurisdiction]

MERS noted as lender’s nominee in the transfer/due on sale clause.

which currently has the address of _____, Florida _____ (“Property Address”):
[City] [Street] [Zip Code]

TOGETHER WITH all the improvements now or hereafter erected on the property, and all easements, appurtenances, and fixtures now or hereafter a part of the property. All replacements and additions shall also be covered by this Security Instrument. All of the foregoing is referred to in this Security Instrument as the “Property.” Borrower understands and agrees that MERS holds only legal title to the interests granted by Borrower in this Security Instrument, but, if necessary to comply with law or custom, MERS (as nominee for Lender and Lender’s successors and assigns) has the right: to exercise any or all of those interests, including, but not limited to, the right to foreclose and sell the Property; and to take any action required of Lender including, but not limited to, releasing and canceling this Security Instrument.

BORROWER COVENANTS that Borrower is lawfully seised of the estate hereby conveyed and has the right to mortgage, grant and convey the Property and that the Property is unencumbered, except for encumbrances of record. Borrower warrants and will defend generally the title to the Property against all claims and demands, subject to any encumbrances of record.

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THIS SECURITY INSTRUMENT combines uniform covenants for national use and non-uniform covenants with limited variations by jurisdiction to constitute a uniform security instrument covering real property.

UNIFORM COVENANTS. Borrower and Lender covenant and agree as follows:

1. Payment of Principal, Interest, Escrow Items, Prepayment Charges, and Late Charges.

Borrower shall pay when due the principal of, and interest on, the debt evidenced by the Note and any prepayment charges and late charges due under the Note. Borrower shall also pay funds for Escrow Items pursuant to Section 3. Payments due under the Note and this Security Instrument shall be made in U.S. currency. However, if any check or other instrument received by Lender as payment under the Note or this Security Instrument is returned to Lender unpaid, Lender may require that any or all subsequent payments due under the Note and this Security Instrument be made in one or more of the following forms, as selected by Lender: (a) cash; (b) money order; (c) certified check, bank check, treasurer's check or cashier's check, provided any such check is drawn upon an institution whose deposits are insured by a federal agency, instrumentality, or entity; or (d) Electronic Funds Transfer.

Payments are deemed received by Lender when received at the location designated in the Note or at such other location as may be designated by Lender in accordance with the notice provisions in Section 15. Lender may return any payment or partial payment if the payment or partial payments are insufficient to bring the Loan current. Lender may accept any payment or partial payment insufficient to bring the Loan current, without waiver of any rights hereunder or prejudice to its rights to refuse such payment or partial payments in the future, but Lender is not obligated to apply such payments at the time such payments are accepted. If each Periodic Payment is applied as of its scheduled due date, then Lender need not pay interest on unapplied funds. Lender may hold such unapplied funds until Borrower makes payment to bring the Loan current. If Borrower does not do so within a reasonable period of time, Lender shall either apply such funds or return them to Borrower. If not applied earlier, such funds will be applied to the outstanding principal balance under the Note immediately prior to foreclosure. No offset or claim which Borrower might have now or in the future against Lender shall relieve Borrower from making payments due under the Note and this Security Instrument or performing the covenants and agreements secured by this Security Instrument.

2. Application of Payments or Proceeds. Except as otherwise described in this Section 2, all payments accepted and applied by Lender shall be applied in the following order of priority: (a) interest due under the Note; (b) principal due under the Note; (c) amounts due under Section 3. Such payments shall be applied to each Periodic Payment in the order in which it became due. Any remaining amounts shall be applied first to late charges, second to any other amounts due under this Security Instrument, and then to reduce the principal balance of the Note.

If Lender receives a payment from Borrower for a delinquent Periodic Payment which includes a sufficient amount to pay any late charge due, the payment may be applied to the delinquent payment and the late charge. If more than one Periodic Payment is outstanding, Lender may apply any payment received from Borrower to the repayment of the Periodic Payments if, and to the extent that, each payment can be paid in full. To the extent that any excess exists after the payment is applied to the full payment of one or more Periodic Payments, such excess may be applied to any late charges due. Voluntary prepayments shall be applied first to any prepayment charges and then as described in the Note.

Any application of payments, insurance proceeds, or Miscellaneous Proceeds to principal due under the Note shall not extend or postpone the due date, or change the amount, of the Periodic Payments.

3. Funds for Escrow Items. Borrower shall pay to Lender on the day Periodic Payments are due under the Note, until the Note is paid in full, a sum (the "Funds") to provide for payment of amounts due for: (a) taxes and assessments and other items which can attain priority over this Security Instrument as a lien or encumbrance on the Property; (b) leasehold payments or ground rents on the Property, if any; (c) premiums for any and all insurance required by Lender under Section 5; and (d) Mortgage Insurance premiums, if any, or any sums payable by

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Borrower to Lender in lieu of the payment of Mortgage Insurance premiums in accordance with the provisions of Section 10. These items are called "Escrow Items." At origination or at any time during the term of the Loan, Lender may require that Community Association Dues, Fees, and Assessments, if any, be escrowed by Borrower, and such dues, fees and assessments shall be an Escrow Item. Borrower shall promptly furnish to Lender all notices of amounts to be paid under this Section. Borrower shall pay Lender the Funds for Escrow Items unless Lender waives Borrower's obligation to pay the Funds for any or all Escrow Items. Lender may waive Borrower's obligation to pay to Lender Funds for any or all Escrow Items at any time. Any such waiver may only be in writing. In the event of such waiver, Borrower shall pay directly, when and where payable, the amounts due for any Escrow Items for which payment of Funds has been waived by Lender and, if Lender requires, shall furnish to Lender receipts evidencing such payment within such time period as Lender may require. Borrower's obligation to make such payments and to provide receipts shall for all purposes be deemed to be a covenant and agreement contained in this Security Instrument, as the phrase "covenant and agreement" is used in Section 9. If Borrower is obligated to pay Escrow Items directly, pursuant to a waiver, and Borrower fails to pay the amount due for an Escrow Item, Lender may exercise its rights under Section 9 and pay such amount and Borrower shall then be obligated under Section 9 to repay to Lender any such amount. Lender may revoke the waiver as to any or all Escrow Items at any time by a notice given in accordance with Section 15 and, upon such revocation, Borrower shall pay to Lender all Funds, and in such amounts, that are then required under this Section 3.

Lender may, at any time, collect and hold Funds in an amount (a) sufficient to permit Lender to apply the Funds at the time specified under RESPA, and (b) not to exceed the maximum amount a lender can require under RESPA. Lender shall estimate the amount of Funds due on the basis of current data and reasonable estimates of expenditures of future Escrow Items or otherwise in accordance with Applicable Law.

The Funds shall be held in an institution whose deposits are insured by a federal agency, instrumentality, or entity (including Lender, if Lender is an institution whose deposits are so insured) or in any Federal Home Loan Bank. Lender shall apply the Funds to pay the Escrow Items no later than the time specified under RESPA. Lender shall not charge Borrower for holding and applying the Funds, annually analyzing the escrow account, or verifying the Escrow Items, unless Lender pays Borrower interest on the Funds and Applicable Law permits Lender to make such a charge. Unless an agreement is made in writing or Applicable Law requires interest to be paid on the Funds, Lender shall not be required to pay Borrower any interest or earnings on the Funds. Borrower and Lender can agree in writing, however, that interest shall be paid on the Funds. Lender shall give to Borrower, without charge, an annual accounting of the Funds as required by RESPA.

If there is a surplus of Funds held in escrow, as defined under RESPA, Lender shall account to Borrower for the excess funds in accordance with RESPA. If there is a shortage of Funds held in escrow, as defined under RESPA, Lender shall notify Borrower as required by RESPA, and Borrower shall pay to Lender the amount necessary to make up the shortage in accordance with RESPA, but in no more than 12 monthly payments. If there is a deficiency of Funds held in escrow, as defined under RESPA, Lender shall notify Borrower as required by RESPA, and Borrower shall pay to Lender the amount necessary to make up the deficiency in accordance with RESPA, but in no more than 12 monthly payments.

Upon payment in full of all sums secured by this Security Instrument, Lender shall promptly refund to Borrower any Funds held by Lender.

4. Charges; Liens. Borrower shall pay all taxes, assessments, charges, fines, and impositions attributable to the Property which can attain priority over this Security Instrument, leasehold payments or ground rents on the Property, if any, and Community Association Dues, Fees, and Assessments, if any. To the extent that these items are Escrow Items, Borrower shall pay them in the manner provided in Section 3.

Borrower shall promptly discharge any lien which has priority over this Security Instrument unless Borrower: (a) agrees in writing to the payment of the obligation secured by the lien in a manner acceptable to Lender, but only so long as Borrower is performing such agreement; (b) contests the lien in good faith by, or

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defends against enforcement of the lien in, legal proceedings which in Lender's opinion operate to prevent the enforcement of the lien while those proceedings are pending, but only until such proceedings are concluded; or (c) secures from the holder of the lien an agreement satisfactory to Lender subordinating the lien to this Security Instrument. If Lender determines that any part of the Property is subject to a lien which can attain priority over this Security Instrument, Lender may give Borrower a notice identifying the lien. Within 10 days of the date on which that notice is given, Borrower shall satisfy the lien or take one or more of the actions set forth above in this Section 4.

Lender may require Borrower to pay a one-time charge for a real estate tax verification and/or reporting service used by Lender in connection with this Loan.

5. Property Insurance. Borrower shall keep the improvements now existing or hereafter erected on the Property insured against loss by fire, hazards included within the term "extended coverage," and any other hazards including, but not limited to, earthquakes and floods, for which Lender requires insurance. This insurance shall be maintained in the amounts (including deductible levels) and for the periods that Lender requires. What Lender requires pursuant to the preceding sentences can change during the term of the Loan. The insurance carrier providing the insurance shall be chosen by Borrower subject to Lender's right to disapprove Borrower's choice, which right shall not be exercised unreasonably. Lender may require Borrower to pay, in connection with this Loan, either: (a) a one-time charge for flood zone determination, certification and tracking services; or (b) a one-time charge for flood zone determination and certification services and subsequent charges each time remappings or similar changes occur which reasonably might affect such determination or certification. Borrower shall also be responsible for the payment of any fees imposed by the Federal Emergency Management Agency in connection with the review of any flood zone determination resulting from an objection by Borrower.

If Borrower fails to maintain any of the coverages described above, Lender may obtain insurance coverage, at Lender's option and Borrower's expense. Lender is under no obligation to purchase any particular type or amount of coverage. Therefore, such coverage shall cover Lender, but might or might not protect Borrower, Borrower's equity in the Property, or the contents of the Property, against any risk, hazard or liability and might provide greater or lesser coverage than was previously in effect. Borrower acknowledges that the cost of the insurance coverage so obtained might significantly exceed the cost of insurance that Borrower could have obtained. Any amounts disbursed by Lender under this Section 5 shall become additional debt of Borrower secured by this Security Instrument. These amounts shall bear interest at the Note rate from the date of disbursement and shall be payable, with such interest, upon notice from Lender to Borrower requesting payment.

All insurance policies required by Lender and renewals of such policies shall be subject to Lender's right to disapprove such policies, shall include a standard mortgage clause, and shall name Lender as mortgagee and/or as an additional loss payee. Lender shall have the right to hold the policies and renewal certificates. If Lender requires, Borrower shall promptly give to Lender all receipts of paid premiums and renewal notices. If Borrower obtains any form of insurance coverage, not otherwise required by Lender, for damage to, or destruction of, the Property, such policy shall include a standard mortgage clause and shall name Lender as mortgagee and/or as an additional loss payee.

In the event of loss, Borrower shall give prompt notice to the insurance carrier and Lender. Lender may make proof of loss if not made promptly by Borrower. Unless Lender and Borrower otherwise agree in writing, any insurance proceeds, whether or not the underlying insurance was required by Lender, shall be applied to restoration or repair of the Property, if the restoration or repair is economically feasible and Lender's security is not lessened. During such repair and restoration period, Lender shall have the right to hold such insurance proceeds until Lender has had an opportunity to inspect such Property to ensure the work has been completed to Lender's satisfaction, provided that such inspection shall be undertaken promptly. Lender may disburse proceeds for the repairs and restoration in a single payment or in a series of progress payments as the work is completed. Unless an agreement is made in writing or Applicable Law requires interest to be paid on such insurance proceeds, Lender shall not be

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required to pay Borrower any interest or earnings on such proceeds. Fees for public adjusters, or other third parties, retained by Borrower shall not be paid out of the insurance proceeds and shall be the sole obligation of Borrower. If the restoration or repair is not economically feasible or Lender's security would be lessened, the insurance proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower. Such insurance proceeds shall be applied in the order provided for in Section 2.

If Borrower abandons the Property, Lender may file, negotiate and settle any available insurance claim and related matters. If Borrower does not respond within 30 days to a notice from Lender that the insurance carrier has offered to settle a claim, then Lender may negotiate and settle the claim. The 30-day period will begin when the notice is given. In either event, or if Lender acquires the Property under Section 22 or otherwise, Borrower hereby assigns to Lender (a) Borrower's rights to any insurance proceeds in an amount not to exceed the amounts unpaid under the Note or this Security Instrument, and (b) any other of Borrower's rights (other than the right to any refund of unearned premiums paid by Borrower) under all insurance policies covering the Property, insofar as such rights are applicable to the coverage of the Property. Lender may use the insurance proceeds either to repair or restore the Property or to pay amounts unpaid under the Note or this Security Instrument, whether or not then due.

6. Occupancy. Borrower shall occupy, establish, and use the Property as Borrower's principal residence within 60 days after the execution of this Security Instrument and shall continue to occupy the Property as Borrower's principal residence for at least one year after the date of occupancy, unless Lender otherwise agrees in writing, which consent shall not be unreasonably withheld, or unless extenuating circumstances exist which are beyond Borrower's control.

7. Preservation, Maintenance and Protection of the Property; Inspections. Borrower shall not destroy, damage or impair the Property, allow the Property to deteriorate or commit waste on the Property. Whether or not Borrower is residing in the Property, Borrower shall maintain the Property in order to prevent the Property from deteriorating or decreasing in value due to its condition. Unless it is determined pursuant to Section 5 that repair or restoration is not economically feasible, Borrower shall promptly repair the Property if damaged to avoid further deterioration or damage. If insurance or condemnation proceeds are paid in connection with damage to, or the taking of, the Property, Borrower shall be responsible for repairing or restoring the Property only if Lender has released proceeds for such purposes. Lender may disburse proceeds for the repairs and restoration in a single payment or in a series of progress payments as the work is completed. If the insurance or condemnation proceeds are not sufficient to repair or restore the Property, Borrower is not relieved of Borrower's obligation for the completion of such repair or restoration.

Lender or its agent may make reasonable entries upon and inspections of the Property. If it has reasonable cause, Lender may inspect the interior of the improvements on the Property. Lender shall give Borrower notice at the time of or prior to such an interior inspection specifying such reasonable cause.

8. Borrower's Loan Application. Borrower shall be in default if, during the Loan application process, Borrower or any persons or entities acting at the direction of Borrower or with Borrower's knowledge or consent gave materially false, misleading, or inaccurate information or statements to Lender (or failed to provide Lender with material information) in connection with the Loan. Material representations include, but are not limited to, representations concerning Borrower's occupancy of the Property as Borrower's principal residence.

9. Protection of Lender's Interest in the Property and Rights Under this Security Instrument. If (a) Borrower fails to perform the covenants and agreements contained in this Security Instrument, (b) there is a legal proceeding that might significantly affect Lender's interest in the Property and/or rights under this Security Instrument (such as a proceeding in bankruptcy, probate, for condemnation or forfeiture, for enforcement of a lien which may attain priority over this Security Instrument or to enforce laws or regulations), or (c) Borrower has abandoned the Property, then Lender may do and pay for whatever is reasonable or appropriate to protect Lender's interest in the Property and rights under this Security Instrument, including protecting and/or assessing the value of the Property, and securing and/or repairing the Property. Lender's actions can include, but are not limited to:

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(a) paying any sums secured by a lien which has priority over this Security Instrument; (b) appearing in court; and (c) paying reasonable attorneys' fees to protect its interest in the Property and/or rights under this Security Instrument, including its secured position in a bankruptcy proceeding. Securing the Property includes, but is not limited to, entering the Property to make repairs, change locks, replace or board up doors and windows, drain water from pipes, eliminate building or other code violations or dangerous conditions, and have utilities turned on or off.

Although Lender may take action under this Section 9, Lender does not have to do so and is not under any duty or obligation to do so. It is agreed that Lender incurs no liability for not taking any or all actions authorized under this Section 9.

Any amounts disbursed by Lender under this Section 9 shall become additional debt of Borrower secured by this Security Instrument. These amounts shall bear interest at the Note rate from the date of disbursement and shall be payable, with such interest, upon notice from Lender to Borrower requesting payment.

If this Security Instrument is on a leasehold, Borrower shall comply with all the provisions of the lease. If Borrower acquires fee title to the Property, the leasehold and the fee title shall not merge unless Lender agrees to the merger in writing.

10. Mortgage Insurance. If Lender required Mortgage Insurance as a condition of making the Loan, Borrower shall pay the premiums required to maintain the Mortgage Insurance in effect. If, for any reason, the Mortgage Insurance coverage required by Lender ceases to be available from the mortgage insurer that previously provided such insurance and Borrower was required to make separately designated payments toward the premiums for Mortgage Insurance, Borrower shall pay the premiums required to obtain coverage substantially equivalent to the Mortgage Insurance previously in effect, at a cost substantially equivalent to the cost to Borrower of the Mortgage Insurance previously in effect, from an alternate mortgage insurer selected by Lender. If substantially equivalent Mortgage Insurance coverage is not available, Borrower shall continue to pay to Lender the amount of the separately designated payments that were due when the insurance coverage ceased to be in effect. Lender will accept, use and retain these payments as a non-refundable loss reserve in lieu of Mortgage Insurance. Such loss reserve shall be non-refundable, notwithstanding the fact that the Loan is ultimately paid in full, and Lender shall not be required to pay Borrower any interest or earnings on such loss reserve. Lender can no longer require loss reserve payments if Mortgage Insurance coverage (in the amount and for the period that Lender requires) provided by an insurer selected by Lender again becomes available, is obtained, and Lender requires separately designated payments toward the premiums for Mortgage Insurance. If Lender required Mortgage Insurance as a condition of making the Loan and Borrower was required to make separately designated payments toward the premiums for Mortgage Insurance, Borrower shall pay the premiums required to maintain Mortgage Insurance in effect, or to provide a non-refundable loss reserve, until Lender's requirement for Mortgage Insurance ends in accordance with any written agreement between Borrower and Lender providing for such termination or until termination is required by Applicable Law. Nothing in this Section 10 affects Borrower's obligation to pay interest at the rate provided in the Note.

Mortgage Insurance reimburses Lender (or any entity that purchases the Note) for certain losses it may incur if Borrower does not repay the Loan as agreed. Borrower is not a party to the Mortgage Insurance.

Mortgage insurers evaluate their total risk on all such insurance in force from time to time, and may enter into agreements with other parties that share or modify their risk, or reduce losses. These agreements are on terms and conditions that are satisfactory to the mortgage insurer and the other party (or parties) to these agreements. These agreements may require the mortgage insurer to make payments using any source of funds that the mortgage insurer may have available (which may include funds obtained from Mortgage Insurance premiums).

As a result of these agreements, Lender, any purchaser of the Note, another insurer, any reinsurer, any other entity, or any affiliate of any of the foregoing, may receive (directly or indirectly) amounts that derive from (or might be characterized as) a portion of Borrower's payments for Mortgage Insurance, in exchange for sharing or modifying the mortgage insurer's risk, or reducing losses. If such agreement provides that an affiliate of Lender

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takes a share of the insurer's risk in exchange for a share of the premiums paid to the insurer, the arrangement is often termed "captive reinsurance." Further:

(a) Any such agreements will not affect the amounts that Borrower has agreed to pay for Mortgage Insurance, or any other terms of the Loan. Such agreements will not increase the amount Borrower will owe for Mortgage Insurance, and they will not entitle Borrower to any refund.

(b) Any such agreements will not affect the rights Borrower has – if any – with respect to the Mortgage Insurance under the Homeowners Protection Act of 1998 or any other law. These rights may include the right to receive certain disclosures, to request and obtain cancellation of the Mortgage Insurance, to have the Mortgage Insurance terminated automatically, and/or to receive a refund of any Mortgage Insurance premiums that were unearned at the time of such cancellation or termination.

11. Assignment of Miscellaneous Proceeds; Forfeiture. All Miscellaneous Proceeds are hereby assigned to and shall be paid to Lender.

If the Property is damaged, such Miscellaneous Proceeds shall be applied to restoration or repair of the Property, if the restoration or repair is economically feasible and Lender's security is not lessened. During such repair and restoration period, Lender shall have the right to hold such Miscellaneous Proceeds until Lender has had an opportunity to inspect such Property to ensure the work has been completed to Lender's satisfaction, provided that such inspection shall be undertaken promptly. Lender may pay for the repairs and restoration in a single disbursement or in a series of progress payments as the work is completed. Unless an agreement is made in writing or Applicable Law requires interest to be paid on such Miscellaneous Proceeds, Lender shall not be required to pay Borrower any interest or earnings on such Miscellaneous Proceeds. If the restoration or repair is not economically feasible or Lender's security would be lessened, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower. Such Miscellaneous Proceeds shall be applied in the order provided for in Section 2.

In the event of a total taking, destruction, or loss in value of the Property, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument, whether or not then due, with the excess, if any, paid to Borrower.

In the event of a partial taking, destruction, or loss in value of the Property in which the fair market value of the Property immediately before the partial taking, destruction, or loss in value is equal to or greater than the amount of the sums secured by this Security Instrument immediately before the partial taking, destruction, or loss in value, unless Borrower and Lender otherwise agree in writing, the sums secured by this Security Instrument shall be reduced by the amount of the Miscellaneous Proceeds multiplied by the following fraction: (a) the total amount of the sums secured immediately before the partial taking, destruction, or loss in value divided by (b) the fair market value of the Property immediately before the partial taking, destruction, or loss in value. Any balance shall be paid to Borrower.

In the event of a partial taking, destruction, or loss in value of the Property in which the fair market value of the Property immediately before the partial taking, destruction, or loss in value is less than the amount of the sums secured immediately before the partial taking, destruction, or loss in value, unless Borrower and Lender otherwise agree in writing, the Miscellaneous Proceeds shall be applied to the sums secured by this Security Instrument whether or not the sums are then due.

If the Property is abandoned by Borrower, or if, after notice by Lender to Borrower that the Opposing Party (as defined in the next sentence) offers to make an award to settle a claim for damages, Borrower fails to respond to Lender within 30 days after the date the notice is given, Lender is authorized to collect and apply the Miscellaneous Proceeds either to restoration or repair of the Property or to the sums secured by this Security Instrument, whether or not then due. "Opposing Party" means the third party that owes Borrower Miscellaneous Proceeds or the party against whom Borrower has a right of action in regard to Miscellaneous Proceeds.

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Borrower shall be in default if any action or proceeding, whether civil or criminal, is begun that, in Lender's judgment, could result in forfeiture of the Property or other material impairment of Lender's interest in the Property or rights under this Security Instrument. Borrower can cure such a default and, if acceleration has occurred, reinstate as provided in Section 19, by causing the action or proceeding to be dismissed with a ruling that, in Lender's judgment, precludes forfeiture of the Property or other material impairment of Lender's interest in the Property or rights under this Security Instrument. The proceeds of any award or claim for damages that are attributable to the impairment of Lender's interest in the Property are hereby assigned and shall be paid to Lender.

All Miscellaneous Proceeds that are not applied to restoration or repair of the Property shall be applied in the order provided for in Section 2.

12. Borrower Not Released; Forbearance By Lender Not a Waiver. Extension of the time for payment or modification of amortization of the sums secured by this Security Instrument granted by Lender to Borrower or any Successor in Interest of Borrower shall not operate to release the liability of Borrower or any Successors in Interest of Borrower. Lender shall not be required to commence proceedings against any Successor in Interest of Borrower or to refuse to extend time for payment or otherwise modify amortization of the sums secured by this Security Instrument by reason of any demand made by the original Borrower or any Successors in Interest of Borrower. Any forbearance by Lender in exercising any right or remedy including, without limitation, Lender's acceptance of payments from third persons, entities or Successors in Interest of Borrower or in amounts less than the amount then due, shall not be a waiver of or preclude the exercise of any right or remedy.

13. Joint and Several Liability; Co-signers; Successors and Assigns Bound. Borrower covenants and agrees that Borrower's obligations and liability shall be joint and several. However, any Borrower who co-signs this Security Instrument but does not execute the Note (a "co-signer"): (a) is co-signing this Security Instrument only to mortgage, grant and convey the co-signer's interest in the Property under the terms of this Security Instrument; (b) is not personally obligated to pay the sums secured by this Security Instrument; and (c) agrees that Lender and any other Borrower can agree to extend, modify, forbear or make any accommodations with regard to the terms of this Security Instrument or the Note without the co-signer's consent.

Subject to the provisions of Section 18, any Successor in Interest of Borrower who assumes Borrower's obligations under this Security Instrument in writing, and is approved by Lender, shall obtain all of Borrower's rights and benefits under this Security Instrument. Borrower shall not be released from Borrower's obligations and liability under this Security Instrument unless Lender agrees to such release in writing. The covenants and agreements of this Security Instrument shall bind (except as provided in Section 20) and benefit the successors and assigns of Lender.

14. Loan Charges. Lender may charge Borrower fees for services performed in connection with Borrower's default, for the purpose of protecting Lender's interest in the Property and rights under this Security Instrument, including, but not limited to, attorneys' fees, property inspection and valuation fees. In regard to any other fees, the absence of express authority in this Security Instrument to charge a specific fee to Borrower shall not be construed as a prohibition on the charging of such fee. Lender may not charge fees that are expressly prohibited by this Security Instrument or by Applicable Law.

If the Loan is subject to a law which sets maximum loan charges, and that law is finally interpreted so that the interest or other loan charges collected or to be collected in connection with the Loan exceed the permitted limits, then: (a) any such loan charge shall be reduced by the amount necessary to reduce the charge to the permitted limit; and (b) any sums already collected from Borrower which exceeded permitted limits will be refunded to Borrower. Lender may choose to make this refund by reducing the principal owed under the Note or by making a direct payment to Borrower. If a refund reduces principal, the reduction will be treated as a partial prepayment without any prepayment charge (whether or not a prepayment charge is provided for under the Note). Borrower's acceptance of any such refund made by direct payment to Borrower will constitute a waiver of any right of action Borrower might have arising out of such overcharge.

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15. Notices. All notices given by Borrower or Lender in connection with this Security Instrument must be in writing. Any notice to Borrower in connection with this Security Instrument shall be deemed to have been given to Borrower when mailed by first class mail or when actually delivered to Borrower's notice address if sent by other means. Notice to any one Borrower shall constitute notice to all Borrowers unless Applicable Law expressly requires otherwise. The notice address shall be the Property Address unless Borrower has designated a substitute notice address by notice to Lender. Borrower shall promptly notify Lender of Borrower's change of address. If Lender specifies a procedure for reporting Borrower's change of address, then Borrower shall only report a change of address through that specified procedure. There may be only one designated notice address under this Security Instrument at any one time. Any notice to Lender shall be given by delivering it or by mailing it by first class mail to Lender's address stated herein unless Lender has designated another address by notice to Borrower. Any notice in connection with this Security Instrument shall not be deemed to have been given to Lender until actually received by Lender. If any notice required by this Security Instrument is also required under Applicable Law, the Applicable Law requirement will satisfy the corresponding requirement under this Security Instrument.

16. Governing Law; Severability; Rules of Construction. This Security Instrument shall be governed by federal law and the law of the jurisdiction in which the Property is located. All rights and obligations contained in this Security Instrument are subject to any requirements and limitations of Applicable Law. Applicable Law might explicitly or implicitly allow the parties to agree by contract or it might be silent, but such silence shall not be construed as a prohibition against agreement by contract. In the event that any provision or clause of this Security Instrument or the Note conflicts with Applicable Law, such conflict shall not affect other provisions of this Security Instrument or the Note which can be given effect without the conflicting provision.

As used in this Security Instrument: (a) words of the masculine gender shall mean and include corresponding neuter words or words of the feminine gender; (b) words in the singular shall mean and include the plural and vice versa; and (c) the word "may" gives sole discretion without any obligation to take any action.

17. Borrower's Copy. Borrower shall be given one copy of the Note and of this Security Instrument.

18. Transfer of the Property or a Beneficial Interest in Borrower. As used in this Section 18, "Interest in the Property" means any legal or beneficial interest in the Property, including, but not limited to, those beneficial interests transferred in a bond for deed, contract for deed, installment sales contract or escrow agreement, the intent of which is the transfer of title by Borrower at a future date to a purchaser.

If all or any part of the Property or any Interest in the Property is sold or transferred (or if Borrower is not a natural person and a beneficial interest in Borrower is sold or transferred) without Lender's prior written consent, Lender may require immediate payment in full of all sums secured by this Security Instrument. However, this option shall not be exercised by Lender if such exercise is prohibited by Applicable Law.

If Lender exercises this option, Lender shall give Borrower notice of acceleration. The notice shall provide a period of not less than 30 days from the date the notice is given in accordance with Section 15 within which Borrower must pay all sums secured by this Security Instrument. If Borrower fails to pay these sums prior to the expiration of this period, Lender may invoke any remedies permitted by this Security Instrument without further notice or demand on Borrower.

19. Borrower's Right to Reinstate After Acceleration. If Borrower meets certain conditions, Borrower shall have the right to have enforcement of this Security Instrument discontinued at any time prior to the earliest of: (a) five days before sale of the Property pursuant to any power of sale contained in this Security Instrument; (b) such other period as Applicable Law might specify for the termination of Borrower's right to reinstate; or (c) entry of a judgment enforcing this Security Instrument. Those conditions are that Borrower: (a) pays Lender all sums which then would be due under this Security Instrument and the Note as if no acceleration had occurred; (b) cures any default of any other covenants or agreements; (c) pays all expenses incurred in enforcing this Security Instrument, including, but not limited to, reasonable attorneys' fees, property inspection and valuation fees, and other fees incurred for the purpose of protecting Lender's interest in the Property and rights under this Security Instrument; and

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(d) takes such action as Lender may reasonably require to assure that Lender's interest in the Property and rights under this Security Instrument, and Borrower's obligation to pay the sums secured by this Security Instrument, shall continue unchanged. Lender may require that Borrower pay such reinstatement sums and expenses in one or more of the following forms, as selected by Lender: (a) cash; (b) money order; (c) certified check, bank check, treasurer's check or cashier's check, provided any such check is drawn upon an institution whose deposits are insured by a federal agency, instrumentality or entity; or (d) Electronic Funds Transfer. Upon reinstatement by Borrower, this Security Instrument and obligations secured hereby shall remain fully effective as if no acceleration had occurred. However, this right to reinstate shall not apply in the case of acceleration under Section 18.

20. Sale of Note; Change of Loan Servicer; Notice of Grievance. The Note or a partial interest in the Note (together with this Security Instrument) can be sold one or more times without prior notice to Borrower. A sale might result in a change in the entity (known as the "Loan Servicer") that collects Periodic Payments due under the Note and this Security Instrument and performs other mortgage loan servicing obligations under the Note, this Security Instrument, and Applicable Law. There also might be one or more changes of the Loan Servicer unrelated to a sale of the Note. If there is a change of the Loan Servicer, Borrower will be given written notice of the change which will state the name and address of the new Loan Servicer, the address to which payments should be made and any other information RESPA requires in connection with a notice of transfer of servicing. If the Note is sold and thereafter the Loan is serviced by a Loan Servicer other than the purchaser of the Note, the mortgage loan servicing obligations to Borrower will remain with the Loan Servicer or be transferred to a successor Loan Servicer and are not assumed by the Note purchaser unless otherwise provided by the Note purchaser.

Neither Borrower nor Lender may commence, join, or be joined to any judicial action (as either an individual litigant or the member of a class) that arises from the other party's actions pursuant to this Security Instrument or that alleges that the other party has breached any provision of, or any duty owed by reason of, this Security Instrument, until such Borrower or Lender has notified the other party (with such notice given in compliance with the requirements of Section 15) of such alleged breach and afforded the other party hereto a reasonable period after the giving of such notice to take corrective action. If Applicable Law provides a time period which must elapse before certain action can be taken, that time period will be deemed to be reasonable for purposes of this paragraph. The notice of acceleration and opportunity to cure given to Borrower pursuant to Section 22 and the notice of acceleration given to Borrower pursuant to Section 18 shall be deemed to satisfy the notice and opportunity to take corrective action provisions of this Section 20.

21. Hazardous Substances. As used in this Section 21: (a) "Hazardous Substances" are those substances defined as toxic or hazardous substances, pollutants, or wastes by Environmental Law and the following substances: gasoline, kerosene, other flammable or toxic petroleum products, toxic pesticides and herbicides, volatile solvents, materials containing asbestos or formaldehyde, and radioactive materials; (b) "Environmental Law" means federal laws and laws of the jurisdiction where the Property is located that relate to health, safety or environmental protection; (c) "Environmental Cleanup" includes any response action, remedial action, or removal action, as defined in Environmental Law; and (d) an "Environmental Condition" means a condition that can cause, contribute to, or otherwise trigger an Environmental Cleanup.

Borrower shall not cause or permit the presence, use, disposal, storage, or release of any Hazardous Substances, or threaten to release any Hazardous Substances, on or in the Property. Borrower shall not do, nor allow anyone else to do, anything affecting the Property (a) that is in violation of any Environmental Law, (b) which creates an Environmental Condition, or (c) which, due to the presence, use, or release of a Hazardous Substance, creates a condition that adversely affects the value of the Property. The preceding two sentences shall not apply to the presence, use, or storage on the Property of small quantities of Hazardous Substances that are generally recognized to be appropriate to normal residential uses and to maintenance of the Property (including, but not limited to, hazardous substances in consumer products).

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Printed Name: _____
[Please Complete]

Mailing Address: *[Printed Name]*

_____ (Seal)
-Borrower

Mailing Address: *[Printed Name]*

_____ (Seal)
-Borrower

Mailing Address: *[Printed Name]*

_____ *[Acknowledgment on Following Page]* _____

This is an Example of a Mortgage which names MERS as the Original Mortgagee (MOM Document).

State of §
County of §

The foregoing instrument was acknowledged before me this [date] by _____,

[name of person acknowledging],

who is personally known to me or who has produced [type of identification] as identification.

Signature of Person Taking Acknowledgment

Name Typed, Printed or Stamped

Title or Rank

Serial Number, if any

After recording please return to:

[Company Name]

[Name of Natural Person]

[Street Address]

[City, State Zip Code]

ATTACHMENT 2:
MBA FACT SHEET ON MERS



MBA Fact Sheet

The Role of Electronic Mortgage Registrations

The Need for Electronic Registration

Recent events in the mortgage loan servicing industry have prompted questions about how mortgages are recorded and their ownership tracked. These questions are important for a number of reasons. In today's mortgage finance system, a loan is often sold one or more times after origination and then securitized as part of a pool of similar mortgages. Additionally, the overwhelming majority of mortgage loans are paid off through refinancing or sale of a property long before their terms (such as 15, 30 or 40 years) expire. These facts make tracking the servicer and ownership of every mortgage challenging and, at the same time, absolutely critical to the efficient operation of the mortgage market.

To understand the purpose of a registry of mortgage rights, it is important to understand the nature of mortgage loans. Mortgage loans are complex financial products that come with piles of paperwork (actual and electronic) at every step of the process – from borrower application to the ultimate marketing of a security backed by that loan. Two instruments are fundamental to virtually every mortgage loan today and rise above the rest in terms of legal importance – the promissory note and the security instrument, which is generally a mortgage or deed of trust. The security instrument establishes the note holder's right to the property, securing repayment of the borrower's promissory note upon the borrower's default.

The legal principle governing the right to receive payment under a mortgage note is that "possession" of the note determines ownership and the security instrument follows the note. The security instrument is recorded in the local (usually county) land records office to provide "public notice" of the mortgage lien.

The American process for allowing a borrower to possess real estate while paying the debt, and requiring the lender to record a notice of lien so that subsequent creditors and other interested parties can be aware of the lender's security interest in the real property, has been in place since the early 17th century. For hundreds of years, it worked pretty much the same way in counties across the country.

In more recent history, it also has been common practice to divide up the rights in a mortgage into "legal" rights and "equitable" or "beneficial" rights. Going back to the launch of FHA-insured mortgages in the 1930's, when a loan was made, the mortgage originator was identified in the public records as "mortgagee of record" on behalf of a life insurance company that would purchase the mortgage obligation. All rights to receive payment were sold to the insurance company which would become the equitable owner of the promissory note. To the world, the mortgage originator/servicer would be the mortgagee of record, but the entity would hold only "bare legal title" in order to service the mortgage on behalf of its investor. "Servicing" includes

collecting mortgage payments, remitting them to investors, and handling mortgage delinquencies and defaults on behalf of an investor. As the secondary mortgage market evolved, this model was adopted by Fannie Mae and Freddie Mac, Ginnie Mae, and private label securitizers.

Under this model, every time servicing obligations changed hands as the mortgage moved through the mortgage business chain, the new servicer was generally required by the investor to record the assignment of its bare legal title in the local land records office. The records also had to be updated and liens released, as they do still today, any time a mortgage was paid off through a refinance or sale of the property.

By the early 1990s, with homeownership continuing to grow and interest rates falling to new lows, it was apparent that the mortgage recordation system that had been in use for nearly 400 years could not keep up with the modern volume of residential real property finance transactions. In fact, the 1993 mortgage refinance boom, still one of the largest in American history, was hampered by a severe backlog of paperwork (which included the assignments between servicers) at land records offices in many areas of the country, often delaying lien releases and related home purchase and mortgage refinance transactions to the detriment of consumers trying to benefit from falling interest rates and compromising the chain of record title. Borrowers, lenders and government officials all became frustrated by this situation which was exacerbated by the growing volume of investor-required mortgage assignments.

The mortgage recordation backlog of the early 1990s was somewhat analogous to Wall Street's "paperwork crisis" of the late 1960s, where clerks were buried in so many paper stock certificates that they could not process them fast enough. To solve this crisis, Wall Street turned to technology and a system of book-entry accounting to track stock ownership. Mortgage companies, banks, investors and government officials saw the positive results of this evolution in the stock market and began to discuss how to apply a similar concept to tracking mortgage ownership rights, servicing rights and warehouse loans (short-term security interests in mortgage obligations prior to their sale into the secondary mortgage market). Out of these discussions was born an industry utility that came to be called MERS, or Mortgage Electronic Registration Systems, Inc.

MERS Today

Today, MERS is an integral part of modern mortgage finance. MERS has dramatically improved the quality and availability of information in the residential mortgage process since its operations began in 1997.

The MERS[®] System is a database of information provided by mortgage lenders, servicers and investors. It is owned and operated by MERSCORP, Inc., the parent company of Mortgage Electronic Registration Systems, Inc. Using a standard Mortgage Identification Number (MIN), the MERS[®] System tracks changes in holders of loan servicing rights, owners of the mortgage note and holders of warehouse loans.

On the majority of mortgage loans today, borrowers agree at settlement to allow Mortgage Electronic Registration Systems, Inc. to be the mortgagee of record – as "nominee" for the promissory note holder – as the note is sold, aggregated and securitized. The mortgage lien and its priority position are properly established in the county recorder's office, while the ownership of the note and other mortgage rights move through the modern system of banking and capital markets, all the time being tracked closely by the MERS[®] System.

Allowing Mortgage Electronic Registration Systems, Inc. to serve as the mortgagee of record has relieved the pressures on the public land records caused by repeated transfers of mortgage rights (such as servicing and ownership rights), and thereby helps protect the accuracy and integrity of the chain of title. MERS also maintains a centralized “mailroom” on behalf of its members to receive and disseminate legal notices it receives as mortgagee of record.

The MERS® System supports the mortgage securitization process by giving banks, brokers, loan originators, servicers, investors and regulators the ability to track key information on every mortgage loan registered on the MERS® System. Since its inception, over 3,000 such market participants have registered more than 65 million loans with on the MERS® System. Today, over half of all outstanding mortgages are registered on the MERS® System.

MERS is also useful to borrowers, both directly and indirectly. MERS, for the first time, created a way for borrowers to track the servicer (and sometimes the investor) for their loan. This service is free online at <http://www.mersinc.org/homeowners/> or by calling (888) 679-6377. Through the reduction of paperwork and other efficiencies, MERS has helped significantly reduce the costs of a mortgage which helps keep the mortgage market liquid and ultimately reduces costs to borrowers. In addition, MERS has decreased the time it takes to refinance a loan which can be a significant benefit to borrowers attempting to lower their interest rate or move from a variable interest rate loan to one with a fixed rate.

As the mortgagee of record, it is common for MERS to play a role in foreclosures. If Mortgage Electronic Registration Systems, Inc. is the mortgagee of record with the county land records, and the borrower is in default on the mortgage, foreclosure can be legally commenced either by Mortgage Electronic Registration Systems, Inc. on behalf of the note owner, or by servicer or other entity if the note owner instructs MERS to assign the mortgage to the servicer or other entity. The process varies in these two ways due to state laws and/or the preference of the servicer or investor. It is important to note that Mortgage Electronic Registration Systems, Inc. only initiates foreclosure when it has been instructed to do so by the owner of the mortgage and possesses the mortgage note.

For more information on MERS, go to www.mersinc.org.

October 29, 2010

ATTACHMENT 3:

“Title Transfer Law 101,” by Karen Gelernt

American Banker, October 19, 2010

Tuesday, October 19, 2010

VIEWPOINT

Title Transfer Law 101

BY KAREN GELERT

Recently, commentators have raised questions about whether certain transfers of residential mortgage loans (made in connection with secondary market transactions such as securitizations) were sufficient to transfer title to the new owner of the mortgage loans and whether such transfers of rights were sufficient to allow the new owner of the mortgages to commence foreclosure, where appropriate.



To better understand these issues, they must be put in their proper perspective based upon the law that underlies transfers of mortgage loans. The underlying tenet, however, is that residential mortgage notes are negotiable instruments which, by their nature, are intended to be liquid and easily transferable by certain key actions outlined in the law. Challenging this notion, irresponsibly questions a well-established body of law affecting trillions of dollars of mortgage loans as well as trillions of dollars of other types of negotiable instruments.

A mortgage loan consists of two important documents: the mortgage note, which constitutes the obligation of the mortgagor

to pay its loan; and the mortgage, that constitutes the lien on the real property that secures the note. The note is a promissory note and notes secured by homes are typically negotiable instruments under law. Negotiable instruments have certain special characteristics under law. First, they are easily transferable (typically by endorsement).

Second, a holder in due course of a negotiable instrument takes the instrument free of most defenses to payment, thereby permitting the holder prompt payment. The intent behind the law of negotiable instruments was to enable such instruments to be as liquid as possible, to encourage commerce and lending. As such, residential mortgage loans are intended to be relatively liquid assets, easily transferred and easily realized upon.

In this way, a residential mortgage note is analogous to a check. In the case of the mortgage note, it is payable to the order of a mortgagee. Similar to a check, which is transferred by endorsement, a mortgage note is also transferred by endorse-

ment. An endorsement can be specific (such as "Pay to the order of Joe Smith") or can be blank (such as "Pay to the order of _____"). When a note is endorsed in blank, it becomes bearer paper (in other words, the bearer, or holder, is presumed to be the owner). The analogy would be a check made out to "cash." In both instances, the instrument can be physically transferred multiple times without the requirement of additional endorsements. If you presented a bank with a check made out to "cash" the bank should not question your ownership. Similarly, the ownership by an entity of a mortgage note endorsed in blank should not, in the ordinary course, be challenged.

In other words (and aside from the separate issue of whether the circumstances that are required to commence foreclosure exist with respect to the mortgage loan), mere possession of a promissory note endorsed in blank (whether a check or a mortgage note) should provide the presumption of ownership of that promissory note by the current holder. So for example, a trustee for a securitization that has physical possession of the mortgage note, should be the presumed owner of that note. Any other outcome would put at risk the entire premise and foundation of negotiable instruments law.

In the end, an endorsement in blank does not, and should not, raise a question of ownership of the instrument.

The second component of a mortgage loan is the mortgage. The mortgage and the transfer of mortgage is governed by real property law. The mortgage must be recorded to put third parties on notice of the lienholder. This protects the mortgagee as well as other parties that might assert an interest in the property, like other lenders, judgment creditors or potential purchasers of the property. It protects the mortgagee because, if a third party were to assert an interest in the real property it would be required to give notice to all the interested parties of record, including the mortgagee of record under the mortgage. If an assignee did not record an assignment of mortgage, then the assignee would not be put on notice. However, this would be a risk borne by the assignee.

Historically, when a mortgage loan was transferred it was accompanied by an assignment of mortgage, oftentimes in blank. Because the secondary market

was so active, buyers of mortgage loans frequently did not record the assignments in blank and merely delivered the assignments with the related mortgage notes endorsed in blank to the subsequent buyer. Frequently, the servicer of the mortgage loans remained the mortgagee of record and would receive any important notices regarding the related mortgaged properties. However, in order to facilitate easy transfers of mortgage loans, and to ease the burden of multiple recordations of assignments of mortgage in an active secondary market, MERS systems was developed. MERS is basically an agent for the mortgagee of record. So while a mortgage note may be transferred several times the mortgagee of record remains MERS and MERS tracks the intended mortgagee in its systems.

But at the end of the day, it is the owner of the mortgage note that dictates ownership of the mortgage (a premise commonly referred to as “the mortgage follows the note”) as evidenced by Article 3 and Article 9 of the Uniform Commercial Code, in effect in all states.

Ideally, at foreclosure, the mortgagee of record should correspond to the holder of the note. However, any disparity should not be an acceptable basis to bar foreclosure, since the mortgage should not be the document that is dispositive of title to the mortgage loan. The holder of the note should be deemed the owner of the mortgage loan with standing and right to foreclose.

The chain of assignment of the mortgage may for various reasons be defective, or in the case of MERS, an agent for the holder may be identified as the mortgagee, but the principles of commercial law and negotiable instruments, if applied correctly, should ultimately prevail and allow the holder of the note to foreclose to the extent permitted by the mortgage loan documents and applicable state law. Any other outcome would call into question the foundations and liquidity of negotiable instruments and severely obstruct what was always intended as a relatively liquid market.

Karen Gelernt is a partner in the capital markets department at Cadwalader, Wickersham & Taft.

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ATTACHMENT 4:

**“MERS Under Attack:
Perspective on Recent Decisions from Kansas and Minnesota,”
by Barkley and Barbara Clark
Clark’s Secured Transactions Monthly
February 2010**

CLARKS' SECURED TRANSACTIONS MONTHLY

Documentation • Bankruptcy • Regulation

MERS Under Attack: Perspective on Recent Decisions from Kansas and Minnesota

by Barkley and Barbara Clark

February 2010

Due to the economic downturn, the business of securitizing loans into secondary markets has come under intense scrutiny. This is particularly true in the real estate area, where loans are routinely bundled into mortgage-backed securities and sold to investors. Since the original lender contemplates the immediate sale of the loan, it is common practice for originators to appoint a nominee, as third-party agent, who remains as mortgagee in the land records throughout the life of the loan. MERSCORP, INC., a privately held shareholder Delaware Corporation, operates the nationwide electronic registry for tracking interests in mortgage loans as they move through the securitization pipeline.

Mortgage Electronic Registration Systems, Inc. (MERS), a wholly owned subsidiary of MERSCORP, Inc. that serves as mortgagee in a nominee capacity for the lender and subsequent assignees—upfront and for the life of the loan—is generating nationwide litigation. Distressed borrowers are seizing on the fact that the name of the recorded mortgagee, and the identity of the investor as the beneficial owner of the mortgage loan, do not match. Borrowers (and some bankruptcy judges) are using the mismatch as ammunition for challenging foreclosure actions and avoiding mortgage obligations.

The legal issues have recently come to a head in significant decisions by the Kansas and Minnesota supreme courts. These cases are high-stakes challenges to the MERS registration system. We think the Kansas Supreme Court misconstrued the law in reaching its decision, but the Minnesota Supreme Court got it right.

MERS loses in Kansas. The Kansas case, decided on August 28, is *Landmark National Bank v. Kesler*, 216 P.3d 158 (Kan. 2009). The Kansas high court recently denied motions for reconsideration. There is a possibility that MERS will take the case to the U.S. Supreme Court in an effort to bolster its position as mortgagee and the mortgage showed an address for MERS on millions of recorded mortgages.

In *Landmark*, MERS was the mortgagee as the nominee for the beneficial owner of the junior mortgage loan. When the first mortgagee foreclosed, it did not notify MERS even though MERS was the recorded mortgagee. A default judgment wiped out the second mortgage and the property sold to a third party. The court did not decide the issue of whether MERS was entitled to notice and service of process in the initial foreclosure action, an issue fundamental to the MERS business model. Instead, it narrowly held that the trial court did not abuse its discretion in denying MERS' motion to vacate a default judgment and require joinder of MERS. Under the court's analysis, even if MERS was technically entitled to notice and service in the initial foreclosure action, MERS would not have had a "meritorious defense."

MERS is interpreting the Kansas court's holding narrowly, based on its procedural posture (the difficulty of overturning a judgment under the "abuse of discretion standard"), and is suggesting that the holding is limited because the court did not want to vacate a default judgment. Nevertheless, consumer advocates and some commentators are reading the decision as challenging MERS' basic right to notice of foreclosure actions. For example, Dan Schechter, a law professor at Loyola Law School in Los Angeles, suggests that the case "deprives the assignee of all economic benefit from the mortgage due to

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the involvement of MERS.” He finds it “hard to quarrel with Kansas law” and posits that the law of “most states would be similar.” Ominously, Professor Schechter concludes that dicta in the decision call into question “whether millions of MERS-administered mortgages are really enforceable.” See 2009 Comm. Fin. News 72 (available on Westlaw).

MERS wins in Minnesota. *Jackson v. MERS*, 770 N.W.2d 487 (August 13, 2009) is the Minnesota case. It came to the supreme court of Minnesota by way of a certified question from the federal district court. Borrowers facing foreclosure brought the lawsuit. Purporting to act on behalf of a class, they challenged MERS’ right to proceed under Minnesota’s foreclosure-by-advertisement statute, arguing that MERS had failed to comply with the statutory provisions requiring recording of an assignment of the underlying indebtedness. Minn. Stat. §§ 590.02 and 580.04 (2006). MERS serves as mortgagee for the lender as well as lender’s assigns.

The Minnesota case turned on the legal question of what constitutes an assignment of a mortgage within the meaning of the foreclosure statute. The court answered the certified question in MERS’ favor, holding that “transfers of the underlying indebtedness do not have to be recorded to foreclose a mortgage” under the foreclosure-by-advertisement statute. Therefore, MERS had no reason to re-record, and MERS was the proper mortgagee, with standing to bring the non-judicial foreclosure. Although the certified question focused on Minnesota’s non-judicial foreclosure statute, the court’s interpretation of the general law applicable to assignments of beneficial ownership interests is important.

How MERS works. Some background about how MERS works helps to put into context the legal issues before both courts. MERSCORP, Inc. tracks changes in the beneficial interests in mortgage loans in the secondary markets. MERSCORP, Inc. is similar to the book-entry systems used by the securities industry since the 1970s. A consortium of key players in the real estate financing industry developed MERSCORP, Inc. and MERS, including the GSEs (Fannie Mae, Freddie Mac, and Ginnie Mae) and the Mortgage Bankers Association; their purpose was to facilitate the operation of the mortgage markets. MERS registers about two-thirds of all residential loans in the secondary market—approximately 62 million mortgages. In a nutshell, MERS is mega.

Typically, the parties use the Fannie Mae/Freddie Mac Uniform Security Instrument. It is a three-party agreement among the borrower, lender, and MERS. The mortgage form names MERS as mortgagee of record in a nominee capacity for the original lender and lender’s successors and assigns. The interest conveyed to MERS is “legal title.” The document explicitly grants MERS the right to act on behalf of the lender as required by law or custom, including the right to foreclose

and sell the property. Under the mortgage, the lender (and its assigns) retain “beneficial” title.

Put another way, the MERS’ system intentionally names MERS as the original mortgagee while the originating lender remains as the payee on the note. When beneficial ownership interests transfer in the secondary market from one MERS member to another, (e.g. the note is negotiated and servicing rights are sold), MERSCORP, Inc. tracks these transfers electronically. The idea behind MERS is that the efficiency of the mortgage markets is vastly improved by maintaining MERS as the mortgagee on public records (in a nominee capacity for the lender and assigns) when transfers of mortgage interests (for mortgage loan sellers, warehouse lenders, mortgage investors, documents custodians, and mortgage servicers) are transacted privately pursuant to clearinghouse rules.

The MERS operating agreement also stipulates that MERS will act on behalf of the beneficial owner according to instructions from that member. Rules governing these agency relationships are set forth in member agreements. As a matter of contract, MERS becomes the agent for a new principal, the next purchasing member, each time there is a transfer. Special rules govern situations where parties that are not members of MERS purchase loans. Under these circumstances, the non-member can choose to keep using the MERS system if the servicer is a MERS member, or de-register the loan. When a non-member removes the loan from the MERS system, there is a recorded assignment of the mortgage to the new note holder.

MERS model relies on fundamental legal principles.

Looking at the MERS system as a whole, it relies on well-recognized principles of real property law, the law of negotiable instruments, and basic contracts law. Important analogies in the UCC rules governing security interests in personal property also support the legal model. Here are the essential elements:

- **Use of a nominee on a security instrument is well established:** Both real estate law and the UCC recognize the validity of using a nominee. UCC § 9-502 (a) (2) states that a financing statement is sufficient if it provides the name of the secured party “or a representative of the secured party.” This section codifies the holding of *In re Cushman Bakery*, 526 F.2d 23 (1st Cir. 1975), cert. denied, 425 U.S. 937 (1976). That case also recognizes the validity of using a nominee as mortgagee on the mortgage for recording purposes on behalf of the note holder. See generally, 59 C.J.S. Mortgages § 80 at 116 (mortgages are valid even if the mortgagees of record are nominees or straw persons); 2 Milton R. Friedman, Friedman on Contracts & Conveyances of Real Property, § 6:1:3 (James Charles Smith ed., 7th ed. 2007). In addition, by private contract parties can establish agency

relationships. UCC § 1-103(b) provides that common law agency principles may always supplement the rules governing secured transactions.

- **Article 9 rules apply even though note is secured by a mortgage.** UCC § 9-109(b) provides that “the application of this article to a security interest in a secured obligation is not affected by the fact that the obligation is itself secured by a transaction or interest to which this article does not apply.” In other words, perfection of a security interest or the outright transfer of a note is not affected by the fact that the note is secured by a mortgage. The comments clearly state that “the security interest in the promissory note is covered” by Article 9 “even though the note is secured by a real-property mortgage.”
- **Under Article 9, there is no need to record a mortgage assignment when the note is transferred.** The clear rules of Article 9 provide that when a note transfers, the security interest in the real estate securing the note also transfers. The principle that the “mortgage follows the note” is a common law principle that is codified in UCC § 9-203(g). UCC § 9-308(e) is the analogous rule for perfection. A promissory note evidences the underlying indebtedness. Negotiation occurs when the new note holder takes possession. There are complicated UCC rules that apply regarding the rights of holders, but the basic rule is that there is no requirement to file assignments of the document evidencing the debt.
- **A mortgagee can remain in place even though there are subsequent assignments of the note in accordance with private contractual agreements.** Under UCC § 9-310(c), if a secured party assigns a perfected security interest, an Article 9 filing is not required to continue the perfected status of the security interest against creditors from the original debtor. The original filing provides sufficient notice that there is a lien. Under real estate law, legal title can remain in a mortgagee without invalidating the security instrument even though the beneficial note holder is another party. Here again, the original mortgage does the trick. Both the UCC filing system and real property recordation statutes provide notice to creditors of the original debtor that there is a security interest or lien on the property. Even if the assignee takes no steps to record a new assignment of the mortgage so that it reflects the name of the new assignee, the security interest remains perfected against creditors and transferees of the original debtor. The comments to UCC § 9-310(c) and longstanding case law support this basic principle.

The basic legal model for MERS is a sound one. MERS' operational model relies on the rules set forth in so-called

member agreements. In order for MERS to operate as a reliable and accurate registry, members are responsible for notifying MERS each time there is an event that occurs involving a registered loan in accordance with member rules. For detailed discussion of the relevant law, see Clark and Clark, *The Law of Secured Transactions under the UCC*, ¶¶ 1.08[10][a][iv] and 2.09[2].

A closer look at the Kansas case. The Kansas dispute dates back to 2004, when a borrower named Boyd Kesler took out a first mortgage on a piece of real property in Kansas. Landmark was the original lender on a \$50,000 first mortgage. About a year later, Kesler took out a second mortgage. The second mortgage secured a loan for \$93,100 from Millennia Mortgage Corp. Millennia was a MERS member; the parties used a MERS mortgage form identifying MERS as mortgagee. The structure of the deal indicates that Millennia contemplated selling the loan but intended to retain MERS as the mortgagee of record. The court assumes that this is exactly what happened. In hindsight, we know that the original lender on the second mortgage did, indeed, sell the loan to Sovereign Bank. Subsequently, the borrower filed for bankruptcy. Landmark got relief from the stay, and then filed a foreclosure action, eventually obtaining a default judgment.

Crucial facts turn on notice. The first-mortgage lender notified the original second-mortgage lender, named as lender in the mortgage and a MERS member. In other words, Landmark notified Millennia; however, Landmark did not notify MERS even though MERS was on the mortgage as nominee for the lender. Millennia failed to appear as a party, and apparently failed to notify MERS of the lawsuit. Compounding the notice problems, Millennia did not notify Sovereign, even though Sovereign purchased the loan from Millennia.

MERS tries to intervene after new buyers purchased the property. Landmark sold the property without anyone appearing to enforce the second lien. The sales price was enough to pay off Landmark's first lien and left a surplus of \$37,000. The borrower tried to grab these funds, thinking it had the right to the money since the default judgment had effectively wiped out the second mortgage. At some point, Sovereign, as the beneficial owner of the second mortgage, learned what was happening and attempted to assert its rights. MERS also learned about the mess and filed motions to intervene, contending that it was a necessary party to the foreclosure action.

The district court denied both parties the right to intervene. The Kansas Court of Appeals affirmed the district court. 40 Kan.App.2d. 325, 192 P23d 177 (2008). The Supreme Court took the case on a petition to review, as a matter of first impression in Kansas. The question before the court

came down to a determination of whether the trial court had “abused its discretion” by refusing to permit MERS to join the litigation as a necessary party. Did MERS have a “meritorious defense” or a sufficient property interest to require joinder?

Reading between the lines: the court had trouble with the facts. Reflecting back on the court’s description of the factual scenario, a couple of points jump out:

- The court spends a lot of time wrestling with the language used in the mortgage document and grapples with its terms, finding the document confusing and conflicting with respect to how it described MERS’ role. Under the terms of the mortgage, the lender retains the right to enforce the mortgage but if “necessary to comply with law or custom,” the mortgage provides that MERS can enforce the interests of the lender and assigns.
- Even though the mortgage gave MERS the right to foreclose, the mortgage directed that Millennia, as lender, receive notice. The court had a hard time reconciling the notice provision with MERS’ argument that it was entitled to notice as mortgagee of record.
- The court seems to have trouble sympathizing with MERS, given the facts. MERS is trying to set aside a default judgment after the sale of the property. The way the court tells the story, there are hints that MERS waited too long to object because MERS’ own rules and procedures malfunctioned.

Kansas court misapplies the law. Notwithstanding the tough facts, we think the court should have ruled in MERS favor on the law. The court ruled that MERS, as straw man nominee, essentially lost the power to act for the lender when the note transferred to a new note holder. The court mistakenly failed to recognize that a mortgagee, holding “legal” title under the terms of the mortgage, retains a sufficient interest in the property to act on behalf of a subsequent assignee of the note. Essentially, the court lost sight of long-standing principles regarding the use of nominees on security instruments and ignored fundamental common law principles of agency law. It misconstrued the principle that “the mortgage follows the note.” It wrongly interpreted the maxim as standing for the proposition that when a separation occurs between the note and holder of the legal title to the mortgage, the mortgage lien is wiped out. To the contrary, under Article 9, a new assignment of the mortgage is not required and the original mortgagee continues to act as a vehicle for the purpose of notice for recording purposes. The mortgage remains in place and is just fine.

A closer look at the Minnesota case. This principle that “the mortgage follows the note,” construed correctly, saved the day for MERS in the Minnesota case. In Jackson, the borrowers facing foreclosure argued that the assignees of their mortgage interests were required to record new mortgage assignments in the land records before they had the authority to foreclose under the Minnesota foreclosure-by-advertisement statute. According to the borrowers, subsequent assignments of the underlying debt required recording of new mortgage assignments under Minnesota law.

The Minnesota supreme court properly rejected these arguments, relying on: (a) longstanding rules sanctioning the use of nominees; (b) the principle that since “the mortgage followed the note,” new mortgage assignments were not required in order to keep the mortgage alive and perfected; and (c) a literal reading of the plain language used in Minnesota’s non-judicial foreclosure statutes. This language requires recording of mortgage assignments when there is a change in mortgagees. Since the parties had retained MERS as mortgagee down the assignment line, the court was able to conclude that there had been no assignment of mortgage rights. We agree with the court’s decision and its reasoning.

Damage control. Without doubt, MERS is unhappy with the Kansas situation, both the Supreme Court decision and the way notice of the foreclosure suit escaped detection in the MERS system for too long. To prevent another fiasco, MERS is reminding its members:

- Notify MERS when it is named as a defendant in a foreclosure case even though the member no longer has any ownership interest in the mortgage loan.
- In the situation where there are multiple mortgage holders and the mortgage holders are MERS members, MERS will be wearing multiple hats in any foreclosure action, acting as nominee for the plaintiff and nominee for the defendant. Under these circumstances, the foreclosing party should notify MERS and name it as a defendant. This creates the strange situation where MERS is both plaintiff and defendant.
- Be certain that recorded mortgages reflect MERS as mortgagee and the indexing system reflects MERS as mortgagee.

(MERS Announcement Number 2009-06, dated October 1, 2009, posted on the MERS website).

Bottom line. Given the fallout from the Kansas case, it is not surprising that MERS is looking seriously at an appeal to the United States Supreme Court. We suspect that borrowers will rely inappropriately on *Landmark* as authority for wiping

out mortgage liens in foreclosure cases and will use the case to challenge MERS' ability to enforce liens in bankruptcy court using standing and real party in interest arguments. *Jackson* is the better precedent. Even with *Jackson* in hand, there may be times when the simple fact that MERS is the mortgagee of record is not enough. Depending on the jurisdiction and posture of the litigation, MERS may need to connect the dots for the court by coming prepared with evidence documenting its agency relationship with the investor as owner of the underlying debt. Documenting the link, however, is an evidentiary matter. It does not change the law.

Note: One of the editors of this newsletter, Barkley Clark, is a partner in the firm of Stinson Morrison Hecker LLP, which represented MERS in the Kansas case. He did not participate in the case.

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ATTACHMENT 5:
“Judicial Versus Non-Judicial Foreclosure”
Mortgage Bankers Association
October 2010



Judicial Versus Non-Judicial Foreclosure

Judicial Versus Non-Judicial Foreclosure

In many discussions about mortgage foreclosures the terms **judicial** and **non-judicial** foreclosure are used. They involve very different processes. These terms refer to how individual states handle real estate foreclosure. Under both systems, time frames and terms vary widely from state to state. The following is a brief, general, description of both processes. The accompanying chart (see last page) depicts the varying time frames involved in the judicial foreclosure process.

Judicial Foreclosures

A judicial foreclosure is a court proceeding that begins when the lender files a complaint and records a notice in the public land records announcing a claim on the property to potential buyers, creditors and other interested parties. The complaint describes the debt, the borrower's default and the amount owed. The complaint asks the court to allow the lender to foreclose its lien and take possession of the property as a remedy for non-payment.

The homeowner is served notice of the complaint, either by mail, direct service or publication of the notice. The defendant (borrower) is permitted to dispute the facts (such as show that payments were made), offer defenses or present counterclaims by answering the complaint, filing a separate suit, and/or by attending a hearing arranged by the court. If the defendant shows there are differences of material facts, a trial will be held by the court to determine if foreclosure should occur. In the vast majority of cases, however, the foreclosure action is undisputed because the borrower is in default and cannot offer facts to the contrary. If the court determines the homeowner did default and that the debt is valid, it will issue a judgment in favor of the servicer for the total amount owed, including costs for the foreclosure process. In order for the judge to determine the amount of the judgment, the servicer submits paperwork through an affidavit that itemizes the amounts due.

Twenty two states use judicial procedures as the primary way to foreclose. These include: Connecticut, Delaware, Florida, Hawaii, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, New Jersey, New Mexico, New York, North Dakota, Ohio, Oklahoma, Pennsylvania, South Carolina, South Dakota, Vermont and Wisconsin.

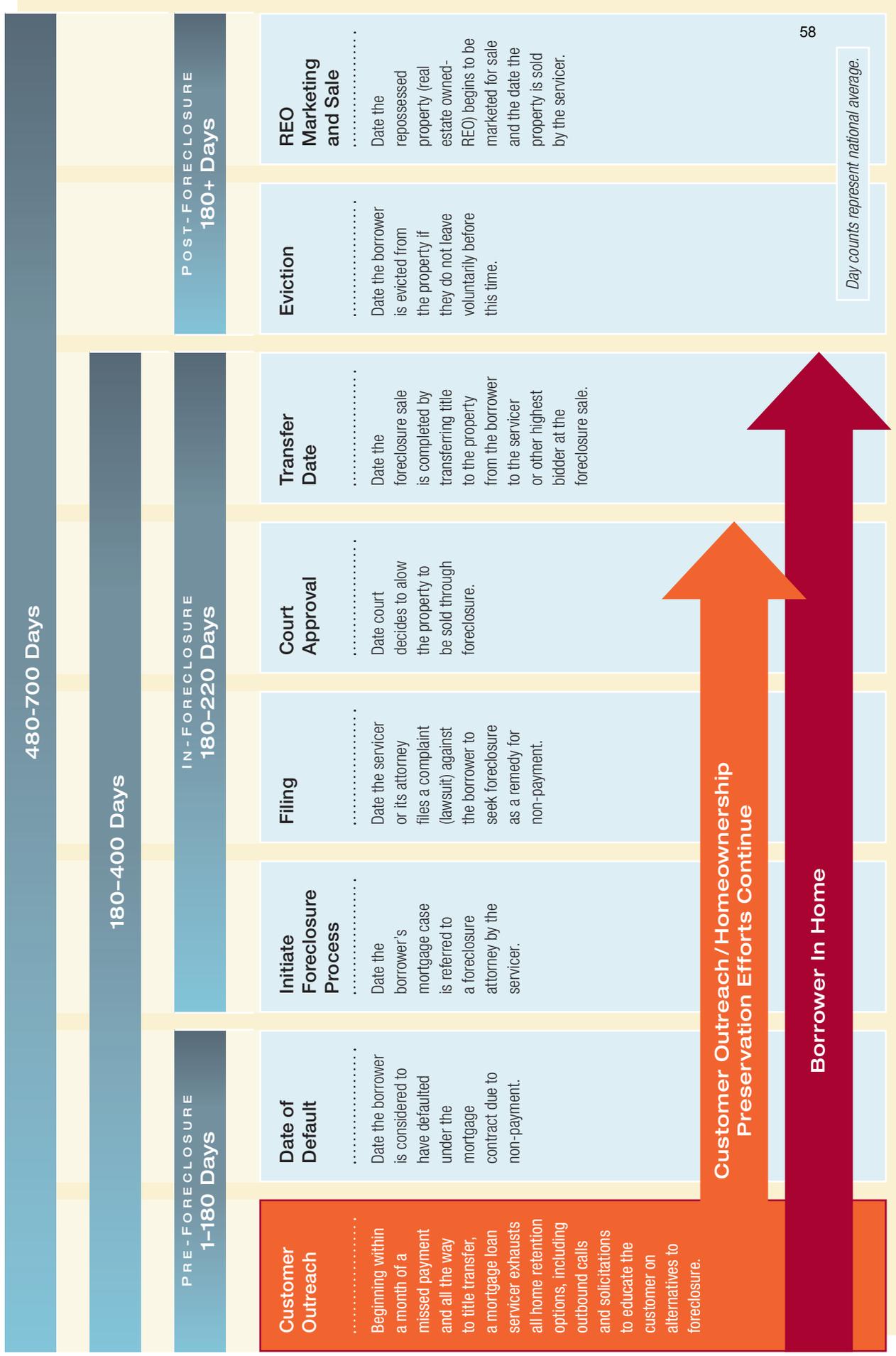
In all other states, foreclosure is usually handled by attorneys who follow a state-provided process. In the mortgage documents, borrowers give lenders the “power of sale” outside of judicial process in the event of an uncured default. Documentation or affidavit issues are not common in these states because of the non-judicial nature of the process.

Next, the court will authorize a sheriff's sale. The sale is an auction of the property open to anyone, and must be held in a public place. Procedures for a sheriff's sale in each locality differ, but the individual with the highest bid is granted the property. After the sale is confirmed by the court, the deed, which transfers ownership, is prepared, recorded and the highest bidder becomes the owner of the property. In most cases, the highest bidder is the servicer, who takes title of the property. The servicer then can sell the property. At this point, it is called **real estate owned (REO)**.

Non-Judicial Foreclosures

The requirements for non-judicial foreclosure are established by state statute; there is no court intervention. When the default occurs, the homeowner is mailed a default letter and in many states a Notice of Default is recorded, at or about the same time. The homeowner may cure the debt during a prescribed period; if not, a Notice of Sale is mailed to the homeowner, posted in public places, recorded at the county's recorder's office, and published in area newspapers/legal publications. When the legally required notice period (determined by each state) has expired, a public auction is held and the highest bidder becomes the owner of the property, subject to recordation of the deed. Prior to the sale, if the borrower disagrees with the facts of the case, he or she can try to file a lawsuit to enjoin the trustee's sale.

Judicial Foreclosure Process





BIOGRAPHY: R.K. Arnold, President & CEO, MERS

R.K. Arnold serves as President & CEO of MERSCORP, Inc. and its subsidiary, Mortgage Electronic Registration Systems, Inc. He joined MERS at its inception in 1996, and served as Senior Vice President & General Counsel until his promotion to President in 1998. He is a member of the MERS Board of Directors. His team has built MERS into the central electronic registry for the mortgage finance industry.

MERS achieved profitability in 2001 and now registers more than half the mortgage loans originated in the United States. The company's goal is a 100% market share nationwide. MERS enables its members to eliminate the need to record assignments by acting as a placeholder for all its members in the local land records. This reduces unnecessary paperwork and makes buying a home more efficient and less expensive. MERS registers loans in every county in every state and serves both the residential and commercial markets. Most recently, the company launched the MERS® eRegistry, which tracks electronic promissory notes and represents the future of mortgage lending.

As General Counsel, **R.K.** managed the successful effort to gain regulatory approval for MERS to serve as original mortgagee of record on uniform security instruments. He orchestrated approval of the Rules Governing Membership in MERS and played a major role in defining the business requirements for development of the MERS® System. Before joining MERS, he served as Vice President & Corporate Counsel at AT&T Universal Card, practiced law with Holloway, Dobson, Hudson & Bachman, and held management positions with USAA and Johnson & Johnson.

R.K. is a former U.S. Army Ranger. He and his wife, Lynne, are both from Oklahoma. He holds a B.B.A. in Finance from the University of Oklahoma, an M.B.A. from the University of Dallas and a J.D. from Oklahoma City University.

RESPONSE OF MERSCORP, INC.

TO QUESTIONS FROM THE

SUBCOMMITTEE ON HOUSING AND COMMUNITY
OPPORTUNITY

HOUSE COMMITTEE ON FINANCIAL SERVICES

NOVEMBER 18, 2010

- **Please describe the origin and role of MERS in recording ownership of real property in the United States.**

MERS¹ is a private company that supports the mortgage finance industry by improving access to, and the reliability of, mortgage loan information, and by making the mortgage finance process more efficient. MERS serves two important functions. First, it maintains a database or registry of mortgage loans, keeping track of changes in servicing rights and beneficial ownership interests in the promissory note over the life of the loan. Second, it can be designated by its members to serve as the mortgagee, or the holder, of the mortgage lien in the public land records.

MERS owns and operates the MERS® System, a central database that tracks the ownership of mortgage loan promissory notes and the servicing rights for mortgage loans. MERS was created by the mortgage finance industry in the mid-1990s as an industry solution to the challenge of tracking loan ownership and servicing information, and the growing volume of mortgage assignments that increased both the expense of mortgage loans and the potential for errors in the public land records when the mortgages are recorded. MERS was conceived and implemented to build upon and supplement, but not displace, the existing public land record system. MERS operates by

¹ Unless otherwise stated, the term “MERS” is used in these answers to collectively refer to MERSCORP, Inc., a Delaware Corporation which owns and operates the MERS® System, an industry database utility, and to Mortgage Electronic Registration Systems, Inc., a wholly owned, bankruptcy remote subsidiary of MERSCORP, Inc. which, as a common agent for the mortgage industry, serves as mortgagee in the county land records as a nominee for the owner of the mortgage loan. The respective roles of MERSCORP, Inc., the MERS® System, and Mortgage Electronic Registration Systems, Inc. are further discussed in these answers and in the MERS testimony.

charging fees to its members (not homeowners), which include 3,000 banks and mortgage lenders across the country.

To understand the role that MERS plays, and the value it brings to consumers, the industry, and the general public, it is important to understand the basics of the mortgage loan process. A real estate loan fundamentally involves two parties—the borrower and the lender—and two documents—a promissory note and a security instrument, commonly called a mortgage.² Also involved are servicers (who act as agent for the note owner) and MERS, which plays a unique and vital role in the overall system as further described in these responses.

When a home loan is originated, the borrower and lender create a written contractual agreement of the terms and conditions for the loan, known as the promissory note. The lender provides money to purchase the house, and in return becomes the owner of the promissory note, with the right to collect payments and enforce the loan terms.

As a further protection for the lender, the borrower and the lender also create a mortgage. The mortgage establishes a lien against the property as collateral for the promissory note's loan, and allows the note owner to foreclose on the property if the borrower does not repay the loan according to the terms of the promissory note.³

² In some states, the security instrument will be a mortgage; in others, it will be a deed of trust. The legal differences between these two forms of security instruments are not germane in this context. For the purposes of this testimony, we will use the term "mortgage" to refer to both mortgages and deeds of trusts.

³ One might assume that the mortgagee (the party with the right to enforce the mortgage) would be the lender or the note owner, but this is often not the case. As discussed later in this testimony, the note owner may elect to conduct business through one or more agents, including having an agent listed as the mortgagee on their behalf. A prime

Together, the promissory note and the mortgage create a “mortgage loan.” While these two documents are linked, they are not the same, and are treated differently upon closing.

Immediately after closing on the loan, the mortgage is recorded at the county land record office, where it is entered into the local index and an official imaged copy is stored. The original mortgage document is returned to the note owner and goes into the master loan file. Recording the mortgage is done for the benefit of the note owner and conveys three essential benefits: 1) it establishes the priority of the note owner’s claim to the property against other creditors; 2) it establishes a right to receive legal notice for any actions against the property that could impact the note owner’s interests; and 3) it puts the world on notice that there is a legal claim against the property. There is generally no requirement to record a mortgage, and a mortgage may be enforced even if it hasn’t been recorded. However, until the mortgage is recorded, the note owner does not receive any of the benefits or protections as described above.

By contrast, after the closing, the note is sent to a custodian (usually a regulated depository institution) for safekeeping on behalf of the note owner.⁴ The note is a negotiable instrument, which means that it can be (and usually is) sold by the original lender to other banks or investors, who may in turn sell the note again in the normal

example of this is Fannie Mae, which owns countless loans but is never listed in the land records as a mortgagee for residential loans.

⁴ Unlike the mortgage, the note is not (and never has been) recorded or stored in the county land records.

course of financial activity.⁵ The Uniform Commercial Code (UCC) Article 3 governs this activity in all fifty states.⁶

The legal principle underlying promissory notes is that legal possession of the note also conveys all of the legal rights inherent in the note; the noteholder is entitled to receive the payments and enforce the loan in the event of a default.⁷ The mortgage is subordinate to the promissory note, which is to say that the rights established in the mortgage flow directly from (and are dependent upon) the rights and the duties established in the note. Without the note, the mortgage has no effect. Likewise, it is commonly said that the “mortgage follows the note” so that when the note changes hands, the mortgage interest automatically follows.

The owners of promissory notes frequently decide that they do not want to be involved with the day-to-day management of the loan. Instead, they will engage a “servicer,” a company that will be responsible for collecting the loan payments and dealing with the borrower on behalf of the note owner. The servicer becomes the agent of the note owner, and it is the servicer (not the note owner) that most people think of

⁵ While the note’s owner may change, the terms of the note do not—the borrower still has the duty to repay the loan, subject to the original terms and conditions. The new owner simply steps into the role of the original lender, with the same rights and obligations. The standard form of note used in the industry discloses that the note may be sold without notice to (or consent by) the borrower and by executing the note, the borrower has agreed to that.

⁶ The transfer of a note is performed through an established process of endorsement and delivery from the seller to the note purchaser, and is similar to the process for another type of negotiable instrument—the common check. As with a check, the seller endorses (signs) the note on the back of the document with instructions transferring their rights to the new owner. The endorsement could name the new purchaser, but is typically made “in blank”, not naming the new owner. A note endorsed in blank is the equivalent of a check made out to cash—it becomes bearer paper, and any person holding the check (or note) has the right to enforce it. A further explanation of this process is provided in Testimony Attachment Three, Karen Gelernt’s American Banker article, *Title Transfer Law 101*, October 19, 2010.

⁷ The holder of a note (i.e., the party in possession) may or may not be the ultimate owner; there are times when the owner of the note permits another party to be the holder of the note on their behalf, including when necessary to prosecute a foreclosure.

as “the mortgage company.”⁸ Just as ownership of the note can change hands, servicing for a loan may also change from one company to another.

MERS is the final element of this system. When servicing rights or promissory notes are sold for loans where MERS is not the mortgagee, the usual practice is for the seller to execute and record an instrument assigning the mortgage lien to the purchaser (commonly referred to as an “assignment”). Assignments are not required by law to be recorded in the land records. The primary reason assignments are recorded (in cases where MERS is not the mortgagee) stems from the appointment of servicers to administer the loan on behalf of the mortgage loan owner. In which case, the servicer will be assigned the mortgage lien (thus becoming the mortgagee) in order to receive the service of process related to that mortgage loan. When Mortgage Electronic Registration Systems, Inc. is the mortgagee (i.e., holds the legal title to the mortgage lien), there is no need for an assignment between its members because it is the common agent for them. It is not the case that the assignments are now being done electronically through the MERS[®] System instead of being recorded in the land records. The need for an assignment is eliminated because title to the mortgage lien has been grounded in Mortgage Electronic Registration Systems, Inc. Moreover, transfers of mortgage notes and servicing rights are not recordable transactions (and have never been reflected in the land records) because they are not a conveyance of an interest in

⁸ The servicer is similar to a landlord in a rental building. The landlord doesn't own the building, but it collects the rent, deals with the tenants, and handles all of the issues associated with the building on behalf of the owners. And just as a building owner can choose to hire or fire a landlord, a note owner can choose to switch servicers.

real property that is entitled to be recorded. Only the transfer of the lien is a conveyance. A promissory note is sold by the seller endorsing the note, and delivering it, to the purchaser. Servicing rights are non-recordable contracts rights. Mortgage Electronic Registration Systems, Inc. remains the mortgagee regardless of the number of these non-recordable transfers that may occur during the life of the loan. Upon such sales, the seller and purchaser update the MERS® System of the transfer with an “electronic handshake” process whereby both parties to a transaction verify and validate the record updates.

To address the inefficiencies and errors created by this process, the mortgage industry—through an open and public process—set out to create a mortgage information clearinghouse and common agent that could step into the place of the servicers as mortgagee, and thereby eliminate the need for the assignments that occurred due to changes in servicing rights. The designation of MERS as the mortgagee is clearly set forth in the mortgage documents that are signed by the borrower at settlement, and the mortgage identifying MERS is what is filed in the land records. The introduction of MERS into this process did not decrease the amount of information available to the public—it actually increased it, by linking the information in the public land records with a central database that provides reliable information regarding a loan’s servicer and owner. Prior to the creation of MERS (when servicers routinely held the mortgage lien for the note owner), the information in the public land records was

not accurate due to delays in recording assignments or missing assignments that never got recorded.

MERS is an industry-created utility that performs three essential and related functions:

- First, MERS maintains the MERS® System, a database that tracks changes in the beneficial ownership of the servicing rights and beneficial ownership interests in the promissory note over the life of the loan.⁹ MERS members provide and update the data on the MERS® System, and MERS works with its members to ensure the accuracy and integrity of the data. The borrower can access the information on the MERS® System to determine the servicer for his or her loan and the ownership of the loan; the information is also available to MERS members on a need-to-know basis.¹⁰
- Second, Mortgage Electronic Registration Systems, Inc.¹¹ serves as a common agent for the mortgage finance industry in the county land records. MERS is the legal owner of the mortgage lien on behalf of its members as their nominee (a limited form of agency). The designation of MERS as nominee and mortgagee is

⁹ MERS tracks the loans registered on its system by means of the Mortgage Identification Number (MIN), an 18-digit identification number that is assigned to each loan. This number is assigned at the early stages of the loan creation process, and remains unchanged for the entire life of the loan, regardless of changes in the loan's ownership or servicing.

¹⁰ MERS complies with the consumer privacy protection laws promulgated by the Graham Leach Bliley Act and the provisions of the Fair Credit Reporting Act.

¹¹ As noted earlier, Mortgage Electronic Registration Systems, Inc., is a wholly owned, bankruptcy remote subsidiary of MERSCORP, Inc. The bankruptcy-remote status of this subsidiary is critical, because it ensures that in the event that MERSCORP, Inc. were to ever suffer a bankruptcy or a fiscal crisis, MERSCORP, Inc.'s creditors could not seize or otherwise impair the mortgages to which Mortgage Electronic Registration Systems, Inc. holds legal title on behalf of its members.

prominently displayed on the mortgage document and is affirmatively approved by the borrower at settlement.¹²

- Third, MERS receives the mortgage-related mail and legal notices concerning the properties for which it serves and mortgagee, and efficiently and expeditiously routes this mail to the appropriate person(s) at the relevant mortgage servicing company.

The role and function of MERS were initially crafted in conformance with, and continues to rest, on long established law and legal principles. For example, the practice of distinguishing a mortgage's legal interest (i.e., the party that owns legal title to the mortgage and appears as mortgagee) and the beneficial interest (i.e., the party that owns the note, is therefore entitled to receive the payments from the mortgage loan, and is therefore the party intended to "benefit" from the lien created by the mortgage) dates back to the creation of the Federal Housing Administration in the 1930s. Fannie Mae, Freddie Mac and many others adopted this model long before MERS was ever conceived.

The MERS[®] System acts as an extension and expansion of the existing public land records system. MERS does not remove or alter any information in the public land records, nor does MERS replace the public land records.¹³ MERS mortgages and mortgage assignments are still recorded in the county land records. However, the MIN

¹² A copy of a sample mortgage document can be found in Testimony Attachment One. A short summary of MERS prepared by the Mortgage Bankers Association can be found in Testimony Attachment Two entitled "MBA Fact Sheet: The Role of Electronic Mortgage Registrations."

¹³ MERS is not involved with the custody or maintenance of mortgage loan documents; the mortgage loan owner and/or servicer handle this. MERS does not have either paper or digital originals or copies of any notes or mortgages.

and the MERS® System now allows public land record information to be linked to information regarding the loan's servicer and holder of the beneficial interest.

- **How many servicers participate in MERS? Which major servicers do not participate? In what ways does non-participation impact MERS' ability to provide accurate and up-to-date information on mortgages?**

MERS functionality is incorporated into virtually all of the servicing software in use today, and through this software (and a MERS membership) all servicers have the ability to access and use the MERS® System (i.e., the MERS database). All major servicers are members of MERS and actively participate in the MERS® System.

The most common example of a "servicer" that does not participate in MERS would be a small community bank or credit union that originates and holds a mortgage loan on its own books, and provides the servicing for the full life of the loan. Also, some mortgage companies only use MERS when they purchase loans from correspondent lenders and brokers. It should be noted that in these cases, the loan is never registered on the MERS® System, and the mortgage is not in the name of MERS.

MERS is able to provide accurate and up-to-date information regarding the loans registered on the MERS® System. As discussed in the written testimony, MERS members have a substantial interest in maintaining accurate and up-to-date information. The "electronic handshake" process whereby both parties to a transaction verify and validate the record updates, helps to ensure that the system remains

accurate. MERS also performs regular system data audits with its members to ensure the integrity of the data on the MERS® System.

However, MERS does not have information on mortgages that are not registered on the MERS® System. Although all of the top 100 lenders and servicers are members of MERS (and use MERS for some part of their business), our best estimate is that half of all home loans are registered on the MERS® System. If all home loans were registered on the MERS® System, it could provide a complete view of the mortgage finance system. Such a global purview would provide greater accountability and transparency, and could be used even more effectively to prevent fraud and abuse. However at present, non-registered loans represent a significant gap in the informational picture.

- **To what extent are MERS members required to update the MERS database with information reflecting the current owner of the beneficial interest in a mortgage loan?**

Our rules and procedures require that the MERS database be updated by the members within a specific time frame whenever there is a closing of a new loan, or transfer of: (1) the beneficial interest in the mortgage loan or (2) the servicing rights, or payoff or foreclosure.

The MERS® System is a tracking system that contains a record of both the servicing rights and beneficial interest information for mortgage loans. There are many reasons why maintaining the accuracy of the data is important to MERS and its members. One

of the most important reasons is that members and the public (including homeowners) rely on the information that is made available through MERS[®] Servicer ID and MERS[®] Investor ID, tools by which MERS provides the free public access (via the internet or a toll free telephone number) to information on the database about the note owner and servicer for each registered loan.

The MERS[®] System holds just a small subset of the universe of information regarding a mortgage loan, and should not be confused with the far more extensive information maintained in the loan file that is held and maintained by the servicer. Information regarding a borrower's payment history and status, loan modification or foreclosure activity is maintained in the servicer's loan file—not on MERS.

As noted in my testimony, a key service provided by MERS is the routing of mail and legal notices regarding a mortgaged property to the appropriate servicer and/or owner for appropriate response and resolution. Failure to receive this information can have serious, negative legal consequences for the servicer and/or owner, up to and including loss of the property interests and the right to enforce the note. This creates a significant incentive for MERS members to maintain an accurate database.

This is re-enforced by the "electronic handshake" that is required to update a record on the MERS[®] System. Because both parties to a transaction must verify and validate the information whenever a record is changed, there is a mutual pressure to execute the updates promptly and accurately. Failure to do so triggers an audit flag for the

MERS team and the servicers, who work together to rapidly resolve any discrepancy and ensure that information is correct.

Furthermore, MERS performs regular system audits and data reconciliations with its members as a further check to ensure the accuracy of the system.

- **To what extent are MERS members required to update the MERS database with information reflecting the location or identity of the entity in possession of promissory notes?**

The MERS® System does not require information regarding the location or custody of the promissory notes for the loans registered on its system. The MERS® System was fundamentally designed to track serving rights and beneficial interests, and does not keep or track any of the underlying mortgage loan documents in any form—physical or digital. The MERS® System provides for the identity of the custodian, the organization that holds the note on behalf of the owner, but the use of that field is optional. If we needed to determine the location of the note for some reason, we would contact the party registered in the investor (i.e., beneficial owner of the note) field to obtain that information.¹⁴

¹⁴ If a judicial foreclosure proceeding is prosecuted in the name of MERS, then our rules require that a MERS certifying officer must be in possession of the note.

- **How does the voluntary nature of updating the MERS database on beneficial ownership assignment conceal the multiple assignment of the same loans to multiple securitization trusts? How does MERS verify that multiple loans have not been pledge to more than one trust?**

First, it should be understood that MERS and the MERS® System have limited involvement in the securitization process. MERS has no role in determining whether any loan will be securitized, into what asset pool or trust that loan might be placed, or the creation of any security that might be issued in reliance upon that loan. All of this activity is controlled by the owners of the loans and legally occurs outside of the MERS® System. It is the obligation of the trustee and its custodian to verify and ensure that the conveyance of loans to the trust is done correctly. MERS is fundamentally a database that tracks servicing rights and beneficial interests based on information provide by its members.¹⁵

Although MERS is not involved in the creation or issuance of mortgage-backed securities, there may still be ways that other parties could utilize the MERS® System to help detect and prevent fraudulent activity with regard to securities. First, every loan registered on the MERS® System is assigned a unique 18 digit Mortgage Identification Number (MIN), which stays with the loan during the entire life of the loan and never changes. If issuers were required to disclose the MIN for each loan associated with the mortgage-backed security, then it should be easy to detect any attempt to associate a

¹⁵ The rating agencies, however, do require that the name of the trustee (or the trust) be registered in the investor field on the MERS® System following the sale of the loan to the securitization trust.

loan with multiple securities. It would also be possible to query the MERS® System to determine if the Investor ID information on the system is consistent with the information contained in the security's disclosure package.

The Securities and Exchange Commission is currently in the process of developing and implementing new regulations regarding standard disclosure requirements for asset-backed securities, including residential mortgage-backed securities and loan-level detail. MERS has submitted comments and is actively participating in this process. It is our belief that MERS, the MIN, and the MERS® System can and should be part of the solution that results in greater transparency for the mortgage-backed securities market.

- **MERS security agreements state that “MERS is the mortgagee” with respect to a loan. Yet, the Supreme Court of Maine recently held that MERS is not actually mortgagee under that state’s real property law. How do you reconcile this contradiction?**

The Maine case of *Mortgage Electronic Registration Systems, Inc. v. Saunders*, 2010 ME 79, Cum-09-640 (MESC), August 12, 2010, was remanded back to the trial court for further determination, so there has been no final ruling. We do not believe that it in any way conflicts with, or otherwise repudiates the basic legal principles upon which the MERS business model is based.

When MERS is named as mortgagee in a mortgage document, it holds the legal title to that mortgage, while the beneficial interest in that mortgage flows to the owner of

the promissory note.¹⁶ A MERS mortgage makes clear that MERS is acting as the nominee (agent) of the lender—the original owner of the beneficial interest in the mortgage—and holds the legal title to the mortgage in this capacity.

A foreclosing party—be it MERS or anyone else—must both hold the note and be the mortgagee of record. As the *Saunders* court noted, Maine’s adoption of the Uniform Commercial Code (UCC) specifically allows the holder of the promissory note the right to enforce its terms. The note is the primary evidence of the borrower’s obligation to repay the debt, and the mortgage is subordinate to the note.

For this reason, MERS rules require that before it will move forward with a foreclosure, MERS must be the mortgagee and the holder of the note.¹⁷ MERS has established rules and procedures for foreclosures to ensure that the necessary evidence is presented to the court and the claim is clearly presented in the pleading. When these rules and procedures are followed, MERS foreclosures are successful. It has been noted in the press and elsewhere that some courts have held that MERS did not have the right to foreclose, despite the fact that MERS is named as the mortgagee on the document. However, these cases are typically the result of a MERS member and/or certifying officer failing to follow the established rules and procedures for a foreclosure. If the MERS member fails to provide the court the proper evidence and plead the case

¹⁶ The practice of separating the legal and beneficial ownership of a mortgage long pre-dates the creation of MERS in 1995. It became a widespread practice in the 1930s following the creation of the FHA, and was subsequently adopted by Fannie Mae, Freddie Mac, and countless others as a standard practice in the mortgage finance industry.

¹⁷ The promissory note may be transferred from the owner to MERS by means of a specific endorsement naming MERS, or (more commonly) by means of an endorsement in blank, which renders the note enforceable, by any holder (including MERS).

appropriately, then they will be unable to establish standing and claim for MERS. The most common failing in these cases is the failure to provide a copy of the note.

The court in Maine recognized and agreed that MERS held legal title. We are aware of no case where MERS has been the mortgagee and presented the note as the noteholder where the court has found that MERS does not have standing to foreclose.¹⁸

- **What entity owns legal title to mortgages registered on the MERS system?**

For the mortgages where Mortgage Electronic Registration Systems, Inc. is named as mortgagee on the mortgage document executed by the borrower, it holds the legal title to that mortgage; the lender (and successive owners of the loan's promissory note) have beneficial and equitable (as opposed to legal) ownership of the mortgage because Mortgage Electronic Registration Systems, Inc. is their common agent. This mortgage document is recorded in the county land records and is listed in the index by the recorder (or clerk) to Mortgage Electronic Registration Systems, Inc.

It is the signing of the mortgage document—not registration on the MERS® System—that creates the legal ownership. The MERS® System is a tracking system, and no legal rights or interests are transferred on, by, or through the MERS® System.

It should also be noted that while most loans registered on the MERS® System are loans where MERS is named the mortgagee, this is not always the case. Using the

¹⁸ This answer is not a formal legal pleading and does not attempt to present all of the legal claims and arguments that MERS may choose to present should this matter move forward in the courts. Nothing in this answer should be construed as an admission or waiver of any legal or material fact, claim or defense.

iRegistration service, mortgage companies are able to register mortgages that are not in the name of MERS on the MERS® System for fraud detection purposes and to comply with requirements of municipalities to provide property preservation contact information on vacant properties owned by the member. In these cases, MERS is not the mortgagee.

- **How does one become a Vice President and/or Assistant Secretary of MERS? What are the qualifications for a person to become a Vice President and/or Assistant Secretary of MERS? What compensation do Vice Presidents and/or Assistant Secretaries of MERS receive? Approximately how many Vice Presidents and/or Assistant Secretaries does MERS, Inc. have? What is MERS policy on conflicts of interest regarding Vice Presidents and/or Assistant Secretaries that are employed by banks or investors that may have other, conflicting interests in a mortgage loan?**

Just like all corporations, MERS conducts business through its corporate officers. Certifying officers conduct much of the business of Mortgage Electronic Registration Systems, Inc. These individuals are employees and officers of MERS members who are appointed as limited officers of Mortgage Electronic Registration Systems, Inc. with the title of vice president and/or assistant secretary by means of a corporate resolution. These certifying officers have a narrow and carefully proscribed scope of limited

authority to act on behalf of MERS.¹⁹ Their appointing resolution also requires that they act in compliance with both MERS rules and the legal requirements of their local jurisdiction.

It is important to note that the certifying officers are the same officers whom the lenders and servicers use to carry out these functions even when MERS is not the mortgagee. MERS has specific controls over who can be identified by its members as a certifying officer. To be a MERS certifying officer, one must be a company officer of the member institution, have basic knowledge of MERS, and pass a certifying examination administered by MERS.

Under the corporate law in Delaware (where MERS is incorporated), there is no requirement that an officer of a corporation also be an employee of that corporation. A corporation is allowed to appoint individuals to be officers without having to employ those individuals or even pay them. This concept is not limited to MERS. Corporations cannot operate without officers; they can and often do operate without employees. It is not uncommon for large organizations to have all its employees employed by an operating company and for those employees to be elected as officers of affiliated companies that are created for other purposes (all corporations are required by law to have officers to act for it). Even for loans where MERS is not the mortgagee, employees of the servicer are generally delegated the power to take actions (e.g., initiate

¹⁹ The authority granted to these officers is limited to: (1) executing lien releases, (2) executing mortgage assignments, (3) initiating foreclosures, (4) executing proofs of claims and other bankruptcy related documents (e.g., motions for relief of the automatic stay), (5) executing modification and subordination agreements needed for refinancing activities, (6) endorsing over mortgage payment checks made payable to MERS (in error) by borrowers, and (7) taking such other actions and executing documents necessary to fulfill the member's servicing duties.

foreclosures) and execute documents (e.g., lien releases and assignments) on behalf of the owner of the loan (and the servicer, in turn, may further delegate such authority to a third-party vendor).

Certifying officers are selected by the MERS member organization, which submits the candidates' names to MERS for approval. As part of the application process, every candidate must take an online examination to confirm that they understand the nature of their relationship to MERS and their duties as a certifying officer. If the appropriate information has been provided, MERS issues a corporate resolution appointing the candidate a limited corporate officer of Mortgage Electronic Registration Systems, Inc.

MERS rules require that certifying officers must hold similar or greater authority on behalf of their MERS member employers, which is to say that they must also have signing authority on behalf of their direct employers.

As of November 15, 2010, MERS has 20,302 certifying officers who work with the more than 31 million active loans registered on the MERS® System.

As noted above, the certifying officers are the same officers whom the lenders and servicers use to conduct activities related to the mortgage loan (even when MERS is not the mortgagee). A conflict of interest does not exist between MERS and its member lenders and servicers because the interest in the mortgage loans held by MERS is co-terminus with that of its members.

- **There have been recent allegations that some banks have used “robo-signers” to process foreclosure paperwork. Are any of these robo-signers Vice Presidents and/or Assistant Secretaries of MERS? How many?**

The term “robo-signers” is a recently coined-term that is used by the media but has no fixed definition. As such, we are not in a position to determine who may or may not have been an alleged “robo-signer.” However, we understand the term to generally refer to bank and/or servicer employees who signed numerous affidavits on mortgage loan foreclosures without (1) individually reviewing each file and/or (2) signing in the presence of a notary public. Mid-level executives at several firms have said in legal depositions that they signed affidavits without *personal* knowledge of the accuracy of these documents.

Over the past several years, through news reports, deposition, litigation, and interaction with our members, MERS became aware that some employees at some servicers may not have been respecting the established legal requirements and or properly following the protocols for foreclosures or other legal matters. We have also determined that some of these individuals were MERS certifying officers. In these cases, MERS has taken steps to remediate the problem. These remedial efforts include:

- Requiring the retraining and recertification of the certifying officer on MERS procedures for certifying officers;
- Suspending or terminating the certifying officer’s relationship with MERS if retraining is unsuccessful in addressing the problem;

- Fining member organizations that have failed to follow MERS rules;
- Terminating the relationship between MERS and its members that are recalcitrant in following MERS rules.

MERS has a culture of being proactive and responsive when issues come to our attention:

- In 2005, upon seeing evidence that the lost note affidavit process was being abused in Florida, MERS also instituted a national policy prohibiting any foreclosure in the name of MERS based upon a lost note affidavit.
- When it became clear to MERS that there was a significant problem with the foreclosure practices in Florida, MERS instituted a moratorium on foreclosures in the name of MERS in that state.²⁰
- When MERS learned that some members were having subordinate employees appointed as MERS certifying officers, MERS instituted a new requirement that certifying officers must also be officers and/or hold signing authority for their sponsoring MERS member.

MERS continues to gather information about potential problems with certifying officers (including information from news reports earlier this year) and we are working to further improve our standards and processes for certifying officers. Planned improvements include:

²⁰ MERS certifying officers retained the authority to perform mortgage assignments.

- Requiring that all MERS certifying officers recertify on an annual basis to ensure that the certifying officer understands his or her duties, authorities, relationship and responsibilities as a MERS limited corporate officer.
- Requiring that all MERS certifying officers participate in a live, face-to-face training session through the MERS annual national conference, regional conference, or an online “webinar.”
- Increasing random and targeted auditing of certifying officer activities to verify compliance with MERS rules and identify candidates for further training or other appropriate remediation efforts.