S.J. QUINNEY COLLEGE OF LAW
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Committee on the Judiciary

Hearing on: "Foreclosed Justice: Causes and Effects of the Foreclosure Crisis"

Written Testimony of

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It is an honor to appear today before this Committee. Thank you for the opportunity to share some thoughts on our national foreclosure crisis. My name is Christopher Peterson and I am the Associate Dean for Academic Affairs and a Professor of Law at the University of Utah where I teach contract and commercial law classes. I commend you, Chairman Conyers, Representative Smith, and other members of the Committee for organizing these hearings and for providing an opportunity to discuss this important and timely national issue.

The foreclosure crisis is an extremely complex problem. With so many fundamental changes, opportunities for moral hazard, agency cost problems, consumer abuses, and impending lawsuits, it is easy to lose track of some of the basic legal and business practice problems that departed from past traditions and helped bring us to our present situation. In particular, it is somewhat perplexing that relatively little attention has been paid to the one company that has been a party in more problematic mortgage loans than any other institution. Mortgage Electronic Registration Systems, Inc., commonly known as MERS, is a corporation registered in Delaware and headquartered in Reston, Virginia.[1] MERS operates a computer database that includes some information on servicing and ownership rights of mortgage loans.[2] Originators, servicers, and other financial institutions pay membership dues and per-transaction fees to MERS in exchange for the right to use and access MERS records.[3] In addition to operating its computer database, MERS also pretends to own mortgage loans in order to help its members avoid paying fees to county governments.

My testimony is largely derived from two scholarly articles I have written on this topic which I invite the committee to review for further information.[4] My prepared statement today will: (1) discuss the Origin and Business Practices of MERS; (2) explore the problematic legal foundation of MERS; (3) suggest that MERS is a deceptive and anti-democratic institution designed to deprive county governments of revenue; (4) explain how MERS is undermining mortgage loan and land title record keeping; (5) argue that MERS was a contributing factor in the foreclosure crisis and has made resolving foreclosures more difficult; and (6) propose some solutions for the committee to consider.

I. The origins and Business Practices of MERS

Since the founding of the American republic each county in the United States has maintained records of who owns the land within that county.[5] Most states have tracked changes in ownership of land, including mortgages and deeds of trust, by maintaining records indexed through the names of

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1. Carson Mullen, *MERS: Tracking Loans Electronically,* MORTGAGE BANKING, May 31, 2000, at 63.
2. Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, Jan. 1, 1997, at 42.
3. *Id.*
4. Both articles are available for download free of charge: Christopher L. Peterson, *Foreclosure, Subprime Mortgage Lending, and the Mortgage Electronic Registration System,* 78 U. OF CINCINNATI LAW REVIEW 1359 (2010) (available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1469749&download=yes); and Christopher L. Peterson, *Two Faces: Demystifying the Mortgage Electronic Registration System's Land Title Theory,* REAL PROPERTY, PROBATE AND TRUST LAW JOURNAL (*forthcoming* 2010) (public working draft available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1684729).
5. PATTON AND PALOMAR ON LAND TITLES § 4 (3d ed. 2003).

grantors and grantees.[6] These grantor-grantee indexes allow individuals and businesses contemplating the purchase of land to investigate (or hire a title insurer to investigate) whether a seller or mortgagor actually owns the land they are offering for sale or mortgage. Communities have traditionally elected their county recorders or registers of deed, providing an important democratic check and balance in the preservation of property rights. A public, enduring, authoritative, transparent record of all land ownership provides a vital information infrastructure that has proven indispensible in facilitating not only mortgage finance, but virtually all forms of commerce.[7] County real property records are the oldest and hitherto most stable metric tracking the "American dream" of family homeownership.

To facilitate this service, county recorders charge modest fees on documents they record. While there is considerable variety in amount and in the method of calculating these fees, a charge of about $35.00 for a mortgage is typical. County recorders use these fees to fund their offices as well as to contribute to county and state revenue. Some county's use real property recording fees to fund their courts, legal aid offices, schools, and police departments.

For centuries American mortgage lenders have eagerly recorded their mortgages loans with county recorders because of incentives created by state land title laws. For example, if a mortgagee fails to properly record its mortgage, and then someone subsequently buys or lends against the home, the subsequent purchaser can often take priority over the first mortgagee.[8] Similarly, where a mortgagee assigns a mortgage to an investor, that investor would eagerly record documentation reflecting the assignment to protect herself from the possibility that the original mortgagee would assign the same mortgage to a different investor.[9]

In the mid-1990s mortgage bankers decided they did not want to pay recording fees for assigning mortgages anymore.[10] This decision was driven by securitization—a process of pooling many mortgages into a trust and selling income from the trust to investors on Wall Street. Securitization, also sometimes called structured finance, usually required several successive mortgage assignments to different companies. To avoid paying county recording fees, mortgage bankers formed a plan to create one shell company that would pretend to own all the mortgages in the country—that way, the mortgage bankers would never have to record assignments since the same company would always "own" all the

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[6] 14 POWELL ON REAL PROPERTY §82.03[2][b].

[7] Gary A Jeffress & Lynn C. Holstein, *An International Survey of Real Property Recording Costs and Some Characteristics: A Preliminary Evaluation*, 5 URISA J. 53, 53 (1993) (international survey suggesting recording systems are a "precondition of an efficient land market").

[8] POWELL ON REAL PROPERTY § 82.02[1][a].

[9] *See, e.g.,* Connecticut Mut. Life Ins. Co. v. Talbot, 14 N.E. 586 (Ind. 1887) ("It is settled everywhere that unrecorded assignments of mortgages are void as against subsequent purchasers, whose interests may be affected thereby, and whose conveyances are duly recorded, provided such assignments are embraced by the recording acts."); Bacon v. Van Schoonhoven, 42 Sickels 446, 1882 WL 12538 (N.Y. 1882) ("The assignments of the . . . mortgage are also conveyances within the act. This is well settled by authority, and such assignments, if not recorded, are void, not merely as against subsequent purchasers of the same mortgage, but also as against subsequent purchasers of the mortgaged premises, whose interests may be affected by such assignments, and whose conveyances are first recorded.")

[10] Phyllis K. Slesinger & Daniel McLaughlin, *Mortgage Electronic Registration System*, 31 ID. L. REV. 805, 810-12 (1995) (describing an Ernst & Young study commissioned by mortgage banker to study how much money they could avoid paying to county governments through the MERS system).

mortgages.[11] They incorporated the shell company in Delaware and called it Mortgage Electronic Registration Systems, Inc.[12]

Even though not a single state legislature or appellate court had authorized this change in the real property recording, investors interested in subprime and exotic mortgage backed securities were still willing to buy mortgages recorded through this new proxy system.[13] Because the new system cut out payment of county recording fees it was significantly cheaper for intermediary mortgage companies and the investment banks that packaged mortgage securities. Acting on the impulse to maximize profits by avoiding payment of fees to county governments much of the national residential mortgage market shifted to the new proxy recording system in only a few years. Now about 60% of the nation's residential mortgages are recorded in the name of MERS, Inc. rather than the bank, trust, or company that actually has a meaningful economic interest in the repayment of the debt.[14] For the first time in the nation's history, there is no longer an authoritative, public record of who owns land in each county.

MERSCORP, Inc., a company closely affiliated with MERS, Inc., now maintains an electronic database that tracks mortgage servicing rights—the right of a company to collect monthly payments on behalf of the actual economic owner or owners of a loan. Instead of paying county governments, financial institutions pay MERSCORP membership fees and per transaction fees for access to the MERS database and to compensate MERS, Inc. for pretending to own the mortgages these financial institutions register on the MERSCORP database.[15] Sometimes MERSCORP also tracks ownership rights—that is actual assignments—but only if investors willingly volunteer this information.[16] Financial institutions have been cavalier about informing MERSCORP of changes in servicing and ownership rights of mortgages because they believe there are no legal penalties for neglecting to make this information available.

II. The problematic legal foundation of MERS

MERS's rights vis-à-vis mortgages registered on the MERSCORP database have created a conundrum for courts, borrowers, and foreclosure attorneys. In boilerplate security agreements included in mortgages around the country, lenders included this clause:

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[11] Peterson, *Foreclosure, supra* note 4, at 1368-73; Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997.

[12] Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997; Carson Mullen, *MERS: Tracking Loans Electronically,* MORTGAGE BANKING, May 31, 2000, 62.

[13] Peterson, *Foreclosure supra* note 4, at 1368-73. At least one state, Minnesota, later explicitly authorized MERS recording by amending its recording act to expressly permit nominees to record "[a]n assignment, satisfaction, release, or power of attorney to foreclose." Act of Apr. 6, 2004, ch. 153, § 2, 2004 Minn. Laws 76, 76-77 (codified at Minn.Stat. § 507.413 (2008)). *See generally* Jackson v. Mortgage Electronic Registration Systems, Inc., 770 N.W.2d 487 (Minn. 2009) (interpreting this statute). However, this legal change was not enacted until long after financial institutions had already been using the MERS system in that state. Similar changes have not been enacted nationwide.

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

[15] Howard Schneider, *MERS Aids Electronic Mortgage Program*, MORTGAGE BANKING, January 1, 1997. Unlike mortgage loan servicers, which are compensated for foreclosure services, MERS does not receive any compensation for assisting in foreclosures. Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 88 (hereinafter: Arnold Deposition).

[16] Financial institutions have not reliably updated the MERS maintained database when they assign loans to businesses that are not members of the MERS system. *See* In re Hawkins, 2009 WL 901766, at n.35 (B.D.Nev).

> "MERS" is Mortgage Electronic Registration Systems, Inc. MERS is a separate corporation that is *acting solely as 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.[17]

This passage, and a similar passage naming MERS the beneficiary in deeds of trust, is confusing to courts, borrowers, and even foreclosure attorneys. On the one hand, MERS purports to be acting as a nominee—a form of an agent. On the other hand, it also is claiming to be an actual mortgagee, which is to say an owner of the real property right to foreclose upon the security interest. It is axiomatic that a company cannot be both an agent and a principal with respect to the same right.[18] In litigation all across the country, attorneys representing MERS frequently take inconsistent positions on the legal status of the company, depending on the legal issue at hand.

Both the MERS-as-an-agent and the MERS-as-an-actual mortgagee theories have significant legal problems. If MERS is merely an agent of the actual lender, it is extremely unclear that it has the authority to list itself as a mortgagee or deed of trust beneficiary under state land title recording acts. These statutes do not have provisions authorizing financial institutions to use the name of one shell company instead of all the actual owners of interests in land. After all, the point of these statutes is to provide a transparent, reliable, record of actual—as opposed to nominal—land ownership. It is legally unclear that recording a mortgage with MERS listed as a mortgagee is sufficient to create a perfected security interest. A basic objective in recording mortgages is to establish priority *vis-à-vis* other lenders, lienors, and buyers. With the exception of Minnesota, every state land title act—the statutes that set out the rules granting priority through recording—was written <u>before</u> MERS came into being. The legislatures that drafted these statutes did not contemplate the possibility that every lender in the country would record their loans in the name of one shell company owned by banks. State supreme courts are currently free to decide that recording in the name of this proxy-mortgagee-shell-company does not perfect the mortgage. Will state Supreme Court's insist on transparent real-party-in-interest recording in this context? Before the financial crisis and all of the documentation problems our country is facing emerged, perhaps it appeared to be a safe bet. But now, it is much less certain that state appellate courts will allow the finance industry to get away with this power grab that privatizes the centuries old public record keeping system.

Counsel for MERS will no doubt continue to point to the occasional case from our history where one court or another has allowed some form of recording with some unusual agency relationship involved. They will say that these occasional cases prove their concept is "legal." But the committee should step back and think about this claim for a moment. Is there <u>really</u> a case that proves that their concept is legal? No. The concept was totally new in the history of the country so there will be no facts that could have given rise to binding case law. Every case the MERS points to will have the potential to be distinguished by a state Supreme Court that believes its legislature did not authorize this type of

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[17] Mortgage Electronic Registration Systems, Inc. v. Bluming, No. GD05-16795, Civil Division, Court of Common Pleas of Allegheny County, PA, slip op. (May 31, 2006) (J. Timothy Patrick O'Reilly).

[18] Restatement (Third) of Agency Law §§1.01, 1.02.

change to the system. And those courts will be on solid ground because—let's be honest—state legislatures simply did not willfully grant permission for this radical change in recording. The land title statutes contemplate recording by many different actual mortgagee's and deed of trust beneficiaries, not by one single a shell company that stands in the place of the entire industry. Counsel for MERS will not find a case that binds a state supreme court to hold otherwise. The truly conservative position on these cases will be to insist that radical changes to the legislatures' land title acts be made by legislatures, not by industry trade associations. Some state Supreme Court justices are likely to resent turning over the county recorders' democratically maintained recording system enshrined in law by the democratically elected legislature to a bank-owned shell company.

Conversely, if MERS is actually a mortgagee, then while it may have authority to record mortgages in its own name, both MERS and financial institutions investing in MERS-recorded mortgages run afoul of longstanding precedent on the inseparability of promissory notes and mortgages. Since the 19th century a long and still vital line of cases has held that mortgages and deeds of trust may not be separated from the promissory notes that create the underlying obligation triggering foreclosure rights.[19] These cases do not merely hold that mortgages follow notes as a matter of default law, but that mortgages cannot legally be separated from notes. Thus, in Carpenter v. Longan the United States Supreme Court announced the classic statement of this rule: "the note and mortgage are *inseparable*…,

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[19] *In* re Bird, 2007 WL 2684265, at ¶¶ 2-4 (Bkrtcy.D.MD. 2007) ("The note and mortgage are inseparable; the former as essential, the latter as an incident. An assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity. . . . It is equally absurd to assume that such bifurcation was intended because such a bifurcation of the note from the deed of trust would render the debt unsecured."); *In re Leisure Time Sports, Inc.* 194 B.R. 859, 861 (9th Cir.1996) (stating that "[a] security interest cannot exist, much less be transferred, independent from the obligation which it secures" and that, "[i]f the debt is not transferred, neither is the security interest"); In re BNT Terminals, Inc., 125 B.R. 963 (Bankr. N.D. Ill. 1990) ("An assignment of a mortgage without a transfer of the underlying note is a nullity. . . . It is axiomatic that any attempt to assign the mortgage without transfer of the debt will not pass the mortgagee's interest to the assignee."); Yoi-Lee Realty Corp. v. 177th Street Realty Associates, 208 A.D.2d 185, 626 N.Y.S.2d 61, 64 (N.Y.A.D. 1 Dept.,1995) ("The mortgage note is inseparable from the mortgage, to which the note expressly refers, and from which the note incorporates provisions for default."); In re AMSCO, Inc., 26 B.R. 358, 361 (Bkrtcy. Conn., 1982) (reaffirming that "[t]he note and mortgage are inseparable"); Barton v. Perryman, 577 S.W.2d 596, 600 (Ark., 1979) ("[A] note and mortgage are inseparable."); Trane Co. v. Wortham, 428 S.W.2d 417, 419 (Tex. Civ. App. 1968) ("The note and mortgage are inseparable. . . ."); Kirby Lumber Corp. v. Williams, 230 F.2d 330, 333 (5th Cir. 1956) ("The rule is fully recognized in this state that a mortgage to secure a negotiable promissory note is merely an incident to the debt, and passes by assignment or transfer of the note. * * * The note and mortgage are inseparable. . . ."); *Kelley v. Upshaw,* 39 Cal.2d 179, 192, 246 P.2d 23 (1952) ("In any event, Kelley's purported assignment of the mortgage without an assignment of the debt which is secured was a legal nullity."); Hill v. Favour, 52 Ariz. 561, 84 P.2d 575 (Ariz. 1938) ("The note and mortgage are inseparable; the former as essential, the latter as an incident.)"; Denniston v. C.I.R., 37 B.T.A. 834, 1938 WL 373 (B.T.A. 1938) ("All the authorities agree that the debt is the principal thing and the mortgage an accessory. . . The mortgage can have no separate existence."); West v. First Baptist Church of Taft, 123 Tex. 388, 71 S.W.2d 1090, 1098 (Tex. 1934) ("The trial court's finding and conclusion ignore the settled principle that a mortgage securing a negotiable note is but an incident to the note and partakes of its negotiable character. . . . The note and mortgage are inseparable; the former as essential, the latter as an incident.") (citations omitted); First Nat. Bank v. Vagg, 65 Mont. 34, 212 P. 509, 511 (Mont. 1922) ("A mortgage, as distinct from the debt it secures, is not a thing of value nor a fit subject of transfer; hence an assignment of the mortgage alone, without the debt, is nugatory, and confers no rights whatever upon the assignee. The note and mortgage are inseparable; the former as essential, the latter as an incident. An assignment of the note carries the mortgage with it, while the assignment of the latter alone is a nullity. The mortgage can have no separate existence.") (citations omitted); Southerin v. Mendum, 5 N.H. 420, 1831 WL 1104, at ¶ 7 (N.H. 1831) ("[T]he interest of the mortgagee is not in fact real estate, but a personal chattel, a mere security for the debt, an interest in the land inseparable from the debt, an incident to the debt, which cannot be detached from its principal.").

the assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity."[20]

This ruling by the Supreme Court is fundamentally in tension with MERS' explanation of its ownership of mortgages. For instance, MERS has stated:

> Mortgage Electronic Registration systems, Inc. (MERS) gets its authority to assign and/or discharge a mortgage because *MERS is the mortgagee*, and as such holds legal title to the mortgage. . . . The nominee language does not take away from the fact that *MERS is the mortgagee*.[21]

Ironically, trustees of residential mortgage backed securitization trusts *also* claim to own legal title to the same mortgages that MERS claims to own.[22] Anglo-American law includes no tradition that supposes *two different simultaneous legal titles* for the same interest in land. Moreover, if the mortgage and the note are "inseparable"[23] MERS cannot be the mortgagee unless it is also the original payee on the note. This is why the Maine Supreme Court recently held: "MERS is not a mortgagee… because it has no enforceable right in the debt obligation securing the mortgage."[24] Similarly the Kansas Supreme Court astutely recognized that MERS' legal position is incoherent when a unanimous court wrote:

> What meaning is this court to attach to MERS's designation as nominee for [the lender]? The parties appear to have defined the word in much the same way that the blind men of Indian legend described an elephant—their description depended on which part they were touching at any given time.[25]

III. MERS is a Deceptive and Anti-Democratic Institution

As a practical matter, the incoherence of MERS' legal position is exacerbated by a corporate structure that is so unorthodox as to arguably be considered fraudulent. Because MERSCORP is a company of relatively modest size, it does not have the personnel to deal with legal problems created by its purported ownership of millions of home mortgages. To accommodate the massive amount of paperwork and litigation involved with its business model, MERSCORP simply farms out the MERS, Inc. identity to employees of mortgage servicers, originators, debt collectors, and foreclosure law firms.[26] MERS invites financial companies to enter names of their own employees into a MERS webpage which

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[20] Carpenter v. Longan, 83 U.S. 271, 274, (1872) (emphasis added).

21.Posting of Sharon Horstkamp, MERS General Counsel, http://www.mersinc.org/forum/viewreplies.aspx?id=13&tid=73 (Apr. 8, 2004, 12:42PM) (emphasis added).

[22] For example, securitization pooling and servicing agreements will typical include language where a securitization depositor warrants that "the Mortgage Loan, including the Mortgage Note *and the Mortgage*, . . . [are]not subject to an assignment or pledge, and *the Depositor* had good and marketable title to and . . . *[is] the sole owner thereof*." CHASE MORTGAGE FINANCE CORPORATION, DEPOSITOR, JPMORGAN CHASE BANK, N.A., SERVICER AND WACHOVIA BANK, N.A., TRUSTEE POOLING AND SERVICING AGREEMENT, Dated as of November 1, 2005, $1,900,007,729.12, Multi-Class Mortgage Pass-Through Certificates Series 2005-A1, at § 3.01(l).

[23] Carpenter, 83 U.S. at 274.

[24] *Id.* at ¶ 15.

[25] *Id.* at 165-66.

[26] Arnold Deposition at 196-98; Mortgage Electronic Registration System, Inc., MERS Law Seminar for USFN Conference, 15-16 (April 21, 2002) (document on file with author) (providing a sample certifying officer resolution).

then automatically regurgitates boilerplate "corporate resolutions" that purport to name the employees of other companies as "certifying officers" of MERS.[27] These certifying officers also take job titles from MERS stylizing themselves as either assistant secretaries or vice presidents of the MERS, rather than the company that actually employs them. These employees of the servicers, debt collectors, and law firms sign documents pretending to be vice presidents or assistant secretaries of MERS, Inc. even though neither MERSCORP, Inc. nor MERS, Inc. pays any compensation or provides benefits to them. Astonishingly, MERS "vice presidents" are simply paralegals, customer service representatives, and foreclosure attorneys employed by other companies. MERS even sells its corporate seal to non-employees on its internet web page for $25.00 each.[28] Ironically, MERS, Inc.—a company that pretends to own about 60% of the nation's residential mortgages—does not have any of its own employees but still purports to have about twenty thousand assistant secretaries and vice presidents. This corporate structure leads to inconsistent positions, conflicts of interest, and confusion.[29]

Furthermore, it is important to take a step back for a moment to look at these relationships from the perspective of a confused, frightened homeowner teetering on the brink of foreclosure and possibly even homelessness.[30] How is a homeowner to understand with whom they can negotiate a settlement, or from whom to obtain additional information, or how to distinguish a legitimate employee of a legitimate company from the thousands of mortgage related con artists and charlatans currently swirling around American families?[31] Congress' Consumer Credit Protection Act in general, and the Fair Debt Collection Practices title of that Act in particular, once took the position that even misleading (as opposed to false) representations had no place in the debt collection industry because of the great potential for consumer abuse and the threat to the American economy from undermining our collective faith in financial markets and institutions.[32] To effectuate this policy of transparency and honesty, misrepresentations and misleading statements are evaluated from the perspective of the "least sophisticated consumer" standard.[33] Unsophisticated consumers that receive communications from a MERS "vice president" or "assistant secretary" are likely to believe that this individual serves a different role in the foreclosure process than the individual actually does. Having foreclosure communications

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[27] MERS, Corporate Resolution Request Form, www.mersinc.org/MersProducts/forms/crrf/crrf.aspx (last viewed: April 6, 2009).
[28] *Id.*
[29] *Compare* MERS Forum, FAQ with Sharon Horstkamp, MERS Vice President and Corporate Counsel, www.mersinc.org/forum/viewreplies.aspx?id=13&tid=73 last viewed June 9, 2004 ("Mortgage Electronic Registration systems, Inc. (MERS) gets its authority to assign and/or discharge a mortgage because *MERS is the mortgagee*, and as such holds legal title to the mortgage. … The nominee language does not take away from the fact that *MERS is the mortgagee*.") (emphasis added); *with* Brief in Support of Defendant's Motion to Dismiss at 3, King v. Ocwen, Civil Action No. 07-11359, 2008 WL 2063553 (E.D.Mich, April 14, 2008) (arguing that MERS could not be liable for Fair Debt Collection Practices Act violations because "*HSBC was the mortgagee* for the property. Ocwen is the servicer for the property. [And,] MERS acted solely as the nominee for the original mortgagee of the property") (emphasis added).
30.*Clomon*, 988 F.2d at 1318 ("The basic purpose of the least-sophisticated-consumer standard is to ensure that the FDCPA protects all consumers, the gullible as well as the shrewd. This standard is consistent with the norms that courts have traditionally applied in consumer-protection law.").
31.*See* John Leland, *Swindlers Find Growing Market in Foreclosures,* N.Y. TIMES, Jan. 15, 2009, at A1; Vivian S. Toy, *Penetrating the Maze of Mortgage Relief*, N.Y. TIMES, June 14, 2009, at RE1; Riva Richmond, *Online Scammers Target the Jobless*, N.Y. TIMES, Aug. 6, 2009, at B6.
32.15 U.S.C. § 1692(a) ("There is abundant evidence of the use of abusive, deceptive, and unfair debt collection practices by many debt collectors. Abusive debt collection practices contribute to the number of personal bankruptcies, to marital instability, to the loss of jobs, and to invasions of individual privacy."); *id.* § 1692(c) ("Means other than misrepresentation or other abusive debt collection practices are available for the effective collection of debts.").
33.*See Clomon*, 988 F.2d 1314; Gammon v. GC Servs. Ltd. P'ship, 27 F.3d 1254 (7th Cir. 1994).

conducted in MERS's name may lead consumers to believe that the servicer has turned the case over to a quasi-official entity that lacks the authority to negotiate loan modifications, short sales, or settlements. The effect could be to pacify the consumer at the point they are most likely to resist through actively litigating (often in a pro se capacity) their all too often legitimate counterclaims and defenses. Indeed, this is precisely the sort of deception targeted by Congress' statute promoting "fair" debt collection.

A fair critique of MERS must include recognition of the dated, expensive, and sometimes cumbersome nature of county real property records systems. Unlike the relatively homogenous personal property lien recording systems governed by Article 9 of the UCC, the National Conference of Commissioners on Uniform State Laws and the American Law Institute have not been able to prevail on state legislatures to standardize real property mortgage and recording laws. Moreover, unlike personal property lien records, which are usually maintained by a secretary of state, real property records are generally maintained by each county. This further diversifies recordkeeping standards and operating procedures. Even with the use of title insurer plant copies, recording and searching in county property records is time consuming, expensive, and often not especially reliable.[34] In contrast, MERS gives each loan a unique identifier, is accessible through the Internet, and is organized in one nationwide system.[35] That being said, many county recorders have rapidly improved their processes recently including over 480 jurisdictions that are now offering fully electronic recording of mortgages and mortgage assignments.

Still, the problem with MERS is not just about what MERS does wrong, but also what the process of creating MERS prevented. By taking the reformation of the county recording systems created by state law upon itself, MERS and the mortgage finance industry circumvented the state and national debate that normally precedes significant legislative change. The MERS system, while digital and nationwide in scope, is not equally available to all. It has given a single corporation the opportunity to grant special "vice president" status to its favored side in foreclosure disputes. It has been manipulated into a device to make foreclosure easier and more anonymous for financiers. The financial industry could have channeled its dissatisfaction with county property records into a campaign for legal reform. This would have necessitated a debate where consumers, county officials, researchers, poverty advocates, and anyone else could have participated. If the finance industry put its formidable legislative muscle behind a public reformation of county recording systems fifteen years ago, perhaps today we would have a national system maintained by a federal regulator, or statewide systems supported by a new article of the UCC. Instead financiers chose to act alone, creating an entirely new system that competes financially with public records, undermines the accuracy of public records, and was never authorized by the elected leaders that guide a republican system of law.

In a moment of refreshing candor, not long ago MERS' President concluded an extolling public relations piece with the acknowledgment that "MERS is owned and operated by and for the mortgage

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34. 14 POWELL ON REAL PROPERTY § 82.03[2].

35. R.K. Arnold, *Yes, There is Life on MERS*, 11 Prob. & Prop., July/Aug. 1997, at 32, 35.

industry."[36] It is ironic, and perhaps not coincidental, that the syntactical form of the sentence bears such close resemblance to President Lincoln's Gettysburg address. One will no doubt recall that Americans have generally aspired to "government 'of the people, by the people, for the people,'" rather than of, by, and for the mortgage bankers.[37] MERS's attempt to "capture every mortgage loan in the country"[38] is an effort to supplant the public land title recording systems' lien records, many of which predate the Constitution itself, with a purely private system. This effort is without question a surrender of the messy compromises inherent in representative democracy to the seductively easy lure of mercantile oligarchy. Perhaps those of us with romantic attachments to our Republic and the rule of law will be excused for supposing that if the mortgage bankers wanted a newer, more efficient, national land title recording system, they should have asked Congress or the legislatures first.

IV. MERS is Undermining Mortgage Loan and Land Title Record Keeping

MERS describes itself as "an innovative process that . . . eliminates the need to prepare and record assignments when trading residential and commercial mortgage loans."[39] The phrase, which the company uses both in legal briefs and public relations material, hints that recording assignments was merely some useless, archaic formality. It is far from clear that state appellate courts will agree that MERS does eliminate the need to record assignments. But even if MERS does eliminate the need to record, it most certainly does not eliminate the need for records. The policy justifications behind recording statutes are as germane today as they were hundreds of years ago when the first American colonies began adopting the statutes. While some of the processes of keeping records may have become dated, the *law itself* has not. Society needs an authoritative, transparent source of information on who owns land in order to protect property rights, encourage commerce, expose fraud, and avoid disputes. Recent case law is beginning to show gathering judicial skepticism regarding the privatized record keeping system that is displacing public county systems.

Apologists for MERS argue that so long as MERS' name is recorded in county records as a lien holder, prospective purchasers will be on notice that they must inquire further before lending against or buying the land. But who exactly are these purchasers to consult? MERS has maintained a toll free phone number where homeowners are allowed to inquire who holds the servicing rights to their mortgage.[40] But, as the recent "robo-signer" stories and examples of wrongful foreclosures in the press have shown, servicers themselves do not always have accurate records of their own. And even if they did, talking to mortgage servicing company customer service representatives, whose business incentives focus on cutting costs, is often unproductive, slow, and unreliable.[41] Moreover, in recent years mortgage servicing and origination companies have frequently become insolvent. Even federally insured

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36. *Id.* at 36.

37. GARRY WILLS, LINCOLN AT GETTYSBURG: THE WORDS THAT REMADE AMERICA 145 (1992).

38. Arnold, *supra* note 34, at 1.

[39] Welcome to MERS, www.mersinc.org (last visited Sept. 17, 2010).

[40] Welcome to MERS for Homeowners, http://www.mersinc.org/homeowners/index.aspx#3 (last visited Sept. 17, 2010) (the current phone number is 888-679-6377).

[41] *See* Kathreine M. Porter, *Misbehavior and Mistake in Bankruptcy Mortgage Claims,* 87 TEX. L. REV. 121 (2008).

banks have been collapsing by the hundreds.[42] After seeing loan after loan in her court room with incomplete documentation and incoherent transactional records, Judge Jennifer Bailey, a Circuit Court Judge in Miami recently stated:

> [T]here are 60,000 foreclosures filed last year. Every single one of them— . . . almost every single one of them—represents a situation where the bank's position is constantly shifting and changing because they don't know what the Sam Hill is going on in their files.[43]

That MERS maintains a database of servicing rights simply does not provide a commercially reliable, authoritative source of lien information because servicers, who are in business to make profit through providing financial services, do not have an incentive to maintain permanent, transparent, publically available records of mortgage ownership.

MERS also does not reliably track beneficial ownership rights of the mortgages registered on its system. Recall that MERS only maintains a database which its members can enter information upon if they want to.[44] When the beneficial ownership interest in a loan changes hands, such as through negotiation of a promissory note and a written assignment of the mortgage, the parties to that transaction can send an electronic message to MERS updating a field of information in the database. MERS calls this process an "electronic handshake."[45] But, unlike most county real property recorders, MERS does not keep digital or hard copies of documents that embody the agreement—making it much more difficult to track fraud and errors through the record keeping system. Even more troubling, MERS members are not legally bound to update this information on the database. In the words of the MERS' CEO, the system "is capable of being used to track [beneficial ownership interests] if the members utilize it for that reason."[46] But, if the MERS members choose not to use the database to reveal themselves, MERS does not investigate further or otherwise insist that members actually use this feature of the database. Instead, MERS leaves this to the "business model" of the financial institution.[47] When asked whether MERS expects financial institutions to update the MERS database regarding changes in loan ownership, the company's CEO replied, "not so much. . . ."[48] Moreover, MERS does not keep track of what entity is in physical possession of the promissory note. Because the mortgage follows the note, the MERS system does not reveal who true current owner of the mortgage is.

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[42] Over 250 banks have failed since 2008. Federal Deposit Insurance Corporation, Failed Banks List, available at: http://www.fdic.gov/bank/individual/failed/banklist.html (Sept. 17, 2010).

[43] HSBC Bank USA, NA as Trustee for Monura Asset Acceptance Corporation, Mortgage Pass-Through Certificates Series 2006-ARI v Eslava, Hearing Transcript on Order to Show Cause, No. 1-2008-CA-055313, at 5 (Fl 11th Cir. Ct., Miami-Dade County, May 6, 2010).

[44] Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 176 (hereinafter: Arnold Deposition).

[45] *Id.*

[46] Deposition of R. K. Arnold, Henderson v. MERSCORP, INC., et al., CV-08-900805.00, Circuit Court for Montgomery County Alabama, September 25, 2009, at 176 (hereinafter: Arnold Deposition) (on file with author).

[47] *Id.*

[48] The deposition transcript on this point reads:

> [Nicholas Wooten] Q: So whenever a transfer occurs of any interest, be it a beneficial interest in the promissory note or be it servicing interest, those you expect to be entered on the MERS system?
>
> [R.K. Arnold] A: It's not so much that we expect it. We operate a system that offers that capability."

Arnold Deposition at 178.

In a laudable, but ultimately anemic effort to respond to mounting criticism of the system's lack of transparency, MERS recently announced a new feature of its internet web page servicer identification system that allows borrowers to inquire as to the identity of a loan's investor. [49] However, the company's press release is somewhat misleading in that for securitized mortgages, MERS appears to only reveal the name of the securitization trustee, rather than the trust that is the true beneficial owner of most securitized loans. Private correspondence from MERS' communications manager explains that "the MERS® System only has the name of the trustee in the Investor field and does not capture information about the trust."[50] Learning the name of a borrower's securitization trustee does not allow the borrower to research the pooling and servicing agreement that controls a servicer's or trustee's authority to negotiate loan modifications. It also does not identify the name of the trust that could be held liable for purchasing loans that violate the Home Ownership and Equity Protection Act or other state predatory lending laws.[51] Even when the name of a securitization trustee is provided, unlike a search of the public recording system—a MERS search result is not a legally authoritative search upon which a searcher is entitled to rely in ruling out the possibility of other potential purchasers that could achieve priority in an ownership dispute under the state's land title statute. Rather it is simply a query to see whether any companies happened to have used an essentially optional "electronic handshake" to enter assignment information on a private database.

Furthermore, the MERS servicer identification system often does not produce any information on beneficial ownership of loans at all, instead giving the message: "Investor: This investor has chosen not to display their information. For assistance, please contact the servicer."[52] Note that this sentence is ambiguous as to whether MERS does not know who owns the loan or the owner of the loan actually refuses to be identified. The former is disturbing in that it illustrates that we as a society no longer have a record keeping system that actually tracks legally recognized ownership interest in land back to a root of title. The latter is disturbing because it reveals how the MERS system has abated an important legal incentive to provide public notice of land ownership interests.

Both updating the MERS database and publically recording a mortgage assignment are permissive choices for financial institutions. But, a key difference is that the public system was backed by strong legal incentives to encourage financiers to provide notice of assignments. In contrast, the MERS system—designed by and operated for the exclusive benefit of mortgage finance companies—deliberately undermines and altogether lacks that incentive. Under the still current (but presently circumvented) law of all fifty states, the owner of an interest in land may intentionally conceal herself, but does so at the risk of losing that ownership interest. In both notice and race-notice jurisdictions, if a mortgage assignee fails to record, and the assignor either intentionally or unintentionally assigns the same mortgage to a second, subsequent assignee who does record, then first assignee will lose

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[49] Press Release, MERS Expands Website To Disclose Loan Investor Information, http://www.mersinc.org/newsroom/press_details.aspx?id=241 (July 16, 2010).
[50] Electronic Mail of Karmel Lejarde, MERSCORP, Inc. Communications Manager, Sept. 3, 3010, (copy on file with author).
[51] *See* Christopher L. Peterson, *Predatory Structured Finance*, 28 CARDOZO L. REV. 2185, 233-46 (2007) (summarizing mortgage loan assignee liability law).
[52] MERS Servicer Identification System Search for Servicer Information Search Results, September 6, 2010 (results available on file with author).

priority.[53] Where both assignees are using the MERS system, the only official recorded notice would be the original mortgage in the name of MERS. The MERS database may simply have no information on whether any assignments have taken place—leaving prospective investors (and courts adjudicating the conflicts that will develop) to speculate on who actually owned rights in the property. There is currently no legal penalty for failing to update the MERS database on changes in loan ownership that would incentivize financiers to avoid this situation. Because many mortgage companies in the boom years planned to sell their loans to investors, they focused on the short term commissions and profits from originating loans. They, quite frankly, did not bother with documentation that would preserve our national legacy of certainty in property rights. As a result, the MERS database does not provide reliable, authoritative information on legally cognizable beneficial ownership of loans registered in its system. County real property records that hold only a reference to the MERS system now have a systemic break in chains of title. Perhaps this is what MERS means by its corporate slogan: "Process Loans, Not Paperwork."[54]

The full risk of confusion and litigation from this system will not be known for years to come. But, the appellate courts that have been critical of the MERS system foretell further long term uncertainty surrounding property rights connected to MERS claims of ownership. For example, recognizing the implications of their own decision in *Landmark National Bank v. Kesler*, the Kansas Supreme court pointed out that "[i]n attempting to circumvent the statutory registration requirement for notice, MERS creates a system in which the public has no notice of who holds the obligation on a mortgage."[55] The Arkansas Supreme court went even further stating that "[p]ermiting an agent such as MERS purports to be to step in and act without a recorded lender directing its action would ***wreak havoc on notice in this state***."[56] And yet, that is precisely what the MERS system is designed to do. In the prototypical MERS as original mortgagee transactions *there are no recorded lenders.* [57] MERS is designed to be the cradle-to-grave notice proxy for all the half-dozen or so financial institutions and shell companies that hold title to the loan at different times—yet remain undocumented both in the public record and often on MERS' own database. We must recognize that our heritage of legal certainty in property rights created by the interaction of public recording systems and land title statutes is an important national economic resource that has been depleted by the MERS system.

V. MERS was a Contributing Factor in the Foreclosure Crisis and has Made Resolving Foreclosures More Difficult

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[53] *See* 66 Am. Jur. 2d *Records and Recording Laws* § 162 (2010). *See, e.g.,* Second Nat. Bank of New Haven v. Dyer, 184 A. 386, 388-89 (Conn. 1936) ("That an assignment of a mortgage falls within the purview of the recording statute follows from the nature of such an instrument. . . . indeed to hold otherwise would make a serious inroad upon the policy of this state that purchasers of interests in real estate are entitled to rely upon the land records as disclosing the true title. . . .").

[54] *See* Welcome to MERS, www.mersinc.org (last visited Sept. 17, 2010).

[55] Landmark Nat. Bank v. Kesler, 216 P.3d 158,168 (Kan. 2009).

[56] Mortgage Elec. Registration System, Inc. v. Southwest Homes of Arkansas, 2009 Ark. 152, 301 S.W.3d 1 (Ark. 2009) (emphasis added).

[57] Some county recorders track the originating lender's name in addition to MERS' name when a mortgage is first recorded. But, once the mortgage is assigned, the name of the original lender is no longer useful and leads to a dead end in searching for actual ownership interest in the land.

While there is plenty of blame to go around, the MERS recording and foreclosure system was an additional contributing cause of the American mortgage foreclosure crisis. MERS facilitates "predatory structured finance"[58] by decreasing the exit costs of originators. As investment banks, hedge funds, institutional investors, and the credit rating agencies weighed the risks of dumping billions upon billions of dollars into mortgage securities drawn out of the balance sheets of thinly capitalized, bankruptcy-prone mortgage lenders, MERS provided an important additional inducement. In previous research, I have argued that in the run-up to the foreclosure crisis, mortgage origination companies were used as disposable liability filters.[59] When thinly capitalized originators churned out more and more securitized loans, claims against those lenders accumulated, while their assets did not.[60] Once the projected costs of disgruntled investor recourse demands and borrower predatory lending lawsuits exceeded the projected costs of bankruptcy and reformation under a new corporate guise, originator management would predictably discard their corporate identity.[61] MERS made this easier by offering a *super-generic placeholder* that transcended the aborted life of lenders. MERS reassured investors that even when an originator goes bankrupt, county property records would remain unaffected and foreclosure could proceed apace. By serving as the true mortgagee's proxy in recording and foreclosure, MERS abetted a fly-by-night, pump-and-dump, no-accountability model of structured mortgage finance.

Moreover, the use of MERS's corporate identity facilitates separation of foreclosure actions and litigation of predatory lending and servicing claims. When MERS (or more accurately servicers or foreclosure specialists acting in MERS's name) brings foreclosure actions, it justifies this entitlement based on a claim of legal ownership of mortgage liens. But when borrowers attempt to assert counterclaims challenging the legality of mortgage brokers, lenders, trusts, or servicers, MERS hides behind its claim of nominee status. One former mortgage lender has estimated that in the mid-2000s approximately 70% of brokered loan applications submitted to mortgage lenders involved some form of broker encouraged fraud.[62] Similarly, Professor Porter's study of mortgage loans in Chapter 13 bankruptcy found that residential mortgage creditors did not supply a promissory note in 41.1% of cases involving a home mortgage.[63] Because promissory notes are not supplied, nor where MERS is involved, is the actual identity of the note holder revealed, consumers and their counsel can verify neither the identity of the parties involved, nor even the amount of the debt in question. In an ordinary foreclosure, using MERS's name erects a tactical barrier to judicial resolution of these types of problems. MERS confuses and pacifies borrowers (and sometimes courts) at precisely the crucial moment: on the eve of foreclosure. Once a family looses their home, their leverage and appetite for litigation dissipate. The separation of predatory lending litigation from foreclosure litigation facilitated by bringing foreclosure in MERS's name decreases the costs of foreclosure and dulls the deterrent force of consumer protection law. MERS represents the mortgage finance industry's best effort to create a single, national foreclosure plaintiff that always has foreclosure standing, but never has foreclosure accountability.

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[58] Christopher L. Peterson, *Predatory Structured Finance,* 28 CARDOZO L. REV. 2185 (available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=929118).
59. *Id.*, at 2275.
60. *Id.*
61. *Id.*
62. RICHARD BITNER, CONFESSIONS OF A SUBPRIME LENDER: AN INSIDER'S TALE OF GREED, FRAUD, AND IGNORANCE 45 (2008).
63. Katherine Porter, *Misbehavior and Mistake in Bankruptcy Mortgage Claims*, 87 TEX. L. REV. 121, 147 (2008).

Obviously MERS is not responsible for failings in the monetary and/or regulatory policy of the Federal Reserve Board.[64] The President and Congress could have intervened in the troubling trends toward unrealistic mortgage loans.[65] Mortgage brokers and lenders systematically strove for volume and commissions, rather than sustainable home ownership.[66] Federal banking regulators obstructed the efforts of state legislators and attorneys general to bring the market to heel.[67] The credit rating agencies rashly gave their seal of approval to the risky, complex, packaged and repackaged mortgage loan securities.[68] While MERS may have reassured investors of the viability of churned residential mortgage backed securities, it had little to do with the over-leveraging of hedge funds, bond insurers, or the government sponsored housing enterprises.[69] Recognizing MERS's role in facilitating the foreclosure crisis is not to ignore nor excuse these other causal factors. Nevertheless, it is a mistake to list the contributing factors associated with the crisis and omit MERS.

VI. Solutions

A. Congress Should Bar the Federal Housing Entities From Purchasing Loans Recorded in MERS' Name.

By allowing Fannie Mae, Freddie Mac, and Ginnie Mae to purchase MERS-recorded loans the federal government has inadvertently undermined sensible state land title laws and consumer protection. Moreover, irrespective of one's views of the benefits or disadvantages of MERS, the simple fact is that the system still faces significant costly legal uncertainty. Going forward Congress should bar the GSEs from digging the hole they are in deeper. Now that the risks of the MERS system are clear, it is time to require the GSEs to simply go back to the traditional system that they lived with since the Great Depression. Absent Congressional action, counsel for financial institutions, federal and state housing agencies, and title insurance companies need to take a candid, reflective look at the implications of mortgage bankers' efforts to usurp government control of real property records. Even those who prefer minimalist government must recognize that in a democratic republic divestment of this responsibility from government to industry should have occurred with the consent of elected representatives of the people. In this case, the early involvement of Fannie Mae and Freddie Mac—federally sponsored corporations that do deserve respect for their efforts to facilitate American homeownership –did not dispense with the sovereign right of state governments to control their own real property recording law. Laws for the states are made by the states, not by Government Sponsored Enterprises. Fannie Mae and

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64. Paul Krugman, *How Did Economists Get It So Wrong?*, N.Y. TIMES, Sept. 6, 2009, at MM36.
65. Jo Becker et al., *White House Philosophy Stoked Mortgage Bonfire,* N.Y. TIMES, Dec. 21, 2008, at A1.
66. BITNER, *supra* note 62, at 181–82.
67. Christopher L. Peterson, *Federalism and Predatory Lending: Unmasking the Deregulatory Agenda*, 78 TEMPLE L. REV. 1, 96–97 (2005); Christopher L. Peterson, *Preemption, Agency Cost Theory, and Predatory Lending by Banking Agents: Are Federal Regulators Biting Off More Than They Can Chew?*, 56 AM. U. L. REV. 515, 549–551 (2007).
68. Steven L. Schwarcz, *Understanding the Subprime Financial Crisis,* 60 S.C. L. REV. 549, 550–52 (2009).
69. Frederick Tung, *The Great Bailout of 2008–09,* 25 EMORY BANKR. DEV. J. 333, 336 (2009); Binyamin Appelbaum, et al., *How Washington Failed to Rein in Fannie, Freddie*, WASH. POST., Sept. 14, 2008, at A1.

Freddie Mac could take a step toward restoring national trust by stepping away from the MERS system and requiring traditional recording practices in qualified loans. With their many critics in Congress the last thing the GSEs need is to take on *more* political and legal risks associated with MERS. Paying recording fees on mortgage assignments is a wise legal and political investment.

Congress should also resist the temptation intervene in State real property law with a MERS "whitewash" bill that covers over the basic legal problems associated with the MERS system. Congress is only likely to make matters worse if it attempts to insert a small, inert pocket of preempted federal law for MERS within the fabric of the existing state commercial and property laws that include Article 3 and 9 of the Uniform Commercial Code, the state Land Title statutes, and state foreclosure laws. A whitewash bill is likely to have unforeseeable unintended consequences on state law. Moreover, the public is likely to resent such legislation as "legal bailout" designed to make it easier for a Wall Street-backed shell company to take homes away from families during a recession.

B. Congress Should Investigate Ways to Help States and Localities Improve the Efficiency and Uniformity of County Recording Systems

While land title law is and should remain a state and local issue, this is not to say that the federal government could not exert a positive influence by facilitating better and more uniform technology in county recording offices. Instead of allowing our democratically maintained real property records to be privitazed, Congress should do the hard work of supporting improvements in the infrastructure homeowners and industry rely upon for commerce in land. Congress could exercise real leadership by providing block grants to county governments to upgrade their recording technology in exchange for adopting uniform standards that help title insurance companies and mortgage finance companies more easily record and search the existing systems. Moreover, Congress could take one of the best features of the MERS system, its unique mortgage loan identification numbers, and instruct the HUD to make available federal unique identification numbers that could in turn be used by county recording systems and mortgage loan servicers alike in facilitating better record keeping.

Congress could task the GAO or HUD to produce recommendations on how to modernize the public county recording system. Alternatively, individual Congressional leaders could use their connections and persuasive authority to call upon the American Law Institute and the National Conference of Commissioners on Uniform State Laws to draft a model state legislation that upgrades the capabilities of and promotes uniformity in county recording offices.

C. Congress should Consider Adopting a Temporary Emergency Homestead Exemption Applicable to Mortgages in Favor of Residential, Owner-Occupied Homeowners.

Looking beyond the issues surrounding MERS, Congress needs to take a fresh look at ideas to help create more meaningful incentives for servicers to modify loans and for homeowners that cannot

afford to stay in their homes to turn their properties over without protracted court battles. One exciting idea that merits further exploration would involve granting a temporary emergency homestead exemption applicable to mortgage loans in favor of owner-occupied borrowers.

In centuries past when the typical American family lived as subsistence farmers each household maintained a supply of seed grain. Living from harvest to harvest, the first portion of each crop went to replenish the supply of seed used to plant next season. One reason the finance crisis has been so terribly destructive is that it has wiped out the twenty-first century equivalent of middle class seed grain for millions of families.

Today, the typical American family gets by living from paycheck to paycheck. Although we do not generally use our homes to grow food, they are nevertheless one of our most productive resources. Homes are the indispensible base from which we enter the labor force. It is nearly impossible to be employed without a place to stay clean, feed ourselves, and rest. This is an important reason that so many families are fighting foreclosures tooth and nail—with the unintended consequences of delaying the reset in housing prices, casting legal uncertainty over financial markets, and suppressing demand for housing.

Families facing foreclosure need seed grain: cash to cover moving expenses, a deposit and first month's rent on a residential lease, or even a down payment on a less expensive home purchased with a new low, fixed interest rate mortgage. State legislatures—or even Congress—could help restart the housing market with a simple legal change that would not cost tax payers a dime. The government should pass emergency legislation providing that the first $15,000 from an owner occupied residential foreclosure sale must go to the departing family. In effect the proposal would act as a first priority "seed lien" in favor of the family.

While this concept is new, it is not unprecedented. Environmental law creates similar liens to cover the cost of cleaning up toxic waste. And the homestead laws of many states already exempt some of the value of a family's home from unsecured creditors, such as credit card companies. This emergency homestead exemption would do the same thing—albeit likely exempting less value—in the case of home mortgages loans. Plus, the law would only expand and solidify expectations surrounding the informal "cash-for-keys" polices the smartest lenders have used for generations. These lenders provided a modest amount of cash to the family in exchange for voluntarily turning over a foreclosed home in good condition. Congrees could make the law temporary with a sunset provision

These emergency laws would dramatically improve the housing market in several ways. First, cash from the proceeds of a foreclosure could convince many defaulting borrowers to turn over their homes without a fight. Many economists believe that the economy cannot turn around until the glut of foreclosures work their way through the system. Leaving fifteen thousand dollars for the family at the finish line would put fuel injectors on this process. Since so many mortgage companies cannot seem to find the records needed to foreclose, the value of cooperation from borrowers in cutting through the red tape should not be underestimated.

Second, an emergency homestead exemption on mortgages would create a stronger financial incentive for the mortgage industry to refinance delinquent loans. If the servicer knows that investors would be facing the automatic loss of fifteen thousand dollars after the foreclosure, it makes even more sense to cover the relatively modest price of underwriting a new mortgage up front.

While it is true that investors will bear the cost of this "seed lien," they may be facing these losses anyway. As it stands, millions of families are digging their heels in forcing lenders to spend thousands of dollars on attorneys' fees and dredging up lost records. We would all be better off if this money were just turned over to the families that need it instead of burned on lawyers in scorched earth legal battles.

But perhaps most importantly, mandating that each owner-occupied resident owns at least fifteen thousand dollars of liquid home equity would give families the seed grain they need to make a fresh start. As a society we simply cannot allow more families to fall into homelessness and despair. People that invested their dreams and life savings in a family home need to be able to take *something* away from the ashes of foreclosure.

In conclusion, thank you for work on behalf of American citizens in working to resolve these complex and important national problems.