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Boston Bar Journal

A Peer Reviewed Publication of the Boston Bar Association

Eaton v. Federal National Mortgage Association: Additional Burdens Provide Little Consumer Benefit

Posted: December 19, 2012 | **Author:** bbabarjournal | **Filed under:** Point/Counterpoint, Winter 2013, Vol. 57, #1 | **Tags:** Carpenter v. Longan, Diane C. Tillotson, Eaton v. Federal National Mortgage Association, Foreclosure, Legal Title, Mortgage assignment, Mortgage Modification, N.A. v. Ibanez, Predatory Lending, Richard A. Oetheimer, Sub-prime lending, U.S. Bank |1 Comment

By Richard A. Oetheimer and Diane C. Tillotson

Counterpoint

From the perspective of conveyancing attorneys and national mortgage lenders and servicers, the recent foreclosure decisions from the Massachusetts Supreme Judicial Court ("SJC") have been surprising and a bit puzzling. Surprising that in such a seemingly settled area of the law the standard foreclosure practices of Massachusetts counsel, in reliance on local title standards, would be found not to conform to state law. Puzzling because the decisions neither address nor resolve the root of the problems underlying the litigation. The decisions have also highlighted some relatively unique aspects of Massachusetts mortgage law.

In many if not most American jurisdictions, the mortgage is mere security for the note and follows the note as a matter of law. *See Carpenter v. Longan*, 83 U.S. 271 (1872). Although Massachusetts has recognized this principle, by holding that the mortgagee holds the mortgage in trust for the note holder, who is the beneficial owner of the mortgage, the SJC's decision in *U.S. Bank, N.A. v. Ibanez*, 458 Mass. 637 (2011) held that only the mortgagee can foreclose and that a note holder requires an assignment of the mortgage to do so. In *Eaton v. Federal National Mortgage Association*, 462 Mass. 569 (2012), the SJC held that, prospectively, a mortgagee must either hold the note or be the authorized agent of the note holder in order to foreclose. Because, as a matter of practice, notes have never been recorded in Massachusetts, retroactive application of this holding would have produced disastrous results as it would have been

impossible to determine the validity of any foreclosure of record. Prospective application of this rule, while manageable, places additional burdens on the lenders and conveyancers but does little to address the underlying consumer issues.

Eaton, Ibanez and *Bevilacqua v. Rodriguez*, 460 Mass. 762 (2011), share a common ancestry: each case arises from efforts by a party grappling with the consequences of the plummeting value of real estate during the recent economic downturn. In *Ibanez*, the central player was a bank foreclosing without a valid assignment of the mortgage at the time of the foreclosure. *Bevilacqua* involved a purchaser for value after a foreclosure sale looking to establish good title in light of *Ibanez*, and in *Eaton*, a homeowner sought to defend against eviction and stay in her home. While each of these cases continues to have a significant impact on foreclosure practice in Massachusetts, the "deficiencies" addressed by the SJC in those cases were not at the root of financial problems faced by the parties and the Court's decisions do little to resolve those issues. Recognizing that the Court can decide only the issues in the litigation before it, it is nonetheless unsettling that the loss to the consumer parties would have occurred regardless whether the assignment in *Ibanez* was timely delivered and/or recorded or whether the note in *Eaton* was held by the foreclosing mortgagee.

The fact pattern underlying *Eaton* is not uncommon. In 2007, Henrietta Eaton refinanced the mortgage on her home in the Roslindale section of Boston, executing a promissory note and mortgage in favor of BankUnited, FSB. Although BankUnited was identified as the lender in the mortgage, Mortgage Electronic Registration System, Inc. ("MERS") was named as mortgagee and as a result became the holder of legal title with the power of sale as nominee of BankUnited or its assignee. The mortgage gave MERS the right to foreclose and sell the property. Two years later, MERS assigned its interest in the mortgage to Green Tree Servicing, LLC ("Green Tree") and when Eaton failed to make payments on the note, Green Tree foreclosed and was the highest bidder at the sale. Shortly thereafter, Green Tree assigned its rights to Fannie Mae which commenced a summary process action to evict Eaton from her home in early 2010.

Eaton defended the summary process action with a counterclaim asserting that the foreclosure was void because Green Tree did not hold the note at the time of the foreclosure. The Housing Court stayed the foreclosure proceeding to give Eaton the opportunity to seek relief in the Superior Court, the Supreme Judicial Court having not yet decided *Bank of New York v. Bailey*, 460 Mass. 327, 333-34 (2011), where it determined that the Housing Court had jurisdiction to adjudicate counterclaims alleging invalid foreclosure sales in summary process actions. Notably, while Eaton raised claims concerning the validity of the foreclosure, she never disputed that the arrearages were owed or claimed that the note had been paid. The Superior Court agreed with Eaton that the foreclosure sale was invalid. The SJC interpreted G.L. c. 244, § 14 to require a foreclosing "mortgagee" to be either the note holder or the authorized agent of the note holder, and remanded *Eaton* for further proceedings on the agency question. Responding to pleas from the conveyancing and lending bar, the Court, noting that "significant difficulties in ascertaining the validity of a particular title" would arise if its holding was not limited to prospective operation, limited its *Eaton* holding to mortgage foreclosures for which the notice of sale was given after June 22, 2012, the date of the opinion.

As noted above, the effect of the *Ibanez* and *Eaton* decisions is to introduce an element of uncertainty to legal titles. Massachusetts is a "title theory" of mortgages state where the granting of a mortgage vests legal title in the mortgagee regardless of the note holder's identity. While payment of the underlying debt would certainly be a defense to foreclosure, as noted below, there is nothing to suggest that this is a problem. In addition, *Eaton* raises a question concerning those situations where a mortgage is used as security for something other than a debt, for example, as security for the performance of obligations

under a settlement agreement. While this concern is not relevant in the consumer context, *Eaton* is not limited to consumer transactions. The Court in *Eaton* did avoid some of the adverse effects of its earlier *Ibanez* ruling by giving its decision only prospective effect. For this reason, any concern that *Eaton* does not resolve "foreclosures in the pipeline" is misplaced; the date of publication of the notice is the touchstone (just as in *Ibanez*). So long as the notice issued prior to the opinion, no relationship to the note need be shown. *See e.g.; McKenna v. Wells Fargo Bank*, 693 F.3d 207 (1st Cir. 2012).

Legislative response to *Eaton* was swift and in the summer of 2012, the General Court amended G.L., c. 244, § 14 and added §§ 35(B) and 35(C). The amendments, effective November 1, 2012, provide a solution for dealing with the impacts of *Eaton* for residential mortgages (and residential foreclosures) of one to four-family dwellings. Prior to the notice of foreclosure sale, the creditor/foreclosing mortgagee must certify compliance with the *Eaton* requirements and the certification must be based on a review of the creditor's business records and provides "conclusive evidence in favor of an arms-length third-party purchaser for value, at or subsequent to the resulting foreclosure sale" that the requirements have been met. Lenders may not pass on the cost of preparing these affidavits or any curative actions taken in response to *Eaton* to third parties. The Real Estate Bar Association of Massachusetts ("REBA") has recently promulgated a form of affidavit meeting the requirements of Section 35(C).

The legislative response, while welcome, did not resolve all open issues. For example, the four-month gap relating to notices published between the June 22, 2012 date of decision and the November 1, 2012 effective date is not addressed, nor are mortgages related to commercial or other properties or large residential complexes. Presumably, affidavits meeting the requirements of Section 35(C) coupled with documentary evidence sufficient to satisfy the title insurance industry will satisfy the conveyancing bar's need for the requisite certainty in certifying titles, albeit without the protection provided by Section 35(C) for residential properties. Conveyancers will need to ensure that the affidavits are executed by persons with appropriate authority and are duly recorded with the foreclosure documents. Certifying title to any property with a foreclosure in the chain of title will impose added burdens on the lender and conveyancing attorney and create additional caseload for the state's housing courts as the "*Eaton* or *Ibanez* defense" will likely be raised in numerous summary process actions.

Whether they are right or wrong in their construction of Chapter 244, as a matter of public policy were the Court's decisions necessary or advisable? Did the problems identified in those cases need to be addressed? Consumer law advocates have argued that securitization of loans resulted in fragmentation of interests that makes it impossible for a mortgagor to challenge authority to foreclose or to seek relief from the mortgage debt. But this argument does not withstand scrutiny.

What consumer law advocates are really lamenting is the institutionalization of the mortgage market in recent decades. For most borrowers, the era of calling George Bailey at the neighborhood Building & Loan to work out their financial difficulties is long past. These market forces were in place with the rise of the secondary mortgage market long before securitization.

When mortgages are securitized, the identity of the trustee, who holds the notes in a pool for the benefit of the certificate holders (the investors) is of little to no practical benefit to borrowers. Under the contractual documents governing the securitization, responsibility for the relationship with borrowers resides in the loan servicers. Federal law in the form of the RESPA statute, 12 U.S.C. §§ 2601 *et seq*., ensures that borrowers know who is servicing their loan, and where they are to send their loan payments. Generally it is the servicer who controls the foreclosure decision and process.

Some consumer advocates view it as problematic that the legal and equitable ownership and foreclosing authority are not united in a single party. But has this posed a real-world problem? Have borrowers

been foreclosed who were not genuinely in default? No one is suggesting any pattern of this; in *Ibanez*,Justice Cordy's concurrence noted there was no dispute that the mortgagors were in default and subject to foreclosure. Is there any evidence of strangers to the mortgage debt foreclosing? Again, no: in *Ibanez* the plaintiffs were the securitization trusts; and in *Eaton* it was the mortgage servicer. Have any mortgagors had creditors make competing claims to their loan debt? Once again, the answer is no; there is no evidence anyone has paid or been called upon to pay twice due to securitization.

In sum, the Court's recent decisions have had the consequence of causing confusion in the marketplace, slowing the foreclosure process and complicating resale of properties. Questions of affixing blame for the sharp decline in housing prices and the resulting increase in foreclosures aside, it is natural to feel empathy for those at risk of losing their homes, and understandable to want to help them. Recent Massachusetts legislation is designed to do so by affording opportunities to certain borrowers to be considered for loan modifications. But at the same time there is a consensus among experts that an efficient foreclosure process is also a necessary component of stabilizing housing prices. It is hoped that the recent legislation passed in response to *Ibanez* and *Eaton* will have the effect of providing what the SJC in *Bevilacqua* believed it could not: good title to innocent third-party purchasers.

Richard A. Oetheimer is a partner at Goodwin Procter LLP. He participated as Amicus in Eaton on behalf of the Mortgage Bankers Association, and has represented mortgage lenders and servicers in foreclosure-related litigation. The views expressed herein are his own and not the views or positions of his clients.

Diane C. Tillotson is a partner at Hemenway & Barnes LLP who specializes in real estate permitting and litigation. She is a former President of both the Real Estate Bar Association and the Abstract Club and participated in the submission of the Amicus brief in Eaton filed on behalf of those associations. The views expressed herein are her own.

One Comment on "Eaton v. Federal National Mortgage Association: Additional Burdens Provide Little Consumer Benefit"

1. *Professional immigration lawyers* says:
   January 25, 2014 at 10:25 am
   This is a great explanation between Eaton and federal national mortgage association. I enjoyed reading it.

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