The First Circuit Strikes Again in Culhane v. Aurora Servicing! Grants Borrowers Legal Standing To Challenge Mortgage Assignments, But Upholds MERS System

We introduce this subject with a riddle: What entity is not a bank but claims to hold title to approximately half of all the mortgaged homes in the country? The answer is MERS. –
Circuit Judge Bruce Seyla

For the second time in a week, the U.S. Court of Appeals for the First Circuit has issued a major foreclosure opinion, this one in ***Culhane v. Aurora Loan Servicing of Nebraska***, No. 12-1285 (click to download opinion). Writing for a distinguished panel which included retired U.S. Supreme Court Justice David Souter, Circuit Judge Bruce Seyla held that the MERS (Mortgage Electronic Registration System, Inc.) regime passes legal muster, but — overruling numerous lower court decisions to the contrary — gave borrowers the right to challenge mortgage assignments in the wrongful foreclosure setting. In my opinion, the net effect of this decision will put to rest the ubiquitous challenges to the MERS system in Massachusetts, yet could result in a slight uptick in foreclosure challenges by blessing borrowers with much sought after legal standing to challenge faulty mortgage assignments.

This opinion is a must read. Judge Seyla is well known for his linguistic talents. Make sure you get out your dictionaries — Judge Seyla likes big words.

MERS — Mortgage Electronic Registration System, Inc.

For those who have not read our prior posts on MERS, it is an electronic registry of mortgages created by lenders in the 1990's in order to facilitate the securitization and sale of mortgage back securities on Wall Street. Basically, when mortgages are bought and sold by various investors and lenders, MERS documents the transfers in its electronic database. However, historically the MERS-assisted transfers were not recorded through mortgage assignments in the state registries of deeds, a practice subject to much criticism. As for who "owns" the actual mortgage — another issue subject to much criticism and litigation — MERS claims that it acts solely as a "nominee" for the actual lender and holds only bare legal title to the mortgage as the mortgage holder of record.

When a loan go into default status and into foreclosure, MERS would, as in the *Culhane* case, facilitate the execution of a mortgage assignment to the current loan servicer, Aurora Servicing in this case. In another much criticized practice, one person wearing "two hats" would often execute these mortgage assignments. For the Culhane loan, an Aurora employee who was also a MERS "certifying officer" executed the assignment transferring the mortgage from MERS to Aurora. Ms. Culhane challenged this practice in her lawsuit seeking to void the foreclosure conducted by Aurora.

Borrower Has Legal Standing To Challenge Mortgage Assignments In Certain Cases

In a question of first impression in the First Circuit, the court considered whether borrowers have standing to challenge a MERS-initiated mortgage assignment even though a borrower is not a party to it. Overruling a significant number of cases around the country, the panel held that borrowers do have legal standing to challenge assignments as "invalid, ineffective, or void (if, say, the assignor had nothing to assign or had no authority to make an assignment to a particular assignee)." Judge Seyla adopted some common-sense reasoning, noting that under Massachusetts' non-judicial foreclosure system, borrowers would be effectively left without

a remedy to challenge a faulty foreclosure without giving them standing to contest a defective mortgage assignment.

MERS System Is Legal And Borrower Ultimately Loses

Ms. Culhane's victory as this point unfortunately became Pyrrhic. Although the court held that borrowers could challenge mortgage assignments going forward, it did Ms. Culhane no good because she could not muster an adequate challenge to the MERS-Aurora mortgage assignment in her case. The court rejected Culhane's argument that MERS did not legally hold the mortgage so it could not assign it, reasoning that nothing in Massachusetts mortgage law prohibited splitting the note and mortgage as the MERS system does. The court also found no legal problem with the same person signing on behalf of both MERS and Aurora.

Not The Last Word…

Culhane, however, may not be the last word on MERS and foreclosures in Massachusetts, as the Supreme Judicial Court always has the last and final say on these matters. Coincidentally, this week the SJC announced that it was soliciting friend-of-the-court briefs in *Galiastro v. MERS,* on whether MERS "has standing to pursue a foreclosure in its own right as a named 'mortgagee' with ability to act limited solely as a 'nominee' and without any ownership interest or rights in the promissory note associated with the mortgage; whether the prospective mandate of *Eaton v. Federal National Mortgage Association*, 462 Mass. 569 (2012), applies to cases that were pending on appeal at the time that case was decided." The *Galiastro* case is scheduled for argument in April 2013.

As always, I'll be on top of the latest developments in this ever-fluid area of law. Now, it's time to eat those bagels and lox I've been waiting for.

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Link: Culhane v. Aurora Loan Servicing (1st Cir. Feb. 15. 2013)