

Legal Update

January 7, 2011

Supreme Judicial Court of Massachusetts Rules Foreclosure Did Not Provide Title Where Foreclosing Party Can't Prove Ownership

The Supreme Judicial Court of Massachusetts has ruled that a foreclosure may be deemed invalid if the foreclosing bank or company can't prove the chain of title, called assignments, providing it ownership of the loan or authority to act for a party who owns the loan.

The case is *U.S. Bank National Association v. Ibanez*, Massachusetts Supreme Judicial Court No. SJC-10894 (January 7, 2011).

This case involves a complicated the sale, transfer, and packaging of a loan. The complexity of the chain of ownership is truly astounding. Rose Mortgage, Inc. provided the loan on the house and recorded the mortgage the day after the sale (December 1, 2005). The story gets good from here.

"Several days later, Rose Mortgage executed an assignment of this mortgage in blank, that is, an assignment that did not specify the name of the assignee. The blank space in the assignment was at some point stamped with the name of Option One Mortgage Corporation (Option One) as the assignee, and that assignment was recorded on June 7, 2006. Before the recording, on January 23, 2006, Option One executed an assignment of the mortgage in blank."

Let's go over that in plain English. An assignment of a mortgage is a sale of that mortgage to another party. Rose provided the money to purchase the house and possessed a mortgage. Several days after providing those funds, Rose assigned the mortgage to ... blank. That's right; Rose executed a legal transfer to no one. We know that another company was, after the fact, stamped into the blank space. That company, Option One, executed another assignment of the mortgage to ... blank.

"According to U.S. Bank, Option One assigned the mortgage to Lehman Brothers Bank, FSB, which assigned it to Lehman Brothers Holdings, Inc., which then assigned it to the Structured Asset Securities Corporation, which then assigned the mortgage, pooled with approximately 1,220 other mortgage loan, to U.S. Bank, as trustee for the Structured Asset Securities Corporation Mortgage Pass-Through Certificates, Series 2006-Z. With this last assignment, the loans were pooled into a trust and converted into mortgage-backed securities that can be bought and sold by investors--a process known as securitization."

The story gets better. There was absolutely no record of the transfer to U.S. Bank. Further, the U.S. Bank "Private Placement Memo" selling this securitized bundle of mortgages claimed that each mortgage in the bundle was "identified in a schedule appearing as an exhibit to the Trust Agreement." U.S. Bank was unable to find a document or schedule indicating the loan at issue was in the bundle.

Of course, U.S. Bank foreclosed on the property on July 5, 2007 as trustee for the securitization trust. Recall that U.S. Bank: (1) couldn't prove the mortgage was ever transferred to it; and, (2) couldn't find a record of the mortgage in the securitization papers issued to the public.

More than one year after the foreclosure, a company called American Home Mortgage Servicing, Inc., who allegedly purchased the loan from Option One, executed an assignment of the loan to U.S. Bank as trustee for the securitization trust. Apparently, someone realized, a year after the foreclosure, that the party foreclosing didn't have anything to do with the ownership of the loan. This was an attempt to paper over the mistakes after the fact.

Massachusetts, like many states, allows for trustee sales. Trustee sales don't require judicial oversight. The company holding the mortgage acts on its own. Recognizing the substantial power that trustee sales grant to mortgage holders, Massachusetts follows the rule that "one who sells under a power of sale must follow strictly its terms. If he fails to do so there is no valid execution of the power, and the sale is wholly void."

One of the terms that must be strictly followed is that only the actual, true, owner, or its agents and assigns, can foreclose on a property. You don't want a company to come at a homeowner "out of the blue" and assert it has the power to foreclose (and recall this is without any judicial oversight).

Judge Cordy (and note these words come from a judge on the Supreme Judicial Court, the highest court in Massachusetts) concurred (agreed) with the decision and added:

"What is surprising about these cases is ... the utter carelessness with which the plaintiff banks documented the titles to their assets.... Although there was no apparent actual unfairness here to the [homeowners], that is not the point. Foreclosure is a powerful act with significant consequences, and Massachusetts law has always required that it proceed strictly in accord with the statutes that govern it."

Analysts said the decision may also threaten banks' ability to package mortgages into securities, and may raise the specter that loans transferred improperly will need to be bought back.

"What they were doing was peddling these mortgages and leaving the paperwork behind," said Michael Pill, a partner at Green, Miles, Lipton & Fitz-Gibbon LLP in Northampton, Massachusetts, who represents homeowners and is not involved in the case.

It will be interesting to see what happens. The Massachusetts Supreme Judicial Court indicated the ruling applies retroactively. This means thousands of homeowners can sue for foreclosures done over the last three years. In this particular case, the outcome was wonderful for the homeowner. One plaintiff was simply allowed to move back into a home and another will be compensated for the price of the deed.

What are other consequences? The banks with improperly sold and securitized loans will be accused of fraud by investors and may be forced to buy back the loans, making them direct mortgage owners. In addition, the loans on the homes become unsecured. The banks can still go after homeowners who default but there is simply no security.

I sincerely hope the California Supreme Court rules as did the Massachusetts Supreme Judicial Court. If so, foreclosures will proceed more slowly as banks work to be precise in ownership. If ownership cannot be proven, foreclosures will be thrown in disarray. We are also looking at years of litigation against the banks for such sloppy work.

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