A National mortgage loan registry
My presentation covers:

• What’s wrong with the present system for documenting secondary market sales of mortgages:
  • Problems with the law
  • Practical problems in using the system
  • Problems with MERS
• What to replace the present system with?
• Draft statute
A mortgage borrower signs two documents:

- Promissory note (promising to pay back the loan)
- Mortgage (imposing a lien on the real estate as security for repayment of the loan)
What can a lender do with a mortgage loan?

• Keep it “in portfolio” and collect the interest on it. (Banks sometimes do this.)

• Sell it to another investor for cash. (Mortgage companies usually do this.)

• Securitize it (use it as collateral for the issuance of bonds). The securities may be:
  – Pass-throughs
  – Multi-class bonds
The “Secondary Mortgage Market”

• Some mortgage loans are held “in portfolio” by their originators (e.g., commercial banks)

• But a high percentage of mortgage loans is sold on the secondary market. The purchaser may hold the loans in its portfolio or securitize them:
  – The GSEs: Fannie Mae and Freddie Mac (hold some and securitize some)
  – Other investors (pension funds, savings banks, etc.) that hold the loans in their investment portfolios
  – GNMA mortgage-backed securities (federally guaranteed)
  – Securitizers (“conduits”) who use the pools of mortgages as collateral for bonds they issue (“private label mortgage-backed securities”)


Fannie, Freddie, and Private-label Securitization Shares

- Securitized by Fannie and Freddie
- Securitized by private-label issuers
- Securitized with a GNMA guarantee
- Not securitized; held in portfolio by the originator or secondary market investor.

Figure 4: Share of Total Residential Mortgage Originations

In the mid-2000s, private-label MBS became dominant:
• The secondary market investor should get:
  – The right to enforce the note
  – The right to enforce (foreclose) the mortgage
How to transfer a loan:

- **Note**: method depends on whether it is “negotiable” or not (under UCC Article 3).
  - If non-negotiable, can transfer by a separate document of assignment.
  - If negotiable, can only transfer by delivery of the original wet-ink signature document.

- **Mortgage**: transfer by a separate assignment, recorded in the real property records.
  - (Assignment is not necessary to transfer the right of foreclosure; “the mortgage follows the note.”)
Why bother executing and recording a mortgage assignment?

• To prevent the assignor from fraudulently releasing the mortgage.

• To get notice of any suit by a superior interest-holder (e.g., foreclosure of a prior mortgage, eminent domain action).

• In 10 states, nonjudicial foreclosure is permitted only if the foreclosing party has a “chain of title” of recorded assignments.
In recent years:

• Secondary market investors quit recording mortgage assignments when loans were transferred.
  – (They set up MERS to take an initial assignment, and then hold the mortgage as “nominee” for the actual holder of the note.)

• They also quit, in many cases, insisting on a transfer of the original notes.
  – The notes were often destroyed.
Problems with the law

- Two operative documents: note and mortgage
- In theory they can’t be separated, but they appear to be separated:
Problems with the Note

• Difficult to tell if it’s “negotiable” or not.
• This dictates whether UCC Art. 3 governs.
• If Art. 3 applies, the original document must be delivered to transfer the right of enforcement.
• This is extremely inconvenient
• Many notes are now “unfindable.”
• Filing a “lost note affidavit” is problematic.
Practical difficulties with transferring notes and mortgages:

- **The note:**
  - Store, track & move notes (65 million of them)
  - Make endorsements and allonges if needed.

- **The mortgage (recording an assignment):**
  - Determine appropriate recording jurisdiction
  - Determine recorder’s document standards
  - Determine recorder’s fee (depends on pages)
  - Prepare & execute assignment
  - Transmit with check for proper fee
  - Redo if incorrect.
Our system for transferring notes and mortgages was developed in the 18th century – it’s archaic!
MERS was designed to eliminate the need for recording mortgage assignments (except when foreclosing or releasing the mortgage):
MERS Problems

• No statutory foundation; does not track notes
• Courts confused by “nominee” status
• Courts confused over apparent separation of note and mortgage
• Use of non-employee corporate “officers”
• Foreclosure in the name of MERS
• Lack of transparency (identification of investors)
• Lack of accuracy of records
• Negative reputation
Overall...

• Both in legal and practical terms, the system of secondary market mortgage transfers in the US is highly confused, disfunctional and inefficient. It cries out for reform.
A National Mortgage Loan Registry

• Adoption by Act of Congress
  – Necessary to preempt state law and create a uniform national system
A National Mortgage Loan Registry

Objectives of federal preemption:
1. Make “negotiability” of promissory notes irrelevant.
   - All notes secured by mortgages would be governed by the same rules.
A National Mortgage Loan Registry

Objectives of federal preemption:

2. Eliminate the need for physical delivery of notes as a means to transfer the right of enforcement.
A National Mortgage Loan Registry

Objectives of federal preemption:
3. Eliminate the uncertainty over the nature of proof needed to foreclose a mortgage.
A National Mortgage Loan Registry

Objectives of federal preemption:

4. Eliminate arguments based on the note and mortgage being separated from one another.
A National Mortgage Loan Registry

• What is being registered?
• The UCC distinguishes between
  – “Ownership” of the note (the right to the proceeds of enforcement) and
  – “Entitlement to enforce” (the right to sue on the note or foreclose the mortgage)
• The “Person Entitled to Enforce” (“PETE”) can sue, foreclose, modify, release or discharge the note. These are the rights to be registered.
For example:

- Fannie Mae and Freddie Mac have their servicers conduct their foreclosures.
Registration vs. Recording

• **Recording** is like operating a library. People can review the documents and decide for themselves who has rights to the property.

• **Registration** is a averment by the government as to who has rights to the property:
  – Motor vehicle registration
  – The Torrens system of land titles
  – The FAA’s registry of aircraft ownership

• The proposed mortgage system would be **registration**, not recording.
A National Mortgage Loan Registry

• Only mortgages that are first recorded locally under state law could be registered.

• The local recording would establish the mortgage’s priority (as at present).
A National Mortgage Loan Registry

• Registration would be done on-line electronically, with appropriate verification of identity.
A National Mortgage Loan Registry

- The holder of the mortgage could also register the mortgage servicer’s identity and authority.
A National Mortgage Loan Registry

- Any member of the public could search a mortgage on-line and determine its holder and servicer.
A National Mortgage Loan Registry

• The entire loan file could be maintained by the registry (loan application, appraisal, credit report, etc.)

• But these documents would not be available to the public.
A National Mortgage Loan Registry

• The registry would issue certificates that would be conclusive evidence of the identity of the mortgage holder.

• The certificates would be acceptable in all courts.
A National Mortgage Loan Registry

• When the loan is paid off or foreclosed, a certificate from the registry would be recorded in the local real estate records.
A National Mortgage Loan Registry

• Fees for registration of mortgages would allow the registry to be financially self-supporting.
A National Mortgage Loan Registry

• A bureaucratic home?
The end