

The Banking Law Journal

Established 1889

AN A.S. PRATT & SONS PUBLICATION

MARCH 2011

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THE MASSACHUSETTS SUPREME JUDICIAL COURT FORECLOSURE DECISIONS: THE IMPACT ON THE SECURITIZATION DOCUMENTATION PROCESS

STEPHEN S. KUDENHOLDT, STEPHEN F.J. ORNSTEIN, AND JOHN P. HOLAHAN

The authors do not believe that recent decisions by the highest court in Massachusetts will call the securitization documentation process into question.

On January 7, 2011, the Massachusetts Supreme Judicial Court (the “Court”) issued its decisions in the closely watched foreclosure cases, *U.S. Bank National Association, trustee v. Antonio Ibanez* (“*Ibanez*”), and a consolidated companion case, *Wells Fargo, N.A., trustee v. Mark LaRacé & Another* (“*LaRacé*”).¹ Although the Court ruled against the trustees, its decisions do not cast doubt on the method in which mortgage loans were typically conveyed to residential mortgage-backed securities (“RMBS”) securitization trusts. As with many recent cases, however, there were issues with how the foreclosures were processed.

The primary issues in *Ibanez* and *LaRacé* were whether the plaintiffs, U.S. Bank and Wells Fargo, in their capacity as trustees in securitizations, held clear title to foreclosed property given that they foreclosed prior to com-

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pleting or recording the assignments of mortgage from the mortgagees of record to themselves as holders. In issuing its decisions, the Court agreed with the Massachusetts Land Court (the "Trial Court") that the plaintiffs did not submit sufficient evidence to prove that the mortgages were assigned to themselves prior to the foreclosure sales. The Court did not address the question of whether U.S. Bank and Wells Fargo were the holders and owners of the notes, but held that, under Massachusetts real property law, the mortgage does not automatically follow the note and must also be assigned to the foreclosing lender prior to the foreclosure sale.

Importantly, the court recognizes that an assignment of mortgage can validly be made by either of two types of documents: 1) a signed instrument that individually assigns a specific mortgage to a named party (an "individual assignment"), or 2) an agreement (such as a PSA or an MLPA as defined below) that transfers a pool of mortgage loans and that both includes operative language that assigns the related mortgages and sufficiently identifies the mortgage loans covered by the agreement (an "assignment agreement"). Given that in these cases an individual assignment was not completed until after the sale, it was incumbent on U.S. Bank and Wells Fargo to submit evidence that the mortgages had otherwise been assigned prior to the sale. Although each trustee attempted to submit evidence in the form of one or more assignment agreements, the Court ruled that such evidence as submitted did not establish that the assignment of mortgage had occurred prior to the foreclosure sales, due to specific shortcomings in the documentation as submitted.

Ibanez and *LaRice* have attracted attention nationwide from both the media and lending industry because they are cases of first impression in Massachusetts, a non-judicial foreclosure state, in a volatile environment where some commentators have provocatively asserted that the underlying securitization documentation process is fundamentally flawed. We do not believe that these cases will call such practices into question.

IBANEZ

Factual History

On December 1, 2005, Antonio Ibanez took out a loan for the purchase of residential property in Massachusetts, secured by a mortgage to the lender,

Rose Mortgage, Inc (“Rose”). Rose then recorded the mortgage. Rose later sold the loan to Option One Mortgage Corporation (“Option One”), and executed an individual assignment of mortgage in blank. Option One then stamped its name on the individual assignment of mortgage and recorded it on June 7, 2006. Before the recording, on January 23, 2006, Option One executed an individual assignment of the Ibanez mortgage in blank.

Option One assigned the Ibanez mortgage to Lehman Brothers Bank, FSB, which included the loan in a pool of loans that were ultimately securitized. Specifically, in securitizing the loan, Lehman assigned it to Lehman Brothers Holdings Inc., which then assigned it to the Structured Asset Securities Corporation, the depositor, which then assigned the mortgage, pooled with other loans, to U.S. Bank, as trustee for the Structured Asset Securities Corporation Mortgage Pass-Through Certificates, Series 2006-Z. Each of these assignments was made by an assignment agreement. As is customary in secondary mortgage market transfers, an individual assignment of mortgage was not created with respect to each such assignment.

The assignment of the Ibanez mortgage to U.S. Bank occurred pursuant to a December 1, 2006 pooling and servicing agreement (the “PSA”) which was not introduced into the Trial Court’s record. However, the Trial Court did have in the record the securitization’s private placement memorandum (“PPM”). The Trial Court noted that the PPM included the representation that mortgages “will be” assigned into the trust. The Trial Court cited a section of the PPM, which specifically stated:

[e]ach transfer of a Mortgage Loan from the Seller [Lehman Brothers Holdings Inc.] to the Depositor [Structured Asset Securities Corporation] and from the Depositor to the Trustee [U.S. Bank] will be intended to be a sale of that Mortgage Loan and will be reflected as such in the Sale and Assignment Agreement and the Trust Agreement, respectively.

The Trial Court also noted that the PPM specified that, “[e]ach Mortgage Loan will be identified in a schedule appearing as an exhibit to the Trust Agreement.” Significantly, U.S. Bank did not introduce to the record a schedule or other documentation identifying the Ibanez loan as among the mortgages that were assigned into the securitization.

Procedural History

On July 5, 2007, U.S. Bank, in its capacity as trustee for the securitization trust, foreclosed on the mortgage, and purchased the property at the foreclosure sale. The foreclosure deed (from U.S. Bank, as holder, to U.S. Bank, as purchaser) and statutory foreclosure affidavit were recorded on May 23, 2008. On September 2, 2008, American Home Mortgage Servicing, Inc. (as successor-in-interest to Option One) executed an individual assignment of the Ibanez mortgage to U.S. Bank, and U.S. Bank recorded the individual assignment on September 11, 2008. In September 2008, U.S. Bank brought an action in the Trial Court to quiet title to the property in order to obtain title insurance on the REO property. However, the Trial Court entered judgment against the plaintiff on March 26, 2009, ruling that the foreclosure sale was invalid because U.S. Bank had not proven that it was the mortgage holder at the time it foreclosed.

U.S. Bank then moved to vacate the judgment of the Trial Court, stating that it could produce assignment agreements that proved it was the holder of the mortgage prior to the notice and foreclosure sale. The Trial Court granted U.S. Bank leave to produce these documents, and U.S. Bank submitted the PPM and related securitization documents, to substantiate its claim. The judge denied the plaintiff's motion to vacate judgment concluding that the securitization documents did not alter the conclusion that the plaintiff was not the holder of the mortgage at the time of foreclosure. U.S. Bank appealed the case to the Massachusetts Supreme Judicial Court.

LARACE

Factual History

On May 19, 2005, Mark and Tammy LaRance refinanced a residential mortgage loan with Option One and the mortgage was recorded the same day. On May 26, 2005, Option One executed an individual assignment of the mortgage in blank.

Option One assigned the LaRance mortgage to Bank of America in a Flow Sale and Servicing Agreement dated July 28, 2005. Bank of America included the LaRance loan in a pool of loans that were ultimately securitized.

Specifically, in securitizing the loan, Bank of America assigned it to Asset Backed Funding Corporation (“ABFC”), the depositor, which then pooled the mortgage with others and assigned it to Wells Fargo, as trustee for the ABFC 2005-OPT 1 Trust, ABFC Asset-Backed Certificates, Series 2005-OPT 1. Each of these assignments was made by an assignment agreement. As is customary in secondary mortgage market transfers, an individual assignment of mortgage was not created with respect to each such assignment.

Wells Fargo did not provide the Trial Court with a copy of any agreement reflecting an assignment of the LaRace mortgage by Option One to Bank of America. However, Wells Fargo did produce an unexecuted copy of the mortgage loan purchase agreement (“MLPA”), which was an exhibit to the securitization’s PSA. The MLPA provided that Bank of America, as seller to ABFC: “does hereby agree to and does hereby sell, assign, set over, and otherwise convey to the Purchaser [ABFC], without recourse, on the Closing Date ...all of its right, title and interest in and to each Mortgage Loan.”

Wells Fargo also produced an unsigned copy of the securitization’s PSA, which was taken from the Securities and Exchange Commission website. The PSA provided that the depositor, ABFC, “does hereby transfer, assign, set over and otherwise convey to the Trustee, on behalf of the Trust...all the right, title and interest of the Depositor...in and to...each Mortgage Loan identified on the Mortgage Loan Schedules,” and “does hereby deliver” to the trustee the original mortgage note, an original mortgage assignment “in form and substance acceptable for recording,” and other documents pertaining to each mortgage.

Finally, Wells Fargo produced a scrubbed and anonymized schedule of loans, which it claimed identified the loans that were assigned to ABFC. However, Wells Fargo did not submit any complete or unanonymized loan schedule to the Trial Court. As determined in these proceedings, the loan schedule that was submitted did not adequately identify the LaRace mortgage.

Procedural History

On July 5, 2007, Wells Fargo, in its capacity as trustee for the securitization trust, foreclosed on the mortgage, and purchased the property at the foreclosure sale. Wells Fargo executed a statutory foreclosure affidavit and

foreclosure deed on May 7, 2008. Additionally, on May 7, 2008, Option One, which was still the record holder of the LaRace mortgage, executed an individual assignment of the mortgage to Wells Fargo as trustee, and Wells Fargo recorded the individual assignment on May 12, 2008. The recorded individual assignment declared an effective date of April 18, 2007, a date that preceded the publication of the notice of sale and the foreclosure sale.

As in *Ibanez*, Wells Fargo brought an action in the Trial Court to quiet title to the property in October 2008, in order to obtain title insurance on the REO property. Additionally, as was the result in *Ibanez*, the Trial Court entered judgment against the plaintiff on March 26, 2009, ruling that the foreclosure sale was invalid because Wells Fargo had not proven that it was the mortgage holder at the time it foreclosed. Wells Fargo was also granted leave to produce additional documentation as to its status as holder, but failed to convince the Trial Court that the securitization documents proved it was the holder at the time of foreclosure. Like U.S. Bank, Wells then appealed the case to the Massachusetts Supreme Judicial Court.

SUPREME COURT LEGAL FINDINGS — IBANEZ & LARACE

On appeal of *Ibanez* and *LaRace* to the Massachusetts Supreme Judicial Court, the Court ruled that the plaintiff trustees did not demonstrate that they were the holders of the mortgages at the time they issued the notices of sale and foreclosed on the properties. (As used in this article, "mortgage holder" means the mortgagee of record, or any assignee pursuant to a valid assignment.) The Court based its findings in part on the fact that the trustees did not have completed individual assignments until after the foreclosure sale. Further, while both trustees argued that the securitization documents they submitted established valid assignments that made them the holders of the mortgages before the notices of sale and the foreclosures, the Court disagreed.

With regard to *Ibanez*, the Court disagreed with the plaintiff trustee because the PPM, which was the principal conveyance document submitted into evidence, made reference only to an intent to assign mortgages in the future, and the evidence submitted did not include a schedule that clearly showed that the *Ibanez* loan was included in the pool of loans being securitized. Thus, as a result of these flaws, the Court upheld the Trial Court's

ruling that, Option One, not U.S. Bank, was the mortgage holder at the time of the foreclosure, and U.S. Bank did not have the authority to foreclose the mortgage.

With regard to *LaRace*, the Court also similarly disagreed with the arguments advanced by the plaintiff trustee. Wells Fargo argued that the LaRace mortgage was included in the pool assigned to ABFC by submitting the PSA, which contained present tense language assigning the loan, and an “anonymized” schedule of loans (which did not include property addresses, names of mortgagors, or any loan or servicing numbers). In using the “scrubbed” schedule as evidence, Wells Fargo argued that a specific mortgage in the schedule with the LaRace property’s zip code and city was the LaRace loan because the payment history and loan amount matched the LaRace loan. The Court observed that while the Wells Fargo PSA, in contrast with U.S. Bank’s PPM, uses the language of a present assignment rather than an intent to assign in the future, the schedule still failed to identify with “adequate specificity” that the LaRace loan had been assigned to the trust. The Court concluded that, as with the Ibanez loan, the mortgage holder of the LaRace loan was Option One, and no evidence was submitted to the Trial Court which demonstrated that the LaRace loan was ever assigned by Option One to another entity before the publication of the foreclosure notice and the sale.

Additionally, in advancing their positions, the trustees raised three supplementary arguments that were each dismissed by the Court. First, the trustees contended that the individual assignments in blank executed by Option One, identifying the assignor but not the assignee, sufficed to be effective assignments in their own right. The Court stated that they have long held that a conveyance of real property, such as a mortgage, that does not name the assignee conveys nothing and is void. Second, the trustees argued that because they each held the mortgage notes, they had a sufficient financial or equitable interest in the mortgages to allow them to foreclose (known commonly as the “mortgage follows the note theory”). However, the Court concluded that consistent with existing Massachusetts law, in the absence of a valid written assignment of a mortgage or a court order of assignment, the mortgage holder remains unchanged.² Third, the trustees argued that post-foreclosure sale individual assignments are sufficient when taken in conjunction with the evidence of a presale assignment. However, the Court again found against

the plaintiffs and stated that because an assignment of a mortgage is a transfer of legal title, it becomes effective with respect to the power of sale only on the transfer date, and not before.

Notably, in making the above findings, the Court opined that in order to show ownership of the mortgage, *the assignment of mortgage does not have to be recorded or be in recordable form at the time of foreclosure notice or sale*. The Court observed explicitly that, "where a pool of mortgages is assigned to a securitized trust, the executed agreement that assigns the pool of mortgages, with a schedule of the pooled mortgage loans that clearly and specifically identifies the mortgage at issue as among those assigned, may suffice to establish the trustee as the mortgage holder." The Court also noted, however, that the parties must show that an assignment was made by an entity that previously held the mortgage. The Court also explicitly stated that an assignment may be demonstrated either by:

1. A complete chain of assignments linking the assignee to the record holder of the mortgage, or
2. A single assignment from the record holder of the mortgage naming the assignee (that is, without showing intervening assignees).

Again, the critical factor emphasized by the Court is that the foreclosing entity hold a valid assignment of mortgage prior to commencing the foreclosure.

In a little noticed aspect of this decision, the Court, in apparently breaking with previous custom in Massachusetts, clearly indicates that the post foreclosure confirmatory assignments of mortgage used in both the *Ibanez* and *LaRace* cases may only be used where there was a valid assignment prior to the foreclosure notice — again, an assignment that was "valid" by being in writing and naming an assignee, but which need not be recorded or in recordable form. Based on an amicus brief submitted in connection with the case, prior to this decision, a confirmatory assignment could be used after a foreclosure sale even if there was no formal prior assignment. The Court's decision apparently has the practical effect of retroactively changing accepted procedures for the use of a confirmatory assignment, which may create difficulties for servicers of mortgage loans in Massachusetts.

It should also be noted that the Court's decision does not address the provisions of Article 9 of the Uniform Commercial Code (the "UCC") as adopted by the state of Massachusetts. Article 9 applies to sales of promissory notes and mortgages, and "Section 9-203(g) adopts the traditional view that the mortgage follows the note, i.e. the transferee of the note acquires the mortgage as well."³ "The attachment of a security interest in a right to payment or performance secured by a security interest or other lien on personal or real property is also attachment of a security interest in the security interest, mortgage or other lien."⁴ Furthermore, the Court also did not address an additional method which, under Article 9 of the UCC, would permit a mortgagee to conduct a non-judicial foreclosure without a recorded assignment. Section 9-607(b) provides "if necessary to enable a [a purchaser of a promissory note] to exercise under subsection(a)(3) the right of a [seller of a promissory note] to enforce a mortgage non-judicially, the [lender] may record in the office in which a record of the mortgage is recorded (1) a copy of the [mortgage loan purchase agreement or equivalent] that creates or provides for a security interest⁵ in the obligation secured by the mortgage; and (2) the secured party's sworn affidavit in recordable form stating that: (A) a default has occurred; and (B) the [lender] is entitled to enforce the mortgage non-judicially."⁶ These provisions of Article 9 have generally been adopted in every state. While the interplay between these provisions and the real property law in a particular state may vary, they could be effective to establish that the noteholder has an ownership interest in the related mortgage.

CONCLUSION: KEY TAKEAWAYS FROM IBANEZ & LARACE

We emphasize that the *Ibanez* and *LaRace* cases are Massachusetts state law decisions, and are binding only in Massachusetts. Under our interpretation of the decisions, the cases do not call into question the structure of existing or future securitizations in Massachusetts or beyond. They do, however emphasize the importance of complying with the requirements of the transaction documents and the local state law foreclosure rules.

Further, the Court indicated that in place of an individual assignment of mortgage, a complete set of assignment agreements — notably including a schedule to the PSA that clearly showed the *Ibanez* and *LaRace* mortgages in

the pools — would have constituted sufficient proof of assignee status by the trustees.

What is critical about the *Ibanez* and *LaRae* decisions is that in Massachusetts, a non-judicial foreclosure state, assuming that the Lender is the owner and holder of the mortgage notes, in order to properly complete a foreclosure in the state, local real property law must be adhered to, which based upon the Court's ruling in these cases can be satisfied by the following:

1. A completed assignment of mortgage, whether or not recorded, from the mortgagee of record that names the securitization trustee as the assignee; or
2. The governing securitization documents, such as the PSA or MLPA, provided that they: (i) include an assignment of the mortgage to the trust in its contractual terms; (ii) identify the loan that is assigned with adequate specificity (and "scrubbed" and "anonymized" schedules, as customarily submitted to the SEC, cannot be used to prove the identity of the loan); and (iii) connect the mortgagee of record to the securitization trustee.

Further, it is clear that the following foreclosure practices *will not* suffice in Massachusetts under the Court's interpretation of the governing real property law:

1. A backdated assignment of mortgage that is provided to the trustee in an attempt to retroactively assign the mortgage prior to the foreclosure notice and sale;
2. A confirmatory assignment after the foreclosure sale unless there was a valid assignment prior to the sale; or
3. An assignment in blank held by the trustee, to the extent it remains in blank and is not completed prior to the foreclosure notice and sale.

NOTES

¹ Massachusetts Supreme Judicial Court, Slip Opinion No. SJC-10694, ___ N.E.2d ___, 2011 WL 38071 (January 7, 2011).

² *But see* discussion *infra*, notes 3-5.

³ Massachusetts Uniform Commercial Code, Official Comment 6 to Section 9-308(e).

⁴ Massachusetts Uniform Commercial Code, Section 9-203(g).

⁵ Section 1-201(37) of the Massachusetts Commercial Code defines “Security Interest” as including “any interest of...a buyer of...a promissory note in a transaction that is subject to Article 9.”

⁶ For a further discussion relating to the UCC’s treatment of sales of notes and mortgages, see Jack Murray, “Title and UCC Issues in Connection with Sales and Assignments of Defaulted CMBS Loans,” *The Abstract*, Fall 2010, p. 14. Relevant UCC provisions are also discussed in the American Securitization Forum’s November 16, 2010 White Paper titled “Transfer and Assignment of Residential Mortgage Loans in the Secondary Mortgage Market.”