CONSUMER LAW — MORTGAGE FORECLOSURE — MASSACHUSETTS SUPREME JUDICIAL COURT UNANIMOUSLY VOIDS FORECLOSURE SALES BECAUSE SECURITIZATION TRUSTS COULD NOT DEMONSTRATE CLEAR CHAINS OF TITLE TO MORTGAGES. — *U.S. Bank National Ass'n v. Ibanez*, 941 N.E.2d 40 (Mass. 2011).

As a result of the ongoing foreclosure crisis, at least two million mortgage foreclosure cases have been brought before state and federal courts over the past five years, and approximately two million more such cases are still waiting to be heard.[1] These cases are forcing courts to examine how long-established principles of state property law apply to modern mortgage lending and securitization practices. Recently, in *U.S. Bank National Ass'n v. Ibanez*,[2] the Massachusetts Supreme Judicial Court voided two foreclosure sales by U.S. Bank and Wells Fargo[3] because the banks could not demonstrate that they were assigned the associated mortgages in writing prior to the foreclosure sales.[4] In reaching this conclusion, the court held that the possession of a promissory note secured by a mortgage is not sufficient to demonstrate authority to foreclose.[5] Some commentators have criticized this holding as a departure from the common law rule that the mortgage "follows the note,"[6] which they claim is codified in the Uniform Commercial Code.[7] However, a careful analysis reveals that *Ibanez* establishes that the mortgage follows the note as a security interest, but not as a real property interest. This holding, in turn, has important implications for foreclosure litigation in Massachusetts and possibly in several other states as well.

In 2005, Antonio Ibanez took out a mortgage loan to purchase a property in Springfield, Massachusetts.[8] The mortgage loan was secured by a mortgage to lender Rose Mortgage, Inc., which then as-

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[1] *Times Topics: Foreclosures*, N.Y. TIMES, http://topics.nytimes.com/top/reference/timestopics/subjects/f/foreclosures/index.html (last updated June 27, 2011).

[2] 941 N.E.2d 40 (Mass. 2011).

[3] *Id.* at 44.

[4] *Id.* at 54.

[5] *Id.* at 53–54.

[6] What is commonly referred to in everyday speech as a "mortgage" is referred to in legal terminology as a "mortgage loan," which is a loan secured by an interest in real property. *See* BLACK'S LAW DICTIONARY 1020 (9th ed. 2009). A mortgage loan is comprised of two key components: a "note" and a "mortgage." The "note" is a promissory note signed by the borrower that obligates the borrower to repay a certain amount of money to the holder of that note. *Id.* at 1162. The "mortgage" is the instrument whereby the borrower grants a security interest in real property to the lender. *Id.* at 1101–02.

[7] *See, e.g.*, 5 BAXTER DUNAWAY, THE LAW OF DISTRESSED REAL ESTATE § 72A:32 (2011); Victoria V. Corder, *Homeowners and Bondholders as Unlikely Allies: Allocating the Costs of Securitization in Foreclosure*, BANKING & FIN. SERVS. POL'Y REP., May 2011, at 19, 23.

[8] *Ibanez*, 941 N.E.2d at 45–46.

signed the mortgage to Option One Mortgage Corporation, which executed an assignment of the Ibanez mortgage "in blank" (that is, without naming an assignee).[9] Then, according to U.S. Bank, the Ibanez mortgage changed hands through a series of assignments and was ultimately pooled with over one thousand other mortgages and assigned to U.S. Bank.[10] At some point, U.S. Bank also came to hold the promissory note secured by the Ibanez mortgage.[11] When the assignment process was complete, "the Ibanez and other loans were pooled into a trust and converted into mortgage-backed securities that [could] be bought and sold by investors — a process known as securitization."[12] That same year, Mark and Tammy LaRace took out a loan secured by a property in Springfield, Massachusetts, and after a very similar series of transactions, Wells Fargo came to hold the LaRaces' promissory note and (allegedly) the mortgage securing it.[13]

In 2007, both Ibanez and the LaRaces defaulted on their mortgage loans, and U.S. Bank and Wells Fargo foreclosed on their properties.[14] The banks then purchased the properties at the resulting foreclosure sales.[15] It was undisputed that the banks held the Ibanez and LaRace promissory notes at the time of the foreclosure sales.[16] However, despite the banks' contentions that they were assigned the mortgages prior to the foreclosure sales, the banks were unable to produce written documentation demonstrating the assignments.[17] Nevertheless, the banks were able to demonstrate that *after* each foreclosure sale they were officially assigned the mortgages in writing.[18] The banks argued that the postsale assignments, together with the evidence they offered of presale assignments, established their authority to foreclose on the properties.[19]

In 2008, the banks brought separate actions in Massachusetts land court to quiet title to the Ibanez and LaRace properties, and the two cases were heard jointly.[20] The banks asserted in their complaints that they became the holders of the mortgages through the assignments ex-

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[9] *Id.* at 46.

[10] *Id.*

[11] *See id.* at 53–54 (taking for granted that U.S. Bank held the promissory note).

[12] *Id.* at 46.

[13] *See id.* at 47–48, 53–54.

[14] *See id.* at 44. Massachusetts foreclosures are conducted nonjudicially via the power of sale granted to the mortgage holder by the terms of the mortgage instrument. *See* MASS. GEN. LAWS ch. 183, § 21 (2011); *id.* ch. 244, § 14.

[15] *Ibanez*, 941 N.E.2d at 44.

[16] *See id.* at 53.

[17] *Id.*

[18] *See id.* at 47, 49.

[19] *See id.* at 54.

[20] *Id.* at 44–45.

ecuted after the foreclosure sales.[21] Neither Ibanez nor the LaRaces initially responded, and the banks moved for default judgment.[22]

The land court entered judgment against the banks.[23] The judge ruled that because the banks had not been assigned the mortgages until after the foreclosure sales, they "had no interest in the mortgages being foreclosed at the time of the publication of the notices of sale or at the time of the foreclosure sales."[24] Therefore, the notices of the foreclosure sales improperly named the banks as the mortgage holders, in violation of the statutory requirements for the foreclosure process.[25]

The Supreme Judicial Court granted the parties' applications for direct appellate review[26] and affirmed in a unanimous opinion written by Justice Gants.[27] Justice Gants began his analysis with a discussion of the requirements for establishing authority to foreclose on a property under Massachusetts law.[28] If the borrower defaults on his or her mortgage loan payments to the holder of the note, Massachusetts's statutory framework provides for nonjudicial foreclosure, whereby the foreclosing party can move to foreclose without first seeking court approval.[29] Because of the "substantial power" that this scheme affords the foreclosing party,[30] Justice Gants stated that the party must "follow strictly"[31] the terms of the power of sale, including the requirement that "only a *present holder of the mortgage* is authorized to foreclose on the mortgaged property."[32] The banks could therefore have had authority to foreclose on the Ibanez and LaRace properties only "if they were the assignees of the mortgages at the time of the notice of sale and the subsequent foreclosure sale,"[33] or in other words, if they could demonstrate valid and complete chains of title for the mortgages (as distinct from the notes secured by those mortgages). Furthermore, because Massachusetts is a "title theory" state,[34] "a mortgage is a transfer

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[21] *Id.* at 44.

[22] *Id.*

[23] *Id.* at 45.

[24] *Id.*

[25] *Id.* (citing MASS. GEN. LAWS ch. 244, § 14 (2011)). The banks subsequently brought motions to vacate the judgment, submitting hundreds of pages of previously undisclosed documents, many of which "related to the creation of the securitized mortgage pools in which the Ibanez and LaRace mortgages were purportedly included." *Id.* The land court denied the motions. *Id.*

[26] *Id.*

[27] *Id.* at 44.

[28] *See id.* at 49–51.

[29] *Id.* at 49.

[30] *Id.*

[31] *Id.* at 49–50 (quoting Moore v. Dick, 72 N.E. 967, 968 (Mass. 1905)) (internal quotation marks omitted).

[32] *Id.* at 50 (emphasis added).

[33] *Id.* at 51.

[34] American courts have traditionally recognized one of three theories of mortgage law: the "title," "lien," and "intermediate" theories. RESTATEMENT (THIRD) OF PROP.: MORTGAGES

of legal title in a property to secure a debt," meaning that any such assignment is a conveyance of an interest in land and therefore must be made in "a writing signed by the grantor."[35] As a result, whether the banks had the authority to foreclose would hinge on whether the documentation they submitted to the court demonstrated clear chains of mortgage assignments ending with the timely assignments of the mortgages to the securitization trusts.[36]

The banks offered four alternative reasons that the documentation they submitted to the court demonstrated valid chains of title.[37] First, they argued that the mortgages were assigned via the agreements that created the securitization trusts.[38] The court rejected this argument because the securitization documents did not contain loan schedules specifically identifying the Ibanez and LaRace mortgages as among those assigned.[39] The court did, however, note that an assignment need not be in "recordable form at the time of the notice of sale . . . although recording is likely the better practice," and that an executed securitization agreement containing a loan schedule that "clearly and specifically identifies the mortgage at issue as among those assigned[] may suffice to establish the trustee as the mortgage holder."[40]

Second, the banks claimed that the mortgages were transferred via the assignments in blank.[41] However, in their reply briefs, the banks conceded that assignments in blank do not constitute lawful assignments.[42] The *Ibanez* court agreed, noting that conveyances of real property that do not name the assignees are facially invalid under Massachusetts law.[43]

Third, the banks claimed that because a mortgage follows the note, the mortgages were assigned via the transfer of the notes.[44] In response, Justice Gants wrote, "the assignment of the note does not carry with it the assignment of the mortgage," but "[r]ather, the holder of the mortgage holds the mortgage in trust for the purchaser of the note, who has an equitable right to obtain an assignment of the mortgage,

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§ 4.1 cmt. a (1997) (explicating the theories). The "title theory" approach is a minority approach. *See id.* cmt. a(2).

35 *Ibanez*, 941 N.E.2d at 51; *see also* MASS. GEN. LAWS ch. 183, § 3 (2011).

36 *See Ibanez*, 941 N.E.2d at 53.

37 *See id.* at 52–54.

38 *Id.* at 51.

39 *Id.* at 52. Wells Fargo had claimed that the LaRace mortgage was clearly identified in the securitization agreement's loan schedule because data for one of the loans listed matched the LaRace property's zip code, city, payment history, and loan amount. *Id.* at 48.

40 *Id.* at 53.

41 *Id.*

42 *Id.*

43 *Id.*

44 *Id.*

which may be accomplished by filing an action in court and obtaining an equitable order of assignment."[45] Thus, "[i]n the absence of a valid written assignment of a mortgage or a court order of assignment, the mortgage holder remains unchanged," and the banks' holding of the mortgage notes was insufficient to establish authority to foreclose.[46]

Fourth, the banks contended that the post-sale assignments of the mortgages established their authority to foreclose.[47] The court wrote that even if such "confirmatory" assignments have in recent years become a standard industry practice, "[a] confirmatory assignment . . . cannot confirm an assignment that was not validly made earlier or backdate an assignment being made for the first time."[48] The court thus voided the foreclosure sales.[49] Justice Cordy[50] concurred separately "only to underscore that what is surprising about these cases is not the statement of principles articulated by the court regarding title law and the law of foreclosure . . . but rather the utter carelessness with which the plaintiff banks documented the titles to their assets."[51]

Much of the existing commentary on *Ibanez* has focused on the decision's implications for the mortgage securitization process.[52] However, a perhaps less understood aspect of the court's decision is its holding that a party must have been validly assigned the mortgage in order to have authority to foreclose. Though the *Ibanez* court purported merely to be applying "well established" law in reaching this conclusion,[53] several commentators have criticized the court for what they

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[45] *Id.* at 53–54 (citing Barnes v. Boardman, 21 N.E. 308, 309 (Mass. 1889); Young v. Miller, 72 Mass. (6 Gray) 152, 154 (1856)).

[46] *Id.* at 54.

[47] *Id.*

[48] *Id.* at 55.

[49] *Id.*

[50] Justice Cordy was joined by Justice Botsford.

[51] *Ibanez*, 941 N.E.2d at 55 (Cordy, J., concurring).

[52] *See, e.g.*, Stephen S. Kudenholdt, Stephen F.J. Ornstein & John P. Holahan, *The Massachusetts Supreme Judicial Court Foreclosure Decisions: The Impact on the Securitization Documentation Process*, 128 BANKING L.J. 195 (2011); Adam Levitin, Ibanez *and Securitization Fail*, CREDIT SLIPS (Jan. 10, 2011, 2:23 PM), http://www.creditslips.org/creditslips/2011/01/ibanez.html.

[53] *Ibanez*, 941 N.E.2d at 55. Interestingly, though the court derived this holding nearly entirely from principles expressed in *Barnes v. Boardman*, 21 N.E. 308 (Mass. 1889), and *Young v. Miller*, 72 Mass. (6 Gray) 152 (1856), these cases were cited in only three of the briefs filed by the parties and their amici. *See* Brief of Defendant-Appellee Antonio Ibanez at 26, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Amici Curiae Darlene Manson, Germano Depina, Robert Lane, Ann Coiley, Roberto Szumik, Geraldo Dosanjos, and National Consumer Law Center at 30, 35–37, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Amicus Curiae the Real Estate Bar Ass'n for Massachusetts, Inc. at 11–12, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694) [hereinafter REBA Amicus Brief]. The other six briefs filed by the parties and their amici did not cite *Barnes* or *Young*. *See* Appellants' Opening Brief, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Appellant Wells Fargo Bank, as Trustee, in Reply to the Brief of Appellees Mark A. LaRace and Tammy L. LaRace, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Appellant U.S. Bank, as Trustee, in Reply to the

claim was a departure from the rule that the mortgage "follows the note," meaning that the transfer of a note confers on the transferee the rights of a mortgage holder. According to these critics, this rule is codified in the Uniform Commercial Code and supersedes conflicting common law doctrines.[54] However, one of the main reasons that the debate over whether the mortgage "follows the note" is so contentious and so confusing is that there are, in fact, two distinct ways in which a mortgage could be said to "follow the note," and only one of these appears to have been addressed by *Ibanez*.

The first way in which the mortgage may follow the note is as the security interest for the mortgage loan. If the mortgage follows the note in this manner, the note would remain secured even after a transfer to an individual who does not hold the mortgage. *Ibanez* is not necessarily inconsistent with the notion that the mortgage follows the note in this fashion, for two reasons. First, *Ibanez* confirmed that the mortgage holder serves as a trustee for the note holder, and this relationship prevents the note from becoming unsecured by virtue of the note holder's inability to enforce it on his or her own.[55] Second, the *Ibanez* court left untouched section 9-203(g) of the Uniform Commercial Code (which has been adopted by Massachusetts), which provides that the transfer of a secured note also transfers the security interest.[56]

The second sense in which the mortgage may "follow the note" is as an interest in real property. If the mortgage follows the note in this manner, the holder of the note could claim legal title to the property securing the mortgage debt. A careful analysis of the language used by the *Ibanez* court strongly suggests that the court used the term "mortgage" only in this sense, and therefore held only that the mortgage does not follow the note as a real property interest. For example, the court referred to "the mortgage" being held "in trust for the purchaser of the note,"[57] and it makes no sense to speak of "holding" a "security inter-

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Brief of Appellee Antonio Ibanez, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief and Supplemental Record Appendix of the Defendants-Appellees Mark A. LaRace and Tammy L. LaRace, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Amicus Curiae the Attorney General on Behalf of the Commonwealth of Massachusetts, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694); Brief of Amicus Curiae Marie McDonnell, CFE, *Ibanez*, 941 N.E.2d 40 (No. SJC-10694).

[54] *See, e.g.*, DUNAWAY, *supra* note 7; Corder, *supra* note 7, at 19, 23. Furthermore, the Real Estate Bar Association for Massachusetts argued in its amicus brief that "[i]t has been long held as an axiomatic principle of Massachusetts law that the mortgage follows the note," REBA Amicus Brief, *supra* note 53, at 11, and that this understanding reflected "an analysis of applicable legal precedent as well as long-standing practice among the conveyancing bar," *id*. at 14.

[55] *See* RESTATEMENT (THIRD) OF PROP.: MORTGAGES § 5.4 cmt. e (1997).

[56] *See* MASS. GEN. LAWS ch. 106, § 9-203(g) (2010); U.C.C. § 9-203 cmt. 9 (2000). Alternatively, it is possible that when the Massachusetts General Court adopted the current version of section 9-203 in 2001, it did not intend to modify the rules for the transfer of real property. That is, it is possible that section 9-203(g) does not apply to mortgage assignments at all.

[57] *See Ibanez*, 941 N.E.2d at 54.

est" in this manner. Furthermore, the relevant passages of the cases cited by the court in support of this holding clearly refer to the term "mortgage" as an interest in real property.[58]

Ibanez therefore can be interpreted as establishing that in Massachusetts the mortgage "follows the note" as a *security* interest (that is, as the security for the mortgage loan), but not as a *real property* interest (that is, as legal title to the property securing the loan).[59] This interpretation of *Ibanez* resolves what at first appears to be a contradiction between state real property law and section 9-203(g) of the Uniform Commercial Code. Furthermore, as the debate over whether the mortgage "follows the note" is not confined to Massachusetts, the *Ibanez* court's resolution of this issue may serve as a model for other state courts, particularly for those in states that follow the title theory of mortgage law.[60]

The *Ibanez* court's resolution of this debate has several important implications for the ongoing foreclosure crisis. First, and perhaps most obviously, *Ibanez* clarifies that any entity wishing to foreclose on a property must be able to demonstrate, in writing, a clear and valid chain of title for the mortgage in question. This holding raises a new (or more accurately, previously ignored) procedural hurdle for foreclosure, and it provides mortgage loan borrowers with another potential defense to foreclosure. One might ask why the court would require such a seemingly duplicative procedure. A possible answer is that, in recognition of the gravity of removing individuals or families from their homes, the *Ibanez* court felt that any interest in maintaining efficiency in the foreclosure process was outweighed by an interest in preventing fraud.[61]

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[58] *See Barnes*, 21 N.E. at 309 (stating that "the mortgagee would hold the legal title in trust for the purchaser of the debt"); *Young*, 72 Mass. (6 Gray) at 153 (stating that the holder of a mortgage note has "an equitable interest in real estate, the legal title to which is in another; such interest being manifested by an actual or resulting trust").

[59] *See also* PERMANENT EDITORIAL BOARD FOR THE UNIFORM COMMERCIAL CODE, DRAFT REPORT: UCC RULES APPLICABLE TO THE ASSIGNMENT OF MORTGAGE NOTES AND TO THE OWNERSHIP AND ENFORCEMENT OF THOSE NOTES AND THE MORTGAGES SECURING THEM 8–9 n.37 (2011) (presenting the assignment of "an interest in the mortgage securing the note" as governed by contract law, but presenting the assignment of "the mortgage" as "the province of real property law").

[60] Many states' statutory schemes explicitly grant the power to foreclose only to the holder of a mortgage or to a party with an analogous function, such as the trustee of a deed of trust. *See, e.g.*, CAL. CIV. CODE § 2932.5 (West 2011); NEV. REV. STAT. ANN. § 107.080 (West 2011). Additionally, a recent Nevada Supreme Court case reached essentially the same result as *Ibanez* on whether the mortgage "follows the note." *See* Levya v. Nat'l Default Servicing Corp., 255 P.3d 1275, 1280 (Nev. 2011).

[61] The court seemed to adopt this perspective when it stated that "[w]here . . . mortgage loans are pooled together in a trust and converted into mortgage-backed securities, the underlying promissory notes serve as financial instruments generating a potential income stream for inves-

Second, *Ibanez* suggests that many recent foreclosures may have been invalid, which could cause individuals who purchased wrongfully foreclosed-on properties to lose any legitimate claims to the titles to those properties.[62] Such fears may be compounded by the fact that many foreclosures are conducted by entities known as "special servicers,"[63] which may not have been formally assigned the mortgage, or by Mortgage Electronic Registration Systems, Inc. (MERS),[64] whose assignment documentation has recently been called into question.[65] This consequence, in turn, may negatively impact title insurers, as it suggests they may face an increase in claims, as well as companies with an existing inventory of properties obtained at foreclosure sales, as they may find it more difficult to sell these properties and to obtain title insurance.[66]

But perhaps the most important lesson of *Ibanez* is that even in an age of rapid innovation in mortgage lending and securitization, mortgage lenders and other participants in the mortgage loan market must still comply with state property law, even if that law has been infrequently examined for over a century and no longer corresponds with widespread mortgage lending industry practices. While it remains to be seen how courts in Massachusetts and other states will resolve the myriad mortgage law issues currently before them, *Ibanez* will almost certainly aid that process by clarifying a complex point of law that, though it might seem quite abstract or technical to a casual observer, is of the utmost importance to mortgage lenders, investors, and families struggling to stay in their homes.

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tors, but the mortgages securing these notes are still legal title to someone's home or farm and must be treated as such." *Ibanez*, 941 N.E.2d at 51–52.

62 *See id.* at 55 (Cordy, J., concurring) (raising this issue). The Massachusetts Supreme Judicial Court recently addressed this issue in *Bevilacqua v. Rodriguez*, 955 N.E.2d 884 (Mass. 2011), in which the court held that a purchaser of a wrongfully foreclosed-on property did not have standing to try title to that property. *Id.* at 892–93, 898.

63 *See* Adam J. Levitin & Tara Twomey, *Mortgage Servicing*, 28 YALE J. REG. 1, 24 (2011) (discussing the role of special servicers).

64 *See In re* Huggins, 357 B.R. 180, 183 (Bankr. D. Mass. 2006) ("MERS administers an electronic registry to track the transfer of ownership interests and servicing rights in mortgage loans, serving as mortgagee of record and holding legal title to mortgages in a nominee capacity.").

65 *See* Jennifer B. McKim, *Coakley Steps Up Probe into Foreclsoure Fraud*, BOSTON.COM (July 26, 2011), http://articles.boston.com/2011-07-26/business/29817105_1_coakley-foreclosure-fraud-mers (noting that the Massachusetts Attorney General launched an investigation to adequately document mortgage assignments). *See generally* Christopher L. Peterson, *Foreclosure, Subprime Mortgage Lending, and the Mortgage Electronic Registration System*, 78 U. CIN. L. REV. 1359, 1374–97 (2010) (discussing the legal issues raised by MERS).

66 *See* Levitin, *supra* note 52.