

Legal analysis to guide the mortgage industry and protect its interests.

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Minnesota and Rhode Island Courts Rule That MERS May Foreclose by Meaghan E. Ryan

Two recent decisions arriving out of non-judicial states have upheld MERS's ability to foreclose. First, the Minnesota Supreme Court recently held that an assignment of the underlying debt does not serve to assign legal title to the mortgage. In addition, the Superior Court of Rhode Island upheld MERS's standing to foreclose as the mortgagee of record because the mortgage specifically authorizes MERS to invoke the power of sale.

The Minnesota case of *Jackson et al. v. Mortgage Electronic Registration Systems, Inc., et al.*, involved five homeowner plaintiffs who claimed that MERS did not comply with Minnesota law regarding foreclosure by advertisement. The plaintiffs argued that because Minnesota law requires that the mortgage and all assignments of the mortgage be recorded prior to the foreclosure by advertisement, MERS must record all transfers of the underlying notes prior to foreclosure. The U.S. District Court for the District of Minnesota certified the question to the Supreme Court of Minnesota, which ruled in favor of MERS.

The relevant Minnesota statute (Minn. Stat. § 580.02) required that a party seeking to foreclose by advertisement meet the following requirements:

- 1) That some default in a condition of such mortgage has occurred, by which the power to sell has become operative;
- 2) That no action or proceeding has been instituted at law to recover the debt then remaining secured by such mortgage;
- 3) That the mortgage has been recorded and, if it has been assigned, that all assignments thereof have been recorded.

First, the plaintiffs argued that the term "mortgage" as used in the statute referred not only to the security instrument, but also to the promissory note because the term is often used indiscriminately to refer to the security instrument, the underlying debt or the two instruments together. The Court disagreed, finding that the term "mortgage," as used in the relevant statute, referred only to the security instrument because the statute as a whole distinguished between the mortgage and the underlying debt. Therefore, the Court concluded that the statutory requirement to record assignments of the mortgage did not require that assignments of the promissory note be recorded.

The plaintiffs also argued that because the assignment of the note results in an assignment of the mortgage as a matter of law, the assignment of the note must be recorded in order to foreclose by advertisement because it operates to also assign the mortgage. The Court also rejected this argument, noting that an assignment of the note is only an equitable assignment of the mortgage and does not transfer legal title to the mortgage. Thus, the Court had not historically required assignment of the equitable interest to the underlying debt. The Court also noted that MERS was the mortgagee of record for each of the plaintiffs' loans. A broader view of Minnesota case law revealed that it was possible for a party to hold legal title to the security instrument without also holding the interest in the underlying promissory note. Ultimately, the Court held that while an assignment of a promissory note does constitute an equitable assignment of the security instrument, a promissory note assignment is not an assignment that affects legal title, and only assignments of legal title of the security instrument must be recorded in order to institute a foreclosure by advertisement. The Court ruled a promissory note assignment by a MERS member does not have to be recorded before MERS can institute a foreclosure by advertisement.

The Rhode Island case, *Bucci v. Lehman Brothers Bank, et al.*, involved a direct attack to MERS's standing to foreclose mortgages despite its role as the mortgagee of record. In *Bucci*, the plaintiffs argued 1) that the language of their mortgages did not authorize MERS to foreclose via the power of sale because only the mortgage granted the power of sale only to the lender, and 2) that Rhode Island law implicitly prohibited MERS from invoking the power of sale.

The plaintiffs claimed that because their mortgage stated that "Lender . . . may invoke the statutory power of sale" and defined "Lender" as Lehman Brothers, only Lehman Brothers could invoke the power of sale. The Court, however, observed that the mortgage stated that "if necessary to comply with law or custom, MERS (as nominee for Lender and Lender's successors and assigns) has the right to exercise any or all of those interests, including, but not limited to, the right to foreclose and sell the Property." Thus, even though the mortgages did grant the power of sale to the Lender, the Court held that the mortgages also granted the power of sale to MERS, and MERS therefore had the right to invoke the statutory power of sale. Because MERS was the named mortgagee and nominee of Lehman Brothers, it could invoke the power of sale.

The plaintiffs also argued that Rhode Island law did not permit MERS to foreclose because Rhode Island law specifically contemplated that the lender and mortgagee would be one and the same. The Court rejected this argument, again noting that MERS was the named mortgagee and was thus entitled to invoke the power of sale. The plaintiffs further claimed that MERS could not be considered a mortgagee because Rhode Island law intended that borrowers would make their payments to the mortgagee and MERS did not collect mortgage payments. The Court disregarded this argument, noting that it would lead to an absurd result because it would preclude mortgagees from employing servicers to service mortgages and collect payments secured by mortgages.

These lawsuits are representative of several somewhat similar lawsuits across the country that object to the involvement of MERS in the foreclosure process and the mortgage finance process in general. Challenges to the MERS system have grown in recent months, and borrowers continue to present new theories to test the MERS system. We will continue to monitor MERS litigation and keep you up to date on any impact it may have on the industry.