Bain vs. MERS – Washington State Supreme Court
"The Financial Lending Industry Gets Its Come-Uppance"

August 30, 2012

Executive Summary

On August 16, 2012 the Washington State Supreme Court rendered a unanimous opinion written by Justice Tom Chambers, answering three questions presented to it by the Federal District Court, Western District of Washington and Judge Coughenour, concerning the foreclosure processes that have been conducted by and through the Electronic Mortgage Registration system (MERS) and it accomplices.[1] Very briefly, the MERS methodology was invented to avoid the time and expense of recording assignments of Deeds of Trust (DOT) and Promissory Notes (Notes) at the County level. It also made it possible for multiple and electronically enhanced global trading of the value ostensibly held by these DOTs and Notes. The MERS system created immediate liquidity in a process that traditionally was not liquid. This system advanced and fueled the well known financial catastrophes that resulted once the house of cards collapsed.[2]

MERS was named as the agent for the holders of the Note and DOT and simultaneously as the "beneficiary" of the DOT. This was a hybrid entity created by the financial wizards. It has no parallel in the American tradition of land ownership and transfer. Similarly, the MERS entity, along with other creative processes, allowed the DOT and the Note to be separated and sold and assigned multiple times as if they had no relationship to each other. Finally, the confusion created by the two first practices has led to the practical impossibility of determining who actually owns the Note or the DOT and hence, the right to foreclose. It is axiomatic, and fortunately upheld by the Washington Court, that it is only the owner of the debt instrument that has the right to foreclose. The fact that someone "says" that MERS is the beneficiary and has the right to foreclose does not create such a right. Paper will not refuse ink.

> The first question was: Is the Mortgage Electronic Registration System, Inc. a lawful "beneficiary" within the terms of ….RCW 61.24.005(2) if it never held the note secured by the DOT? The short answer: No.

[1] I use the word "accomplice" intentionally to convey the potential criminality of what has transpired in the "global economic meltdown" caused by these financial manipulations. Nevertheless, the Bains vs. MERS case does not enter into the criminal discussion.

[2] Many treatises, books and legal opinions have been written on the broader context of the financial crisis. That is not the subject of this memo. However, it should be understood that these types of systems were and are directly responsible for the "Great Recession", as it now in its eighth year is being called.

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The second question was: What is the legal effect of MERS acting as an unlawful beneficiary under Washington's Deed of Trust Act? The short answer: The Court declined to answer this question based upon the facts before it.

The third question was: Does a homeowner possess a cause of action under the Washington Consumer Protection Act against MERS if MERS acts as an unlawful beneficiary under Washington's Deed of Trust Act? The short answer: Yes, but the plaintiff has to establish all of the elements of the CPA claim.

The case will go back to Judge Coughenour and it is expected that the Court will "runs MERS through the wringer if it tries to stonewall discovery of its records and this case will force MERS for the first time into actual semi-transparency on its practices and records."[3]

Critical Points of the Case and What They Might Mean As Applied

Several questions about the impacts of this case come to mind immediately:

1. Will our Superior Courts readily restrain, upon proper motion and proof, any action that is brought to halt a foreclosure that involves the use of MERS in the capacity of agent and beneficiary?

2. Will the ruling be applied retroactively? In other words, will homeowners who were non-judicially foreclosed with a MERS tainted process be able to go back and reinstate their DOT and Note or at least possession of the property while the ownership interests are sorted out, if ever?

3. Will the Bain vs. MERS case become a lever in the mediation process under Washington's Foreclosure Fairness Act of 2011 and assist in the process to get reasonable and fair loan modifications for homeowners if the mediation matter involved a MERS situation?

4. Will foreclosures involving a MERS situation even go forward? Or, put in another way, can MERS produce the documents showing the Note and the chain of assignments leading to the current holder that could authorize such a foreclosure by it as the real beneficiary?

[3] Eric C. Nelsen, of Sayre Law Offices in Seattle (206) 625-0092, provided an analysis of the Bains vs. MERS case to the King County Real Property list serve and to the WSBA Real Property, Probate and Trust Section list serve immediately upon the filing of the Court's decision. Mr. Nelsen's short memo will be cited again.

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5. Will MERS and its creators and accomplices really be held liable for the penalties under the Washington Consumer Protection Act if a plaintiff proves each element under the statute?[4]

6. Finally, what kind of equitable solution will be fashioned in the "foreclosure fiasco" across state, federal and global jurisdictions that do not give a borrower a windfall but do not allow unscrupulous lending practices to go unremedied?[5]

1. Restraint on MERS foreclosures will likely occur unless MERS has provided a perfect chain of title for the assignments regarding the Note. Someone with the actual right, not the contorted and unlawful nominal beneficiary, such as MERS, has to give the authority to foreclose. The Court did make reference to judicial foreclosures as a means to determine who has the right to foreclose. That process is available to MERS but it will still have to produce a perfect chain of the right to foreclose.[6] "The securitization process was happening so fast that companies were often not keeping good records. The distinction between the loan servicer and the actual note holder is also going to cause problems—it is another layer of record keepers who …often didn't keep very good records. …I doubt that MERS has even been privy to all the securitizations and assignments. MERS probably doesn't know who has the Note." [7]

2. The ultimate determination of the Bains vs. MERS case at the Federal District Court level may or may not answer the question of retroactive application. The Washington Supreme Court dodged it. Nevertheless, it is rational and consistent with Washington law that if a person/entity uses illegal, fraudulent of deceptive procedures to acquire gain, that gain can be reversed and reinstated to the proper party and all consequential damages, including attorney's fees and costs in some instances, can be assessed against the perpetrator.[8]

3. The Washington Foreclosure Fairness Act of 2011 has implemented a "good faith" requirement that the lender attempt to modify the loan in a practical manner. This has caused no small change in a process that heretofore rendered no one available who could negotiate a modification. The lights were on but no

[4] The Bains vs. MERS Court recited the elements of the CPA cause of action and though it did not rule outright to support such a claim in this specific case, it made it look like a promising field of work for plaintiff's lawyers.

[5] Quid pro quo is an underlying premise of legal and equitable justice. Though I am a plaintiff's lawyer and "feel the pain" of the millions who were taken in by this predatory lending climate over the past decade, it is still not right for homeowners to escape paying a fair market value for their home on practical and reasonable terms. Why the lenders will not come to the table to discuss a "global" resolution is beyond me; they will become property owners and managers, with all those attendant costs, rather than bankers.

[6] It is more than a little ironic that the profits to be realized by the immediate "liquidity" created by the unlawful MERS system may ultimately cost the lenders more than they realized by their cleverness.

[7] Eric C. Nelson, memo after the Court decision, supra.

[8] There is no need for a long recitation of cases or treatises on this basic human principal of justice.

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one was home. Specifically, the Bains Court stated "There is no evidence in the record or argument that suggests that MERS has the power to 'reach resolution and avoid foreclosure' on behalf of the note holder, and there is considerable reason to believe it does not." (At page 20.) It can be expected that if a purported note holder is engaged in a Foreclosure Fairness Act mediation that the presence of MERS in the situation will expose the purported note holder to considerable pressure to modify the debt along reasonable and practical terms[9] or it will be in violation of "good faith" by the very fact that MERS was involved. The result should be very good for borrowers with a MERS situation in mediation.

4. It is likely that MERS foreclosures will grind to a halt. The full extent of the impact of Bains vs. MERS will not be known until the Federal District Court action is decided and all appeals exhausted.[10] It is unlikely that counsel for MERS will subject themselves to Rule 11 sanctions in addition to the liability for lack of good faith required for all trustees towards the beneficiary as well as the borrower.

5. The Washington Attorney General believes that the DOT used by MERS purports to transfer its beneficial interest on behalf of *its own* successors and assigns, and not on behalf of any principal. The Court found that it is "deceptive to claim authority when no authority existed and to conceal a true party in a transaction." (At page 36.) The Court also held that "characterizing MERS as the beneficiary has the capacity to deceive and thus, [for the CPA question] presumptively the first element (of a CPA claim) is met". (At page 37.) "Because MERS is involved in an enormous number of mortgages in the country (and our state)….it would have a broad public impact", thus satisfying that element of the CPA. The question of "injury" will have to be determined on an individual basis, but the Court gave several common fact patterns that would qualify as "injury" and each of them is present in almost every DOT and Note foreclosure scenario: to wit, disputes may need to be resolved with the note holder, legal protections may need to be taken advantage of and expressed to the note holder, etc. The Supreme Court has opened the door for claims against MERS and its cohorts under the Washington Consumer Protection Act.[11]

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[9] "Reasonable and practical terms" would be along the lines of the Net Present Value equation that has been developed for modification negotiation, though the lender still holds the upper hand in these negotiations. I believe that a reasonable and practical solution is to modify the loan so that the fair market value of the property is established as the base for the debt. Any substantial down payment by the borrower would be credited against this baseline. Then the debt, the fair market value minus the down payment, would be extended to a term of years, such as 30 or 40 years, and charged interest at no more than 3% that will reduce the monthly payment to a level that the homeowner can actually afford. See footnote 3.

[10] This author has not contacted counsel to learn the schedule for the Federal District Court proceedings.

[11] The Bains Court, at page 13, describes the traditional system of recordation and how MERS and company invented a way to "circumvent these procedures" and now find it impossible to identify the current note holder who may have the right to enforce the note and deed of trust. They have created their own noose (fraud and misrepresentation) in pursuit of grandiose profits. Irony abounds in this case.

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6. The San Bernardino Board of Supervisors came up[12] with a novel idea to address the ultimate or global issues surrounding the inequities of both the fraudulent and deceptive practices of MERS and company, but to also address the inequity of homeowners remaining in possession of or gaining quiet title to property for which they have not paid. Under the "plan" the County would take ownership of underwater mortgages (the title to the property) by eminent domain and then assist the homeowner into a new "reasonable and practical" mortgage owned by the County. The County would publish its notice of intent to exercise eminent domain and the burden of proof would be upon MERS or any other claimant to establish title in a court proceeding. Under Bain, the title could likely not be proved and would pass to the County or the Land Bank set up by County. The property could then be sold, free and clear of all old interests, and bring financial income[13] and stability to the County that has been hard hit by the financial crises. In some respects this approach may provide the answer to the "global" question about how we, as a country, are going to deal with these underwater and oftentimes abandoned properties before they become a public condemnation expense.[14]

Conclusion

Under the deed of trust act, the beneficiary must hold the promissory note. Simply put, if MERS did not own the note, it was not a legal beneficiary, regardless of the purported contract and agency language utilized on the face of the DOT. MERS was not empowered to contract around Washington statutes.

A Consumer Protection Act violation may very well sit, depending upon the specific facts of each case, in a MERS DOT non-judicial foreclosure situation.

Finally, it is this author's opinion that something, perhaps the San Bernardino approach of eminent domain followed by a relending on practical terms to the homeowner, or federal legislation and administrative implementation that "modifies loans", is needed or the country, let alone Washington State, will face another series of economic crises as homes deteriorate and become a burden on the public at large. The insurance fraud tactics of the major lenders will run their course and one day they will have to deal with the reality of what they have created. Without some sort of global answer, major lenders are still in jeopardy.

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[12] The concept was actually brought before the Board by Mortgage Resolution Partners, a private equity firm, who were roundly dismissed from the discussions as being too close of cousins to the entities that created the problems in the first place.

[13] Several Washington attorneys have been bantering back and forth on the Real Property, Probate and Trust section list serve about the missed recording fees that MERS diverted to itself. The recording fees are "fees for services" so nothing filed, nothing paid. However, this aspect of the negative impacts of MERS could warrant further investigation.

[14] Just as it would be nearly impossible to determine who has the right to foreclose, it will also be impossible to figure out who to bill for condemnation and demolition costs.

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