The Note Is All a Lender Needs to Foreclose

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Recently, the issue of a lender's authority and right to pursue foreclosure on defaulted residential mortgage loans has become a subject of national interest. It is at the heart of the $25 billion settlement agreed to recently between the Federal government, 49 state attorneys general and the nation's five largest loan servicers.

Mortgage foreclosure practices are also the focus of suits brought by certain state attorney generals against several major banks in the past few months. The propriety of mortgage foreclosure processes are defenses commonly raised by defaulting borrowers in contested foreclosure litigation.

The courts are clogged with people asking the same question: does *this* bank have the right to foreclose on *this* home?

Two documents are critical to a residential lending relationship, and therefore to foreclosure on a defaulting borrower's loan: the note and the mortgage (or deed of trust).

The note identifies the amount of the loan, and the repayment terms. The mortgage provides security for the loan. To have the authority to foreclose the mortgage (what lawyers call "standing"), a plaintiff must be the "holder" or "assignee" of the note. In the current environment where mortgage loans have frequently been bought, sold and securitized, confusion has sometimes ensued over who is the proper party to commence the foreclosure — or at least over a bank's ability to prove its authority.

Counsel for borrowers often demand that lenders prove that *both* the note and mortgage are held by the foreclosing lender before a residential mortgage foreclosure may proceed, and some courts have, mistakenly, agreed. Certain courts have gone so far as to say that lenders who cannot provide exacting evidence of when and how the note and mortgage were transferred to the bank cannot maintain a foreclosure action, thereby allowing borrowers to reside at the mortgaged home "payment free," without making mortgage payments and without the risk of foreclosure.

Proving the right to foreclose, however, should not be as difficult as those attorneys and courts claim. Under the Uniform Commercial Code, a note is a negotiable instrument (just like a check), freely transferable by endorsement to a specific entity or by physical delivery of the note endorsed in "blank" to a new party, who becomes the "holder" of the note. The holder of the note (or check) whether or not he is the owner of the instrument can enforce it. Thus the party who "holds" the note has standing to enforce the note. This is no different from a check. You can receive a check payable to you and then endorse it by signing the back. If a check is payable to you, your signature on the back makes the check enforceable by any person in possession.

Here, however, is the important part when it comes to the transfer of a note. When a note has been transferred, the mortgage securing it *automatically* follows. This rule is codified in the UCC section 9-203. The maxim that the "mortgage follows the note" has been followed in most states, including Florida, New York, Ohio, Texas and California.

Though UCC law is long established, it is often forgotten or ignored in the mortgage foreclosure context. Applying this simple, clear rule to foreclosure cases would quiet much of the uproar about who has the right to foreclose because the focus would, correctly, be on the note *only*.

Disputes about whether mortgages were properly assigned to the foreclosing lender by Mortgage Electronic Registration System — commonly known as MERS — could be put to the side. Lenders designate MERS as their nominee and grant MERS the authority to transfer mortgages within its network of lenders, without recording the assignments publicly. MERS has become a favored whipping boy of borrower lawyers who regularly challenge the validity of mortgage assignments executed by or on behalf of MERS. But an assignment by MERS, and whether it legally transfers the mortgage or not, is irrelevant because possession of the endorsed note is *all* that matters.

Another issue that arises repeatedly is the claim that assignments of mortgages were "robo-signed." Borrowers claim that the mortgage assignments are invalid because they were improperly notarized or signed by someone without verifying the facts in the document. Again, this issue regarding the assignment of the mortgage does not affect the legal right of the lender to foreclose if the UCC is followed.

These issues regarding assignments and documentation of mortgage transfers have become serious distractions in many cases and on the national political stage, causing delay and expense for foreclosing parties, burdening courts unnecessarily and wastefully expending taxpayer money to address an "issue" which is not an issue at all.

Lawyers and judges need to keep their eye on the ball, and here all that is needed to prove the right and authority to foreclose is proper transfer and physical possession of the loan note.

Lenders would be well-served to check their files and confirm that they have possession of the original note, either endorsed in blank or endorsed specifically to them, before commencing their next foreclosure action. If a lender can walk into court waiving the original note, the lender has standing to foreclose and nothing about the assignment of the mortgage, robo-signing, faulty notary stamps, and so on, matter. If the lender has possession of a properly indorsed note, the law will do the rest.

David Dunn and Allison J. Schoenthal are partners at Hogan Lovells.