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No. 68177-01

DIVISION I, COURT OF APPEALS
OF THE STATE OF WASHINGTON

WMC MORTGAGE CORP., a California corporation,
Appellant

v.

SCOTTY'S GENERAL CONSTRUCTION, INC., A WASHINGTON
CORPORATION,
Respondent

ON APPEAL FROM KING COUNTY SUPERIOR COURT
(HON. MARY E. ROBERTS)

BRIEF OF APPELLANT

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I. INTRODUCTION

This appeal concerns a recorded mortgage that has incontestable priority over a junior construction lien. Appellant WMC Mortgage Corporation (WMC) was the original Beneficiary of the mortgage. The loan and deed of trust were assigned by WMC to Deutsche Bank National Trust Company (Deutsche) under the Pooling and Servicing Agreement dated September 1, 2005, GSAMP Trust 2005-WMCI. Deutsche appointed Northwest Trustee Services, Inc. (Northwest) as successor trustee under the Deed of Trust on February 26, 2010. Litton Loan Servicing, LP (Litton) was further appointed as Attorney in Fact for Deutsche. Northwest proceeded with a Trustee's Sale and delivered Deutsche a Trustee's Deed on June 25, 2010. Deutsche, through Litton, subsequently transferred the property in question to Shiad Investment, L.L.C. by way of Bargain and Sale Deed on August 23, 2010. That Deed was recorded at the King County Auditor under number 20100825001030 on August 25, 2010.

The construction lien was foreclosed in a prior suit brought by respondent Scotty's General Construction, Inc. (Scotty's). Neither Deutsche nor Litton was a party to the prior suit.

WMC is appealing from the December 18, 2011 denial of the Motion to Set Aside the Default and Vacate the Judgment requested under

Civil Rule 55(c) and CR 60. WMC also seeks a declaratory judgment that the mortgage is first in time and first in right over the construction lien. In response to WMC's motion, Scotty's contended WMC was bound by the prior suit and default judgment. Misled by Scotty's prior judgment awarding more relief than requested or to which it was entitled, the trial court denied WMC's motion to vacate the judgment. The dismissal was a clear and prejudicial error, and an abuse of discretion resting on untenable grounds. There are three black letter rules of substantive law and one rule of procedural law that are dispositive of the issues presented in this appeal.

The first substantive dispositive rule is a foreclosure decree cannot bind a person who has an interest in the property and was not a party to the suit.¹ The rule conclusively applies in this case. Deutsche was assigned the mortgage. Deutsche was not joined as a party in the quasi in rem foreclosure suit, so it is not bound by the decree. Due process was also denied when Scotty's failed to provide to the designated grantee of record notice of the suit.

The second substantive dispositive rule relates to the first-in-time priority under the "race-notice" recording statute and the priority provision

¹*Diversified Wood Recycling, Inc. v. Johnson*, 161 Wn. App. 859, 902-03, 251 P.3d 293, 308 (2011); *id.* at 902 & n. 2 (using the more inclusive title, construction liens, for mechanics' and materialmen's liens under Chapter 60.04 RCW).

of the construction lien statute.² When a mortgage is recorded before the effective date of a construction lien, the mortgage is senior to the construction lien. In this case, the purchase money mortgage was recorded almost two years before the effective date of the construction lien. Therefore, the mortgage is first in time and first in right.

The third substantive dispositive rule is “[a] mortgage having once obtained priority of record does not lose its place by being held by anyone under an unrecorded assignment.”³ The mortgage did not lose its priority when it was transferred through the delivery of the note. The governing maxim is: the mortgage follows the note. Washington law has followed this maxim since 1908.⁴ Here, the assignment instrument was recorded over a month before the judgment was entered in the lien foreclosure suit. The mortgage continues to have priority over the construction lien, just as in *Keltch v. Don Hoyt, Inc.*, 4 Wn. App. 580, 583, 483 P.2d 135 (1971).

The dispositive procedural rule is that “The Supreme Court of this State has long voiced a strong preference for resolution of cases on their merits over default judgments.” *Morin v. Buris*, 160 Wn.2d 745, 161, P3d

² *Zervas Group Architects, P.S. v. Bay View Tower LLC*, 161 Wn. App. 322, 325 n. 7, 254 P.3d 895 (2011); RCW 60.04.061 (entitled “Priority of Lien”).

³ *Miller v. Am. Savings Bank & Trust Co.*, 119 Wash. 243, 205 P. 388 (1922) (“a mortgage ... passes to the assignee by assignment of the debt without any formal assignment of the mortgage itself,” quoting *Jones on Mortgages* (7th ed.), § 525, p. 828).

⁴ *Bartlett Estate Co. v. Fairhaven Land Co.*, 49 Wash. 58, 63, 94 P. 900 (1908); Restatement (Third) of Property, Mortgages § 5.4(a) (1997). See Reporters’ Note to “Transfer of the obligation also transfers the mortgage” (citing *Bartlett Estate Co.*, 49 Wash. at 63 (1908)).

956 (2007); See Also *Hull v. Vining*, 17 Wash. 352, 360, 49 P. 537 (1897). The Court will, in fact, liberally set aside default judgments pursuant to CR 55(c) and CR 60 and for equitable reasons in the interests of fairness and justice. *Morin, Id.* Courts prefer to give parties their day in court and have controversies determined on their merits. *Griggs v. Averbeck Realty, Inc.*, 92 Wn.2d 576, 581, 599 P.2d 1289 (1979) (Quoting *Dloughy v. Dloughy*, 55 Wn.2d 718, 721, 349 P.2d 1073 (1960)). Here, a court has yet to hear and consider the merits of this action, since no opportunity has been afforded outside the procedural conundrum created by Scotty's in initiating its action with faulty notice and service to all necessary parties.

The default and overreaching judgment applying to WMC cannot preclude this case being decided on the merits. At the time of Scotty's action, Deutsche had both the note and a formal assignment of the mortgage. With either the note or the assignment, Deutsche would have a prima facie claim for declaratory relief. Possessing both, Deutsche has an incontestable claim for declaratory relief.

The title records reflect the borrower defaulted on the mortgage. There is a foreclosed construction lien claiming priority over the mortgage. The priority dispute is ripe for declaratory relief. The denial of WMC's motion to vacate was a clear and prejudicial error and an abuse of discretion, which must be reversed. Notwithstanding the procedural

question of whether this Court ought to vacate Scotty's Judgment against WMC, and because priority is an issue of law, Deutsche requests this Court also decide that legal issue on appeal to avoid further confusion upon remand.

For the purpose of this brief, the more general term (mortgage) will be used to include a deed of trust.

II. ASSIGNMENT OF ERROR

Assignment of Error

No. 1. Did the trial court err in denying a Civil CR 55(c) and CR 60 motion to set aside and vacate the judgment?

Issues Pertaining to the Assignment of Error

No. 1. Deutsche holds the mortgage note and the recorded assignment of the mortgage.⁵ Do the holder of the mortgage note and transferee of the mortgage have standing to bring a declaratory action regarding the priority of the mortgage over a junior construction lien?

No. 2. The grantee and trustee of the mortgage were not named as parties in the construction lien foreclosure suit, a quasi in rem action. Is the transferee of the mortgage note and the mortgage bound by the default foreclosure decree?

⁵ See Permanent Editorial Board of the UCC Committee Report *Application of the Uniform Commercial Code to Selected Issues Relating to Mortgage Notes* (Nov. 14, 2011) (using term, mortgage note), Appendix A.

No. 3. Scotty's failed to provide notice of the suit to the grantee of record for the mortgage, which is a clearinghouse that tracks the transfers of beneficial interests in the mortgage. Did the contractor comply with the due process requirement to provide notice to interested persons whose identities are reasonably ascertainable?

No. 4. The chain of title gave Scotty's constructive notice of the prior recorded mortgage and later of the recorded assignment of the mortgage. Does the assignment take the priority of the mortgage?

No. 5. The mortgage note was transferred to a lender. Does the status of MERS as the mortgage's original beneficiary, acting as the nominee for the lender and the lender's assigns, alter the effectiveness of the mortgage and its priority?

No. 6. Scotty's was not involved in any part of the loan/mortgage transaction. Does a party that was not involved in any part of the loan/mortgage transaction have standing to assert a claim challenging the status of MERS as the mortgage's original beneficiary, acting as the nominee for the lender and its assigns?

No. 7. As a matter of law, does the deed of trust assigned to Deutsche have priority of record over any interest of Scotty's in Parcel 062205-9056-07?

No. 8. Does this Court have sufficient grounds to set aside and vacate the Order of Default and Judgment against WMC?

III. STATEMENT OF THE CASE

WMC asks this Court to set aside the order denying its motion to vacate the judgment against it, and further requests this court grant declaratory relief establishing lien priority over the property in question in its favor. A proceeding to vacate or set aside a default judgment is equitable in character, and the relief sought or afforded is to be administered in accordance with equitable principles and terms. *Roth v. Nash*, 19 Wn.2d 731, 144 P.2d 271 (1943). Higher courts are, in fact, less likely to reverse a trial court decision that sets aside a default judgment than a decision that does not. *Colacurio v. Burger*, 110 Wn. App 488, 494-95, 41 P.3d 506 (2002), review denied, 148 Wn.2d 1003, 60 P.3d 1211 (2003).

There are two parcels at issue. The reporter's index (by parcel number) for Parcel 9056 refers to Scotty's lien, but the index for Parcel 9036 does not refer to Scotty's lien. The former parcel is the one encumbered by Deutsche's mortgage. A subsequent and separate appeal has been filed regarding the mortgage that CentralBanc Mortgage Corporation (now Bank of New York Mellon, hereinafter "BNY Mellon") originated and which encumbers Parcel 9036.

A. When the property owner acquired two parcels, she granted three purchase money mortgages.⁶

The property owner, Gloria Pazooki, acquired two parcels in Kent, Washington.⁷ As part of the purchase of property for \$815,000,⁸ the property owner received three loans totaling \$739,270. The three loans were secured by three mortgages recorded on the same day in June 2005.⁹

First, the property owner received a \$321,270 loan from WMC secured by a mortgage encumbering both parcels. CP 92-189, Exhibit D, WMC Motion to set aside Judgment and Default. The recorder's index lists WMC Mortgage as the associated person. That listing satisfies the recorder's statutory duty to list grantees on the recorder's index. RCW 65.04.050 (requiring a recording index); RCW 65.04.015(5) (defining grantor/grantee as "the names of the parties involved in the transaction used to create the recording index."). The form document is a "Fannie Mae/Freddie Mac Uniform Instrument." The mortgage at page 1 states: "MERS is a separate corporation that is acting solely as nominee for

⁶ The Restatement (Third) of Property, Mortgages § 7.2 (1997) defines a "purchase money mortgage" as a "mortgage given to a vendor of the real estate or to a third party lender to the extent that the proceeds of the loan are used to: (1) acquire title to the real estate."

⁷ Parcels Nos. 062205-9036 and 062205-9056. The street address is 20541 92nd Ave. S., Kent, WA.

⁸ Instrument No. 20050607001225 (Parcel 9036 for \$440,000) and Instrument No. 20050607000348 (Parcel 9056 for \$375,000).

⁹ Instrument No. 20050607000349 (WMC deed of trust), Instrument No. 200506070001227 (MERS deed of trust); Instrument No. 20050607001228 (Central Bank deed of trust).

Lender and Lender's successors and assigns. **MERS is the beneficiary under this Security Instrument.**" (Bold in original). CP 92-189, Exhibit B, WMC Motion to Set Aside Judgment and Default. The recorder's index also identifies MERS as the name associated with the mortgage.

Second, the property owner received a \$352,000 loan from CentralBanc Mortgage Company secured by mortgage encumbering one parcel. (This is the mortgage later assigned to BNY Mellon.) The mortgage also names MERS as the beneficiary. CP 92-189, Exhibit D, WMC Motion to Set Aside Judgment and Default.

Third, the property owner received a \$66,000 junior loan from CentralBanc secured by a mortgage covering one parcel. The mortgage at page 2 identifies "the Beneficiary, Mortgage Electronic Registration Systems, Inc. ("MERS"), (solely as nominee for Lender, as hereinafter defined, and Lender's successors and assigns)." CP 92-189, Exhibit D, WMC Motion to set Aside Judgment and Default.

B. More than four years after the recording of the mortgages, Scotty's filed a lien foreclosure suit. The suit did not name as a party the grantee or the trustee of the mortgage at issue.

On December 29, 2008, Scotty's recorded a construction lien. The lien claimed work was started in May 2007. In February 2009, Scotty's sued

to foreclose the lien. CP 1.¹⁰ Scotty's did not record a lis pendens, so persons reviewing title records had no notice the lien was perfected through the filing of a lawsuit. The complaint identifies the lien but not particular instruments recorded against the property.¹¹ The complaint names the property owner and her spouse and another couple as defendants. CP 1. The complaint also names WMC Mortgage Corp. and Centralbanc as companies claiming interests in the property.¹² The complaint fails to make reference to any assignments of the mortgage; it "reserves the right to add additional parties who claim an interest in the real property as those parties become known," but it is uncontested those parties were never added.¹³ The complaint does not name MERS, which was listed in the recorder's index as the grantee of the mortgage later assigned to Deutsche.¹⁴ Nor does the complaint name the mortgage's trustee.¹⁵

Although WMC never answered the complaint, Scotty's filed a case management pleading representing all mandatory pleadings had been filed.

¹⁰ Scotty's was paid approximately \$250,000. See Finding Nos. 12-13, Findings of Fact and Conclusions of Law in *Scotty's v. Pazooki*, King County Case No. 09-2-07414-3, Dkt. No. 31, CP 31.

¹¹ Compl. ¶ 4.1 (identifying recording number), CP 1.

¹² *Id.* ¶¶ 1.4, 1.5, 8.3.

¹³ *Id.* ¶¶ 1.2-1.6, 8.4.

¹⁴ *Id.* ¶¶ 1.2-1.6, CP 1.

¹⁵ *Id.*

C. Scotty's had constructive notice (if not actual notice) of the assignment of a mortgage to Deutsche – more than four weeks before judgment was entered in the foreclosure suit.

WMC moved in the foreclosure suit to vacate the default judgment, which had been entered against it. In response to that motion, Scotty's submitted a letter as evidence in support of the default judgment. The letter is dated July 14, 2010 and was sent by Scotty's counsel to the trustee and assignee of the WMC mortgage, Deutsche Bank National Trust Company. CP 42. Scotty's complained that, although it had a recorded lien, Deutsche Bank and its trustee had not given Scotty's notice of the trustee's sale. (That is ironic because this suit arises from Scotty's failure to give notice to MERS and Deutsche of the foreclosure suit, although they had recorded interests in the property.) Explaining how Scotty's discovered the trustee's sale, Scotty's brief states: "In the beginning of July, 2010 in preparation for trial, counsel for Scotty's discovered that in April, 2010...WMC transferred title to Deutsche Bank National Trust." CP 42.

His letter also refers to the trustee's deed resulting from the foreclosure sale by Deutsche. The trustee's deed to Deutsche was recorded June 25, 2010. Four days after the recording of that deed, there was also notification in the title record on June 29 of another prior assignment of a mortgage to BNY Mellon in the very same county records. The recorded assignment to Deutsche precedes the date of the letter from Scotty's

counsel by two weeks. (There is a twenty-four hour lag between recording of a document and when a document is available for on-line viewing. Appendix B.¹⁶) In short, when Scotty's reviewed the county's website on July 13, an instrument recorded fourteen days earlier was listed – namely the assignment to Deutsche, recorded on June 25, 2010.

By this chain of events, it is undeniable that Scotty's had actual notice of the assignment of Deutsche's mortgage. Once the assignment to Deutsche was recorded, Scotty's had actual notice that WMC did not control the mortgage any longer. Yet, Scotty's proceeded to prepare and obtain an overreaching order for default against all parties having an interest in the property.

Scotty's filed a declaration of service on WMC in its foreclosure suit. CP 1. The trial court entered a default judgment, along with findings and conclusions drafted by Scotty's. CP 31. Those findings and conclusions make no reference at all to the recorded mortgages, the assignments, or even the more recent trustee's deed conveying the property owner's interest in Parcel 9056 to Deutsche. CP 31. The order provided that "Scotty's interest in the property was superior to the interest of all defendants and all parties which claim to have acquired an interest

¹⁶Frequently asked questions, How long is the lag between when the document is recorded and when it is available for viewing. www.kingcounty.gov/business/Recorders/FAQ/, Appendix B. *See also* RCW 65.08.070 ("An instrument is deemed recorded the minute it is filed for record.").

subsequent to May 7, 2007....” CP 31. The judgment authorizes Scotty’s to foreclose against “any right, title, and interest acquired by and person subsequent to May 7, 2007.” CP 31. Interestingly, this order grants Scotty’s far more relief than it requested in its Complaint, where the only relief requested was “for foreclosure of Plaintiff’s lien in favor of the Plaintiff, Scotty’s, and against the interest of the each of the Defendants with a valid claim to an interest in the property and each of them **as they existed, at the time of commencing of the work and the furnishing of the material under said contract...**and against the interest of any person or persons claiming under them, and against any right, title and interest **subsequently acquired by Defendants ...**and for an Order declaring the interest of Plaintiff, Scotty’s in the real property superior to all other interests, **by sale and the manner provided by law....** CP 1.

Simply put, the judgment grants Scotty’s more relief than they are entitled to by law. There is simply no authority offered by Scotty’s that can possibly place it ahead of all others, since not all others are named. WMC is not Deutsche. CentralBanc is not BNY Mellon.

D. WMC moved to vacate the judgment and have the case decided in favor of WMC on the merits.

As stated above, the property owner was in default on the purchase money mortgages. Almost five months before the foreclosure judgment,

Deutsche Bank caused a notice of trustee's sale for Parcel 9056 to be recorded, and the property was transferred to Shiad Investment, L.L.C. by way of Bargain and Sale Deed on August 23, 2010. That Deed was recorded at the King County Auditor under number 20100825001030 on August 25, 2010.

Subsequently, upon receiving notice of entry of Scotty's default judgment, WMC Mortgage moved in the principal foreclosure suit to vacate the default judgment entered against it. In response to the motion to vacate, Scotty's raised the argument that MERS never had an interest in the property to convey to Deutsche Bank and was not a required party to foreclose the construction lien, along with other grounds. The trial court denied the motion to vacate, and WMC timely appealed in early January 2012. CP 48.

BNY Mellon initiated a similar process, causing the recording of the assignment of the mortgage for Parcel 9036, and the notice of trustee's sale. In that instance, the notice of trustee's sale was recorded eleven days before the default judgment was entered on August 2, 2010.

The recording of the trustee's notice of sale carries with it the presumption that the trustee "had proof that the beneficiary is the owner of any promissory note or other obligation secured by the deed of trust" RCW 61.24.030(7)(a) (requiring such proof "before the notice of trustee's sale is recorded, transmitted, or served"). When the property owner

did not cure the default here, Deutsche's sale proceeded. After the trustee's sale, the trustee issued a trustee's deed confirming Deutsche's possession of the note.

As discussed briefly above, six months after the default judgment was entered in the construction lien foreclosure suit, BNY Mellon brought an independent suit for a judgment declaring that its mortgage is superior to Scotty's interest and other relief. The trial court granted Scotty's pre-trial motion to dismiss in that action. BNY Mellon has timely filed an appeal in that action under King County Cause No. 11-2-05908-1 KNT, and is further seeking declaratory relief from this court on the issue of lien priority under No. 67370-0-I.

IV. ARGUMENT

A. Standard of Review.

On appeal, a trial court's disposition of a motion to vacate will not be disturbed unless it clearly appears that it abused its discretion; abuse of discretion is less likely to be found when a default judgment is set aside. *Lindgren v. Lindgren*, 58 Wn. App. 588, 595, 794 P.2d 526, 531 (1990) (citing *Griggs v. Averbek*, 92 Wn.2d at 582, 599 P.2d 1289). Abuse of discretion means that the trial court exercised its discretion on untenable grounds or for untenable reasons, or that the discretionary act was

manifestly unreasonable. *Coggle v. Snow*, 56 Wn. App. 499, 507, 784 P.2d 554.

B. There are sufficient grounds to vacate and set aside the Order of Default and Judgment against WMC.

As stated in the introduction to this brief, there is one black letter rule of procedural law that is dispositive to this appeal – “Default judgments are disfavored, and therefore, a trial court should ‘exercise its authority ‘liberally, as well as equitably, to the end that substantial rights be preserved and justice between the parties be fairly and judiciously done.’ ” *Griggs*, 92 Wash.2d at 582, 599 P.2d 1289 (1979) (quoting *White v. Holm*, 73 Wash.2d 348, 351, 438 P.2d 581 (1968)).

The Court has two primary methods by which it can undo a default. The first is Washington State Superior Court Civil Rule 55(c)(1), which states, “For good cause shown and upon such terms as the court deems just, the court may set aside an entry of default and, if judgment by default has been entered, may likewise set it aside in accordance with rule 60(b). The second is Superior Court Civil Rule 60(b), which provides in pertinent part, “On motion and upon such terms as are just, the court may relieve a party or his legal representative from a final judgment, order, or proceeding for the following reasons:

- (1) Mistakes, inadvertence, surprise, excusable neglect or irregularity in obtaining a judgment or order;

- (9) Unavoidable casualty or misfortune preventing the party from prosecuting or defending;
- (11) Any other reason justifying relief from the operation of the judgment.” CR 60(b)

The motion shall be made within a reasonable time and for reasons (1)... not more than 1 year after the judgment, order, or proceeding was entered or taken. CR 60(b).

So although Rule 55 makes “good cause” the standard by which a court can set aside an **entry** of default, the rule also clearly refers to Civil Rule 60(b) for relief from an entry of a default **judgment**. CR 55(c) [Emphasis added]. Rule 60(b) provides the means to relief from default judgments under specific conditions. Further, courts are not bound to consider just good cause, and uniformly also consider whether defendant has a meritorious defense. *Id.*, (citing 10 C. Wright, A. Miller, & M. Kane, *Federal Practice & Procedure* § 2694 (1983) and *Falk v. Allen*, 739 F.2d 461, 463 (9th Cir. 1984)).

“The different treatment of default entry and judgment by Rule 55(c) frees a court considering a motion to set aside a default entry from the restraints of Rule 60(b) and entrusts determination to the discretion of the court.” *Hawaii Carpenters’ Trust Funds v. Stone*, 794, F.2d 508, 513 (9th Cir., 1986) (Discussing the Federal Rule of Civil Procedure 55(c), but because the Washington rules were based on the federal rules, federal

court interpretation of the federal rules is highly persuasive in determining the effect of Washington's rules. See *American Discount Corp. v. Saratoga W., Inc.*, 81 Wash.2d 34, 499 P.2d 869 (1972)).

As a practical matter, however, when considering a motion to set aside a default entry, the parallels between granting relief from a default entry and a default judgment encourage utilizing the list of grounds for relief provided in Rule 60(b), including considering whether a defendant has a meritorious defense. *Hawaii*, at 713. The underlying concern for the court is to determine whether there is some possibility that the outcome of the suit after a full trial will be contrary to the result achieved by the default. *Id.* (citing Wright & Miller, at § 2694).

The above distinction is important in this case because, as of this date, we are past one year from entry of the April 16, 2009 and August 2, 2010 Orders on Default and Default Judgment. However, the Court is not bound by that one-year time limit in consideration of a Rule 55(c) motion. Nor is it bound by that time limit in consideration of a Rule 60(b) motion that falls outside the 60(b) (1), (2) or (3) conditions. CR 60(b). In *Sanderson v. University Village*, the court considered that very issue as it applied to Federal Rules of Civil Procedure 55(c) and 60(b) and held that a motion to set aside an entry of default is not governed by Rule 60(b) or by any express time limits, and thus may be set aside upon a showing of good

cause. *Sanderson v. University Village*, 98 Wash.App. 403, 410, 989 P.2d 587 (1999).

Courts have been even more specific on just how much discretion the court has in deciding Rule 55(c) motions since *Sanderson*. For example, in *Jesmore v. Frank*, an Order of Default and Default Judgment was taken against a defendant who claimed he had no notice of the proceedings, and also claimed a meritorious defense to the action. *Jesmore v. Frank*, 105 Wn. App. 1043 (2001). A motion to set aside the order of default was filed more than one year after the entry of default. The trial court found good cause under CR 55(c) and also went through the 60(b) analysis in ruling to set aside the default order and judgment. On appeal, the decision was affirmed and the court found it was well within the trial judge's discretion to set aside the default order. Specifically, the trial judge's analysis considered both the good cause requirement of Rule 55(c) and the 60(b) factors of having a meritorious defense, due diligence in responding to the claim and prejudice to the Plaintiff. The appellate court found no error in this analysis, stating "the court's oral decision is adequate when taken with its written order to establish the findings, underlying basis, and reasoning on these conclusions. *Id.* Lastly, the court's decision reflected its broad discretion in unwinding defaults in stating "CR 60(b)(11) affords relief if 'other reasons' justifying relief

exist. These ‘other reasons’ are not bound by the one-year limit for relief under CR 60(b)(1).”

In this instance, then, WMC is asking the court to vacate the Judgment under CR 60(b)(9) and (11), which do not fall under any time limits. Second, WMC is asking the court to apply the good faith analysis of Rule 55(c) in consideration of WMC’s Motion to Set Aside the Order of Default, where the court is likewise not bound by any time limits. Here, the court can, in its discretion, apply the conditions enumerated in Rule 60(b)(1) as a roadmap to a ruling on whether to set aside the Order of Default and Default Judgment.

In looking to CR 60(b) (As both a roadmap for CR 55(c), and also for its own conditions for vacation of a default judgment), the test to be applied by a trial court in reviewing a motion to vacate a default judgment consists of four factors. The primary factors are: (1) the existence of substantial evidence to support, at least prima facie, a defense to the claim asserted; and (2) the reason for the party’s failure to timely appear, i.e., whether it was the result of a mistake, inadvertence, surprise or excusable neglect. The secondary factors are: (3) the party’s diligence in asking for relief following notice of entry of the default; and (4) the effect of vacating the judgment on the opposing party. *White v. Holm*, 73 Wn.2d 348, 438 P.2d 581 (1968); see also CR 55(c)(1) and CR 60(b)(1).

As can be gleaned from their designations as “primary” and “secondary” above, the four factors are not weighted equally. “The primary factors are the major elements to be demonstrated by the moving party, and they, coupled with the [latter two] secondary factors, vary in dispositive significance as the circumstances of the particular case dictate. Thus, where the moving party is able to demonstrate a strong or virtually conclusive defense to the opponent’s claim, scant time will be spent inquiring into the reasons which occasioned entry of the default....”. *White, Id.*

For the primary factor (a prima facie and meritorious defense), WMC points the court to the black letter rules outlined below in sections 1a, 1b and 1c. As to good cause under CR 55(c), a court looks in its analysis to whether a party can demonstrate excusable neglect and due diligence. *Estate of Stevens*, 94 Wn. App. 20, 30, 971 P.2d 58 (1999) (citing *Seek Sys. Inc. v. Lincoln Moving/Global Van Lines, Inc.*, 63 Wn. App. 266, 271, 818 P.2d 618 (1991)). All of the above arguments for vacation under CR 60(b) also apply to WMC’s excusable neglect and due diligence in responding to this action as soon as reasonably possible. On the same grounds, should the court not choose to vacate the default and judgment, the court should set aside the Order of Default based upon this showing of good cause. Again, this would open this case up again to be

decided on the merits, affording ample opportunity for the Plaintiff's to establish their case and the Defendant WMC to defend against it.

Here, in denying the motion to vacate, the trial court ignored the clear law and made a decision on untenable grounds. Since no written findings accompanied the order, it can only be surmised what the court's reasons were, but the underlying issues and merits of this case have yet to see the light of day. If it fails to take appropriate measures to assure service on all proper parties, a mechanics lien ought never to be able to jump ahead of a purchase money mortgage.

1. **Three black letter rules of law are dispositive of the issues presented on appeal.**

As stated in the introduction to this brief, there are three black letter rules of substantive law that are dispositive to this appeal. Those rules are set forth in subsection 1a, 1b, and 1c.

a. A foreclosure decree cannot bind a person who has an interest in the property and was not a party to the suit. The mortgage's grantee of record was not named as a defendant in the foreclosure suit. Therefore, the transferee of the mortgage (Deutsche) is not bound by the decree of foreclosure in the prior suit. CP 39, WMC's Mot. to Vacate at page 13 (arguing MERS should have been joined in the suit because it had

a recorded interest and RCW 60.04.171 does not specify what kind of recorded interest must be joined).

Scotty's has contended the construction lien foreclosure suit properly named all parties with an interest in the subject property as required by RCW 60.04.171 and that this motion to vacate should be denied. CP 42. That argument rests on the false assumption that the prior suit was an in rem action, when it actually was a quasi in rem action affecting only the specific interests joined in the suit. Again, Scotty's cannot be awarded more than it requested in its complaint or more than to which it is entitled by law.

The construction lien foreclosure suit does not affect the interests of persons who are not joined as parties to the suit. *Diversified Wood Recycling, Inc. v. Johnson*, 161 Wn. App. 859, 877, 251 P.3d 293, 308 (2011) (Diversified Wood I, as amended Jul. 11, 2011); *Diversified Wood Recycling, Inc. v. Johnson*, 161 Wn. App. 891, 903, 251 P.2d 908 (2011) (Diversified Wood II, May 16, 2011). In *Diversified Wood II*, this Court reaffirmed: "Actions to foreclose construction liens are 'quasi in rem,' i.e., they determine interests of *certain defendants* in a thing in contrast to a proceeding in rem which determines the interests of all persons in the thing." 161 Wn.2d at 902 (italics added). Deutsche was not one of those "certain defendants," nor was its specific interest (the mortgage) joined in the suit. Therefore, as a

matter of law its interest was not adjudicated. The law regarding the joinder of mortgagees has been clear and consistent since 1991.

In 1991 and 1992, there was “a comprehensive revision of the entire construction lien statute, chapter 60.04 RCW.” *Diversified Wood I*, 161 Wn. App. at 886. RCW 60.04.171 codifies the proposition “recognized in Washington decisions such as *Davis*, that the mortgagee’s interest cannot be affected by a lien foreclosure unless the foreclosing party joins the mortgagee as a party to the foreclosure.” *MB Constr. Co. v. O’Brien Comm. Center Assocs.*, 63 Wn. App. 151, 158, 816 P.2d 1274 (1991) (referring to *Davis v. Bartz*, 65 Wash. 395, 118 P. 334 (1911)). “*Davis* clearly stands for the proposition ... that foreclosure action which omits a mortgagee is void only as to the mortgagee.” 63 Wn. App. at 165.

RCW 60.04.171, entitled Foreclosure—Parties, states in pertinent part:

The court shall have the power to order the sale of the property. *In any action brought to foreclose a lien, the owner shall be joined as a party. The interest in the real property of any person who, prior to the commencement of the action, has a recorded interest in the property, or any part thereof, shall not be foreclosed or affected unless they are joined as a party.*

Diversified Wood I construes the italicized sentence as a “clarification and simplification of” the prior requirement of serving and joining “all necessary parties.” *Diversified Wood I*, 161 Wn. App. at 887-89. The new

requirement is to serve merely the property owner with the suit but not necessarily join the owner as a party. *Id.* The former 60.04.120 also required the joinder of other construction lien holders,¹⁷ but RCW 60.04.171 omits that requirement as part of the simplification of construction lien proceedings.

Another clarification and simplification is the underlined sentence in RCW 60.04.171 (preventing a “recorded interest ..., or any part thereof” from being “foreclosed or affected ... unless the [party] is joined”). It creates an optional remedy -- a suit *may* include a prior recorded interest but the prior “recorded interest in the property, *or* any part thereof, shall not be foreclosed or affected unless they are joined as a party.” RCW 60.04.171. Construing RCW 60.04.171 in *Diversified Wood II*, this Court ruled: “The consequence of [nonjoinder] is that the interest of a person not joined may not be foreclosed or otherwise affected.” 161 Wn. App. at 903.

Scott’s took a short cut here, and the law simply does not reward that behavior. RCW 60.04.171’s plain terms mandate that Deutsche’s “recorded interest” was not affected, because it was not “joined as a party” in the prior suit. RCW 60.04.171. The trustee’s recorded interest was not

¹⁷ See *MB Constr.*, 63 Wn. App. at 154 (stating former “RCW 60.04.120 mandates the joinder of parties who have prior recorded ‘claims of lien,’” ruling the provision did not resolve whether a mortgagee must be joined, and ruling mortgagee is not a necessary party to the foreclosure suit).

“affected,” because the trustee was also not “joined as a party.” MERS’ recorded interest was not “affected” (nor was “any part thereof” affected), because MERS also was not “joined as party.” *Id.* The failure to join those three parties meant the prior suit had no legal effect whatsoever on the mortgage at issue. As *Diversified Wood II* observes: “This is consistent with what happens in a judicial foreclosure of a mortgage: Clearly, due process requires a ‘day in court’ before property interests can be extinguished.”¹⁸ Deutsche did not receive its day in court. The lack of joinder and the lack of notice was a denial of due process. The holder of the mortgage note was a necessary party in any action determining rights relating to the security interest (mortgage). Notice was necessary to satisfy the due process requirement to apprise interested parties of the pendency of the action and their opportunity to be heard.

Due process requires notice be reasonably calculated under all circumstances, which includes notice to interested persons identifiable through “reasonably diligent efforts.”¹⁹ “Washington ... has what is

¹⁸ 161 Wn. App. at 903 (“*Valentine v. Portland Timber & Land Holding Co.*, 15 Wn. App. 124, 128, 547 P.2d 912 cited in 27 Majorie Dick Rombauer, *Wash. Practice: Creditors’ Rights Remedies—Debtors Relief* § 3.2 at 138 n. 7”). *Id.* (citing 18 William B. Stoebuck & John W. Weaver *Wash. Practice., Real Estate Judicial Foreclosure* § 19.2 at 374).

¹⁹ *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 314, 70 S. Ct. 652, 94 L. Ed. 865 (1950) (“notice reasonably calculated, under all circumstance to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections” is an “elemental and fundamental requirement of due process.”); *id.* (written and mailed notice required to beneficiaries of trust estates where names and

called a ‘grantor-grantee’ index for its recording system. Since indexing will be by names of the parties, it is critical they appear clearly.”²⁰ Here, the index specifies MERS as the grantee of record; MERS held legal title to some interest including one for notification and tracking purposes. CP 39, Exhibit B.²¹ In a quasi in rem proceeding “to determine the claims of specifically identified persons,” “[a]t minimum what is required is a mailed notice addressed to the person at his last reasonably discoverable address ...”²² But this minimal actual notice was not given to MERS.²³ There was also a separate procedure for notifying

addresses were known or could be reasonably ascertained); *Herring v. Texaco, Inc.*, 161 Wn.2d 189, 196-98, 165 P.3d 4 (2007) (regarding notice to known creditors whose identities are reasonably ascertainable through a reasonably diligent search).

²⁰ 18 Stoebeck & Weaver, *Washington Practice, Real Estate: Transactions* § 14.6 at 132, 134 (2004).

²¹ Deed of Trust at page 1 (“DEFINITIONS ... (E) MERS ... is a separate corporation that is acting solely as the nominee for the Lender and Lender’s successors and assigns. MERS is the beneficiary under this Security Agreement.”); CP 39. (“Borrower understands and agrees that MERS holds only legal title to the interests granted by the Borrower in this Security Agreement, but if necessary to comply with law or custom, MERS (as nominee for Lender and Lender’s successors and assigns) has the right: take any action required of Lender ...”). *Id.* at page 3.

²² Restatement (Second) of Judgments § 6 cmt. a (1982).

²³ “MERS is a private electronic database, operated by MERSCORP, Inc., that tracks the transfer of the ‘beneficial interest’ in home loans, as well as any changes in loan servicers. After a borrower takes out a home loan, the original lender may sell all or a portion of its beneficial interest in the loan and change loan servicers.” *Cervantes v. Countrywide Home Loans, Inc.*, 656 F.3d 1034, 1038 (9th Cir. 2011) “If the lenders sells or assigns the beneficial interest of the loan to another MERS member, the change is recorded only in the MERS database, not in the county records, because MERS continues to hold the deed on the new lender’s behalf.” *Id.* at 1039.

other persons with interests in the property (the recording of a lis pendens) which was not followed.²⁴

This Court may resolve this appeal on the basis of the statute without reaching the due process issue. “Any person” means “any” in the context of RCW 60.04.171, whose purpose is not to extinguish property interests but merely to “give[] the court some latitude in deciding whether and when to allow joinder of other persons with ... an interest in the same property.” *Diversified Wood I*, 161 Wn. App. at 889. RCW 60.04.171’s broad language protects “any person” who has a recorded interest – including the now transferred interest of MERS, and most certainly the recorded interest of BNY Mellon (with its substantial property interest).²⁵ The failure to name them was Scotty’s election/option under the simplified process for the foreclosure of construction liens. If not an election/option, then it was a mistake or irregularity in obtaining the judgment. The judgment is void or voidable due to the lack of adequate notice, the misrepresentation regarding joinder and mandatory pleadings.²⁶ Alternatively, it is no longer equitable that

²⁴ *United Savings & Loan Bank, v. Pallis*, 107 Wn. App. 398, 405, 27 P.3d 629 (2001) (stating “[t]he purpose of lis pendens is to give notice of pending litigation affecting title to real property, and not give notice that anyone who subsequently deals with the affected party will be bound by the outcome of the action to the same extent as if he or she were a party to the action”).

²⁵ Courts should be wary of creating a windfall for the mortgagor, or for a third-party like Scotty’s, and the forfeiture of the security. Restatement (Third) of Property, Mortgages § 5.4 cmt. e.

²⁶ *Accord*, CR 60(b)(1), (4), (5), (6), (11) (grounds for relief from judgment or order).

the judgment should have prospective relief, when the mortgage and grantee was not named in the suit, and there has been no foreclosure sale.

Scotty's is no newcomer to foreclosing security interests, and has no doubt encountered this situation before. Over the years, it has recorded more than 50 liens and other instruments in King County.²⁷ When the legislature amended the lien statutes, it made a title report a cost recoverable by a prevailing party.²⁸ Yet, Scotty's cost application in the prior suit did not seek the compensation for a litigation guaranty as a cost. But its attorney fee application refers to the review of a litigation guaranty and consideration of lien priority issues.²⁹ The contents of this undisclosed litigation guaranty is likely more evidence that could demonstrate that Scotty's had actual knowledge of the recorded interests that were not joined in the suit.

Coincidentally, Scotty's counsel is the same construction law firm that prosecuted the *MB Construction* appeal in 1999, which confirmed a mortgagee's interest cannot be foreclosed unless joined as a party to a

²⁷ www.kingcounty.gov/business/Recorders/RecordsSearch.aspx.

²⁸ RCW 60.04.181(3) (allowing recovery of "costs of title report ..."); *Wash. Asphalt Co. v. Boyd*, 63 Wn.2d 690, 696-97, 388 P.2d 965 (1964) (reversing award of such costs).

²⁹ Ex. A to Decl. of Hans P. Juhl in Supp. of Pl.'s Req. for Award of Fees (Aug. 2, 2010) (listing costs); Decl. at 4:1-16 (referring to Deutsche Bank notice of foreclosure sale, and tender of claim to Fidelity); Ex. A to Decl. at 1-2 (Jan. 29, Feb. 6, Feb. 10, Feb. 26, 2009; Apr. 9, 2009 referencing either a guaranty or lien priority issues). See *Diversified Wood II*, 161 Wn. App. at 897 & n. 4 (describing a litigation guarantee and comprehensive title report to ensure all persons and entities with an interest in the property are named in the suit).

foreclosure suit.³⁰ The dismissal of this case on the ground that the prior suit extinguished the mortgage is not supported by the facts and the decisions going back to *MB Construction*. Therefore, the dismissal should be reversed on the ground that the prior suit did not adjudicate Deutsche's interest. There is also a second independent ground for reversal.

b. Deutsche has first-in-time priority under the "race-notice" recording statute. An additional ground for reversal of the dismissal is because the mortgage has priority of record over the junior construction lien. A foreclosure sale to satisfy a junior lien will extinguish lesser liens and interests. But such a foreclosure sale will not extinguish a senior mortgage. Deutsche has such a senior mortgage and recorded a lis pendens to warn potential purchasers of its right. This declaratory suit is necessary to preserve its property right.

Deutsche argues here that Scotty's construction lien was not prior to its recorded mortgage. RCW 60.04.061's first-in-time rule of priority requires that when a mortgage is recorded before the effective date of a contractor's lien, the mortgage is senior to the contractor's lien. *Zervas Group Architects, P.S. v. Bay View Tower LLC*, 161 Wn. App. 322, 325 n. 7, 254 P.3d 895 (2011) (construing RCW 60.04.061 (entitled "Priority of Lien")). In this case, the purchase money mortgage was recorded almost

³⁰ 63 Wn. App. at 152 "Barokas & Martin, ... for petitioner.").

twenty months before the effective date of the construction lien.

Therefore, the mortgage is senior to the construction lien.

RCW 60.04.061 provides:

The claim of lien created by this chapter upon any lot or parcel of land shall be prior to any lien, mortgage, deed of trust, or other encumbrance which attached to the land after or was *unrecorded* at the time of commencement of labor or professional services or first delivery of materials or equipment by the lien claimant.

(Underline and italics added). Its plain terms create the priority of a lien over a deed of trust that is “unrecorded at the time of commencement” of lienable services. RCW 60.04.061 (adding underline). But RCW 60.04.61 does not apply in this case -- there was a recorded deed of trust at the time of commencement of lienable services. Therefore, the construction lien is junior to mortgage. For these reasons, there should be an affirmative ruling in favor of Deutsche on the seventh issue presented for review above. Issue No. 7 (“As a matter of law, does the deed of trust held by Deutsche have priority of record over any interest of Scotty’s in Parcel 062205-9056-07?”).³¹ The assignment of the mortgage did not forfeit its priority of record.

c. A mortgage’s priority of record is not lost when held by an unrecorded assignment. The third dispositive rule in this

³¹ See RAP 12.2 (“The appellate court may ... take any other action as the merits of the case and the interests of justice may require.”).

appeal is “[a] mortgage having once obtained priority of record does not lose its place by being held by anyone under an unrecorded assignment.” *Miller v. Am. Savings Bank & Trust Co.*, 119 Wash. 243, 250, 205 P. 388 (1922) (quoting *Jones on Mortgages* (7th ed.), § 525, p. 828). The assignment takes the mortgage’s priority of record over the construction lien.

The court of appeals reaffirmed this rule in *Keltch v. Don Hoyt, Inc.*, 4 Wn. App. 580, 583, 483 P.2d 135 (1971): “It is well established that a priority acquired by the recording of a mortgage is not lost because one holds it under an unrecorded assignment.” *Id.* (citing *Miller*, 119 Wash. 243 and quoting *Jones on Mortgages*). In *Keltch*, the appellate court held the mortgage was superior to construction liens, even though the original lender assigned the mortgage in an assignment that was not recorded until two years *after* the commencement of the foreclosure suit. *Id.* at 580-82. The mortgage maintained its superiority even though it covered future advances. *Id.* at 580.³²

In this case, the assignment also takes the priority of the original mortgage. The confirmatory assignment instrument was recorded fourteen months after the commencement of the suit – a shorter period than in

³² See also *Liska v. Beckmann*, 168 Wash. 489, 492, 12 P.2d 599 (1932) (ruling mortgage recorded and assigned before mortgagee assigned new mortgage held first lien.) *Id.* at 494 (denying relief as to estoppel).

Keltch. The same principle of constructive notice to the junior lienholder governs. The recorded mortgage warned about the possible transfer of the note and the consequences of encumbering the property. The assignment takes the mortgage's priority, as in *Keltch* and prior decisions. The junior lienholder cannot leap frog ahead of the senior mortgage.

2. **WMC was not a representative of Deutsche in the foreclosure suit.** Scotty's apparently makes the claim that Deutsche was bound by something akin to the doctrine of virtual representation addressed in *Diversified Wood II*. 161 Wn. App. at 904-06. But as established *supra* in Section III.C and III.D, the title records conclusively eliminate any possible reasonable inference that WMC somehow represented Deutsche. WMC lost any authority over the mortgage, immediately after closing the loan five years earlier, when it transferred the note to Deutsche.

The declaration by WMC's officer for service bound only WMC. If Scotty's goal was to have its suit determine the priority of its lien versus the mortgages against the property, then it should have looked past the original named beneficiary's on the notes. With MERS listed, practice and common sense dictated further investigation before initiating a foreclosure suit. With proper information, Scotty's could have better decided whether to join further persons or entities in the suit. The declaration of service on WMC has no

indicia that the statements were communicated to Deutsche or anywhere beyond WMC. It thus cannot preclude Deutsche from now seeking reversal of the order denying vacation of the judgment and seeking a declaratory judgment on its own behalf establishing lien priority.

3. Deutsche has further standing to request declaratory relief.

Although the present action seeks primarily to reverse the Trial Court's denial of WMC's motion to vacate, WMC respectfully asks this Court to decide the issue of declaratory relief in this matter to avoid further litigation and consumption of time and resources. The fact that the mortgage is a deed of trust does not alter the inevitable conclusion that the prior suit did not bind Deutsche and that its mortgage retains priority over the construction lien. "[A] deed of trust is subject to all laws relating to mortgages on real property," and "the parties may insert in such a mortgage any lawful agreement or condition." RCW 61.24.020;³³ RCW 61.12.020. Here, the deed of trust names a trustee whose successor was the grantor of a later trustee's deed. CP 39, Exhibit B, WMC Motion to Set Aside Judgment and Default Order. There had been no reconveyance by

³³ *Bank of Am., N.A. v. Prestance Corp.*, 160 Wn.2d 560, 562 n. 1, 160 P.3d 17 (2007) ("[A] deed that contains or is accompanied by an agreement that it shall be cancelled or the land reconveyed upon payment of debt is a mortgage."); *id.* (citing 18 William B. Stoebuck & John W. Weaver, *Washington Practice, Real Estate: Transactions* § 20.2, at 405 (2d ed. 2004)).

the trustee. RCW 61.24.110 (reconveyance “upon satisfaction of the obligation secured and written request for reconveyance made by the beneficiary or other person entitled thereto.”).

The form deed of trust’s uniform covenants notify anyone reviewing the title that the secured note may be sold and a loan servicer will collect the loan payments. The mortgage note was transferred to Deutsche -- long before the construction lien foreclosure suit was commenced. With that transfer, Deutsche received the right to enforce the note both under the Uniform Commercial Code³⁴ and the long-established real property law, previously cited. Deutsche as the holder of the note had rights under the mortgage’s uniform covenant 6 authorizing the lender to protect its interest in the property “by appearing in court” when there is a legal proceeding affecting the lender’s rights under the security agreement or when the borrower has abandoned the property. Both of those conditions apply in this case: there was an earlier legal proceeding

³⁴ See U.C.C. § 3-203 (Transfer of instruments; rights acquired by transfer), RCW 62A.3-203. “Transfer of an instrument, vests in the transferee any right of the transferor to enforce the instrument” § 3-203(b). Even if a servicer held the note, someone besides WMC who had transferred the note had authority to enforce the note. See Official Comment 1 to UCC § 3-203 (“The right to enforce an instrument and ownership of the instrument are two different concepts.”); Permanent Editorial Board of the UCC Committee Report *Application of the Uniform Commercial Code to Selected Issues Relating to Mortgage Notes* at 12-14 (Nov. 14, 2011) (addressing effect of transfer of mortgage note on the mortgage and actions to become assignee of record), Appendix A. *Id.* at 14 (transferee of note automatically has property right in mortgage).

allegedly affecting the secured instrument and the hypothetical (and actual) situation is the property was abandoned.

Declaratory judgments are authorized by Civil Rule 57 and the Uniform Declaratory Judgment Act, RCW 7.24.010-.190. RCW 7.24.020 specifically authorizes: “A person interested under a deed, ... may have determined any question of construction or validity arising under the instrument, ... and obtain a declaration of rights, status or other legal relations thereunder.” Here, Deutsche with two instruments (the note and the assignment of the mortgage) has standing to seek declaratory relief under the plain terms of the mortgage.

Again, though this appeal concerns the procedural motion to vacate the outstanding judgment, Deutsche also maintains an actionable claim for a declaratory judgment. In *BNC Mortg., Inc. v. Tax Pros, Inc.*, 111 Wn. App. 238, 246, 46 P.3d 812 (2002), another commercial lender sought a similar judgment that its deed of trust was superior to a creditor’s judgment lien. *Id.* As the appellate court in *BNC Mortg., Inc.* observed: “A deed of trust creates a lien against the property it describes. The lien first in time is the lien first in right, unless the holder of the lien first in time voluntarily subordinates it.” 111 Wn. App. at 246.

In this case, there was no voluntary subordination. There is evidence of default on the mortgage note. Scotty’s did not pay to

extinguish the obligation secured by the mortgage. Scotty's simply claims that Deutsche has no interest in the property and hopes this Court will uphold the erroneous forfeiture of the mortgage. Both the law and equity abhor a forfeiture. Scotty's claims raise a controversy. Denial of WMC's Motion to Vacate constitutes an abuse of discretion on clearly untenable grounds, in going beyond what is manifestly reasonable under these facts and well-established law.

Scotty's contentions about the issues before the Supreme Court regarding the beneficiary status of MERS and about the alleged conflicts of interest by the trustee are smoke and mirrors whose purpose is to conceal the substantial flaws in its defenses.

4. **The MERS issues under review by the Supreme Court do not affect the determination of this appeal.** Three questions are currently pending before the Washington Supreme Court regarding MERS: (1) if MERS can be a lawful beneficiary within the terms of the deed of trust act if it never held the promissory note secured by the a deed of trust; (2) if not, what is the legal effect of MERS acting as an unlawful beneficiary under the terms of the Deed of Trust Act; and (3) does a homeowner possess a cause of

action under the Consumer Protection Act, if MERS acts as an unlawful beneficiary under the terms of the Deed of Trust Act?³⁵

The resolution of those questions does not affect the determination of the issues presented for review in this appeal. The questions before the supreme court flow from the premise of the first question: MERS never held the note. In contrast, the questions in this appeal flow from the premise of the first question presented: WMC transferred the note at closing and Deutsche possesses the note. *Compare* supreme court clerk's summary of issue ("Whether Mortgage Electronic Registration Systems, Inc., a corporation formed to provide a national electronic registry to track the transfer of ownership interests and servicing rights in mortgage loans, and nominated by many lenders as mortgagee of record and beneficiary under deeds of trust, may lawfully serve as beneficiary under the Washington Deed of Trust Act where it never held the underlying promissory note?")³⁶ with *supra* Issue No. 1 ("Deutsche holds the mortgage note and a recorded assignment of the mortgage. Does the holder of the mortgage note and assignee of the record have standing to

³⁵ *Bain v. Metro. Mortg. Elec. Group, Inc.*, No. 86206-1 (Wash).
Selkowitz v. Litton Loan Servicing Co., No. 86207(Wash).

³⁶ *Bain v. Metro. Mortg. Group Inc.*, No. C09-0149-JCC (W.D. Wash. June 27, 2011), (Coughenour, J.), *Bain v. Mortg. Elec. Registration Sys., et al.*; *Selkowitz v. Litton Loan Servicing, LP, et al.* (3/15/12) (Certified Question from U.S. District Court, for the Western District of Washington), supreme court commissioner's summary of issue, at www.courts.wa.gov/appellate_trial_courts/supreme/issues.

bring a declaratory action ...?”). *See also supra* Issues No. 2-3 (regarding the effect of prior suit and the effect of the transfer of the note).

The remaining issues presented for review in this appeal relate to the effect of constructive notice on the contractor from recorded instruments, the contractor’s actual notice of those interests, the contractor’s failure to provide notice of the suit and joinder in compliance with due process, the retention of priority when a mortgage is assigned, and the uncontestable priority of the mortgage itself. Those issues are not affected in any way by the issues under review by the Supreme Court. This appeal is determined by aforementioned three black letter rules regarding the priority of the recorded mortgage over the junior construction lien.

5. The beneficiary status of MERS is a red herring.

Scotty’s cannot argue that MERS failed to transfer any interest to Deutsche. That argument fails for three reasons.

a. The mortgage follows the note; Deutsche’s rights are vested from its possession of the note. The mortgage was transferred once by delivery of an instrument (the note) and again by a conveyance document (the written assignment). “[T]he maxim [is] the mortgage follows the debt” *Fidelity & Deposit Co. of Maryland v. Ticor Title Ins. Co.*, 88 Wn. App. 64, 68, 943 P.2d 710 (1997). “A transfer of an

obligation secured by a mortgage also transfers the mortgage unless the parties to the transfer agree otherwise.” Restatement (Third) of Property, Mortgages § 5.4(a) (1997).³⁷ Deutsche alone had standing to enforce the mortgage. “A mortgage may be enforced only by, on in the behalf of, a person entitled to enforce the obligation the mortgage secures.” § 5.4(c).

Deutsche, by way of its non-judicial sale, enforced the terms of the mortgage – not MERS. MERS’ function in this case was merely as a mechanism to notify the holder of the loan/note/mortgage and would have facilitated Scotty’s to satisfy the due process of reasonable notice as articulated in *Mullane v. Central Hanover Bank & Trust Co.* and its progeny. This fundamental and discrete issue of due process is not before the supreme court. There are also additional reasons why the beneficiary status of MERS is a red herring.

b. MERS transferred any rights it had under the mortgage. When MERS transferred its rights through signing the assignment instrument, MERS divested any rights it had to enforce the mortgage. As this Court said in the context of a security interest under the U.C.C.: “An absolute assignment divests the assignor of all control and right to a cause of action against the original debtor; the assignee is

³⁷ See also Reporters’ Note to “Transfer of the obligation also transfers the mortgage” (citing *Bartlett Estate Co. v. Fairhaven Land Co.*, 49 Wash. at 63 (1908)).

entitled to control and to receive the benefits of the contract between the original debtor and the assignor.”³⁸

The absolute assignment divested all rights of MERS as the mortgage’s original beneficiary (who was acting as the nominee for the lender and the lender’s assigns). Deutsche held the mortgage note and thus was the “lender’s assign” with the right to enforce the mortgage. Therefore, the beneficiary status of MERS is a red herring diverting the court’s attention away from the relief sought in this case – reversal of the order denying WMC’s motion to vacate and a declaratory judgment regarding the priority of the mortgage over a junior construction lien.

6. Alternatively, the majority of state appellate and federal court decisions affirm the legitimacy of MERS. In *Vawter v. Quality Loan Service Corp.*, the district court for the western district of Washington provides a persuasive conclusion that MERS can act as a beneficiary, stating:

[t]he deed of trust act allows a beneficiary, such as MERS, to appoint a successor trustee, which MERS did in this case. Plaintiff argues, however, that MERS cannot be a beneficiary and therefore MERS’ appointment of a new trustee was invalid. . . . Plaintiff provides a printout from MERS’ website stating that it is an electronic registry that tracks the ownership of loans. Plaintiff argues that because MERS only registers documents it does not actually hold them. Plaintiffs’ argument is unconvincing. Simply because MERS registers documents in a database does not

³⁸ *Uni-Com NW, Ltd. v. Argus*, 47 Wn. App. 787, 794, 737 P.2d 304 (1987).

prove that MERS cannot be the legal holder of an instrument.

707 F. Supp. 2d 1115, 1122 (Apr. 22, 2010)(quoting *Moon v. GMAC Mortg. Corp.*, 2008 WL 4741492, at *5 (W.D. Wash. 2008)).

The western district court reaffirmed the authority of MERS in *Daddabbo v. Countrywide Home Loans*, 2010 WL 2102485 (W.D. Wash. May 20, 2010), stating:

[t]he deed of trust, of which the court takes judicial notice, explicitly names MERS as a beneficiary. The deed of trust grants MERS not only legal title to the interests created in the trust, but the authorization of the lender and any of its successors to take any action to protect those interests, including the ‘right to foreclose and sell the Property.’³⁹ [Citations omitted.]

The court in *Daddabbo* found that no fact the plaintiffs introduced “remotely supports Plaintiffs’ assertion that MERS somehow has been stripped of the power that the deed of trust grants.” *Id.*

In *Blau v. America’s Servicing Company*, the district court for Arizona considered a deed of trust that named MERS as “both the lender’s nominee and ‘beneficiary’ of the agreement.” 2009 WL 3174823 (D. Ariz. Sept. 29, 2009). The court found that “MERS, acting on behalf of the lender,” was entitled to transfer the lender’s interest to a subsequent

³⁹ The citation to *Daddabbo* and other federal court decisions, *supra*, is made pursuant to Fed. R. App. P. 32.1, which permits the use of unpublished “opinions, orders, judgments, or other written dispositions” after January 1, 2007. *Cf.* GR 14.1(b).

beneficiary. *Id.*; see also *Pazmino v. LaSalle Bank, N.A.*, 2010 WL 2039163 (E.D. Va. May 20, 2010) (allowing the same).

In *McGinnis v. GMAC Mortg. Corp.*, the district court for the central district of Utah points out that:

[c]ourts have consistently held that [language naming MERS as a beneficiary in a security instrument] . . . gives MERS the authority to foreclose in behalf of the lender and that MERS need not possess the note in order to appoint a trustee in behalf of the lender who does hold the note.” 2010 WL 3418204 (C.D. Utah Aug. 27, 2010).

In *Burnett v. MERS, Inc.*, the district court for the northern district of Utah found that “MERS had authority to ‘take any action’ required of Lender. . . ,” which included appointing a successor trustee and even selling the property. 2009 WL 3582294 (N.D. Utah Oct. 27, 2009).

Recently, a federal court handling multidistrict litigation challenging numerous aspects of MERS’ conduct in non-judicial foreclosure states issued a decision that affirmed MERS’ ability, as a specifically-named beneficiary, to make assignments, appoint trustees, or take other acts in connection with a foreclosure. See *In re MERS Litig.*, 2010 WL 4038788 (D. Ariz. Sept. 30, 2010); see also *Silvas v. GMAC Mortg., LLC*, 2009 WL 4573234 (D. Ariz. Jan. 5, 2010) (ruling MERS can foreclose where MERS is designated on a deed of trust as the beneficiary).

These jurisdictions follow other courts that have held MERS may hold legal title to the deed of trust as the beneficiary, has standing to assign

the deed of trust, may substitute trustees, and can even foreclose to enforce the property interest granted to it in the mortgage or deed of trust.⁴⁰

At the trial court level, Scotty's cited *Landmark Nat'l Bank v. Kesler*, 289 Kan. 528, 216 P.3d 158 (2009), and argued that MERS had no interest in the deed of trust. The *Kesler* court emphasized the narrowness of its holding, expressly stating, "[w]hether MERS may act as a nominee for the lender, either to bring a foreclosure suit or for some other purpose, is not at issue. . . ." *Id.* at 180.⁴¹ *Kesler* focused on Kansas law and civil procedure standards. Nothing in the decision states that MERS cannot possess an interest in a deed of trust.

Washington's recording system has a grantor-grantee index.⁴² In this case, MERS was the grantee of record until Deutsche became the grantee of record. Anyone searching the recorder's index had notice of those interests.

⁴⁰ See, e.g., *Saterbak v. MTC Fin., Inc.*, 2011 WL 484300 (D. Nev. Feb. 4, 2011) (rejecting plaintiffs argument that MERS was not a proper beneficiary or nominee); *Maxa v. Countrywide Loans, Inc.*, 2010 WL 2836958 (D. Ariz. Jul. 19, 2010) (rejecting assertion that MERS is not a valid beneficiary because it lacked possession of the note); *Ciardi v. Lending Co., Inc.*, 2010 WL 2079735 (D. Ariz. May 24, 2010) (deed of trust, freely entered into by plaintiff designates MERS as beneficiary with authority to foreclose and sell the property); *Wurtzberger v. Resmae Mortg. Corp.*, 2010 WL 1779972 (E.D. Cal. Apr. 29, 2010) (MERS had right to foreclose and assign beneficial interest under deed of trust); *Cervantes v. Countrywide Home Loans Inc.*, 656 F.3d 1034 (9th Cir. 2011) (affirming dismissal of class action suit for conspiracy to commit fraud through the MERS system and wrongful foreclosure).

⁴¹ After the *Kesler* decision, the Kansas Legislature completed a comprehensive overhaul of the Kansas Civil Procedure Code, which in part, requires the joining of any party in an action to determine title or affecting a security interest in real property if that party is a nominee of record on behalf of a beneficial owner.

⁴² 18 Stoebuck & Weaver, *Washington Practice, Real Estate: Transactions* § 14.6 at 132, 134.

Yet, Scotty's quasi in rem suit simply did not join the recorded interest assigned to Deutsche. The present suit, therefore, could not as a matter of law extinguish the mortgage held by Deutsche.

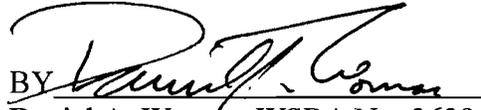
V. CONCLUSION

In summary, Deutsche is not bound by the foreclosure decree granted in the quasi in rem suit to which it was not a party. The failure of Scotty's to join MERS in the prior suit, or give written notice to MERS of the suit, results in a jurisdictional defect as to Deutsche and its interest in the property. The judgment against WMC should be vacated so that the Court can conclusively decide this case on the merits, and award a declaratory judgment that Deutsche was not bound by the prior suit and its mortgage has priority of record over the junior construction lien. The denial of WMC's motion to vacate was an abuse of discretion, and must be reversed.

The merits of this case and the interests of justice support an affirmative ruling on Issue No. 7 (the deed of trust held by Deutsche has priority of record over any interest of Scotty's in Parcel 062205-9056). Deutsche respectfully requests this determination.

RESPECTFULLY SUBMITTED this 6th day of March, 2012.

FIDELITY NATIONAL LAW GROUP,
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BY 

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Trust 2005-WMCI, as successor to WMC
Mortgage Corporation

Appendices

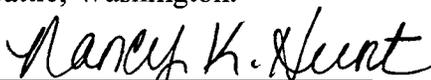
- A: Permanent Editorial Board of the UCC Committee Report
*Application of the Uniform Commercial Code to Selected Issues
Relating to Mortgage Notes* (Nov. 14, 2011) (using term, mortgage
note).
- B: King County Recorder's Frequently Asked Questions (lag between
recording and availability on website – 24 hours).

CERTIFICATE OF SERVICE

I hereby certify that on the date given below I caused to be served the foregoing document entitled BRIEF OF APPELLANT on the following individuals in the manner indicated:

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SIGNED this 6th day of March, 2012, at Seattle, Washington.


 Nancy K. Hunt

APPENDIX A

**REPORT OF THE PERMANENT EDITORIAL BOARD
FOR THE
UNIFORM COMMERCIAL CODE**

**APPLICATION OF THE UNIFORM COMMERCIAL CODE TO
SELECTED ISSUES RELATING TO MORTGAGE NOTES**

NOVEMBER 14, 2011

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PREFACE

In 1961, the American Law Institute and the Uniform Law Commission, the organizations that jointly sponsor the Uniform Commercial Code, established the Permanent Editorial Board for the Uniform Commercial Code (PEB). One of the charges of the PEB is to issue commentaries “and other articulations as appropriate to reflect the correct interpretation of the [Uniform Commercial] Code and issuing the same in a manner and at times best calculated to advance the uniformity and orderly development of commercial law.” Such commentaries and other articulations are issued directly by the PEB rather than by action of the American Law Institute and the Uniform Law Commission.

This Report of the Permanent Editorial Board is such an articulation, addressing the application of the Uniform Commercial Code to issues of legal, economic, and social importance arising from the issuance and transfer of mortgage notes. A draft of this Report was made available to the public for comment on March 29, 2011, and the comments that were received have been taken into account in preparing the final Report.

**REPORT OF THE PERMANENT EDITORIAL BOARD
FOR THE
UNIFORM COMMERCIAL CODE**

**APPLICATION OF THE UNIFORM COMMERCIAL CODE TO SELECTED ISSUES
RELATING TO MORTGAGE NOTES**

Introduction

Recent economic developments have brought to the forefront complex legal issues about the enforcement and collection of mortgage debt. Many of these issues are governed by local real property law and local rules of foreclosure procedure, but others are addressed in a uniform way throughout the United States by provisions of the Uniform Commercial Code (UCC).¹ Although the UCC provisions are settled law, it has become apparent that not all courts and attorneys are familiar with them. In addition, the complexity of some of the rules has proved daunting.

The Permanent Editorial Board for the Uniform Commercial Code² has prepared this Report in order to further the understanding of this statutory background by identifying and explaining several key rules in the UCC that govern the transfer and enforcement of notes secured by a mortgage³ on real property. The UCC, of course, does not resolve all issues in this field. Most particularly, as to both substance and procedure, the enforcement of real estate mortgages by foreclosure is primarily the province of a state's real property law (although determinations made

¹ The UCC is a uniform law sponsored by the American Law Institute and the Uniform Law Commission. It has been enacted in every state (as well as the District of Columbia, Puerto Rico, and the United States Virgin Islands) in whole or significant part. This Report is based on the current Official Text of the UCC. Some states have enacted some non-uniform provisions that are generally not relevant to the issues discussed in this Report. Of course, the enacted text of the UCC in the state whose law is applicable governs. See note 6, *infra*, regarding the various different versions of Article 3 of the UCC in effect in the states.

²In 1961, the American Law Institute and the Uniform Law Commission, the organizations that jointly sponsor the UCC, established the Permanent Editorial Board for the Uniform Commercial Code (PEB). One of the charges of the PEB is to issue commentaries "and other articulations as appropriate to reflect the correct interpretation of the [Uniform Commercial] Code and issuing the same in a manner and at times best calculated to advance the uniformity and orderly development of commercial law."

³ This Report, like Article 9 of the UCC, uses the term "mortgage" to include a consensual interest in real property to secure an obligation whether created by mortgage, trust deed, or the like. See UCC § 9-102(a)(55) and Official Comment 17 thereto and former UCC § 9-105(1)(j). This Report uses the term "mortgage note" to refer to a note secured by a mortgage, whether or not the note is a negotiable instrument under UCC Article 3.

pursuant to the UCC are typically relevant under that law). Accordingly, this Report should be understood as providing guidance only as to the issues the Report addresses.⁴

Background

Issues relating to the transfer, ownership, and enforcement of mortgage notes are primarily governed by two Articles of the UCC:

- In cases in which the mortgage note is a negotiable instrument,⁵ Article 3 of the UCC⁶ provides rules governing the obligations of parties on the note⁷ and the enforcement of those obligations.
- In cases involving either negotiable or non-negotiable notes, Article 9 of the UCC⁸ contains important rules governing how ownership of those notes may be transferred, the effect of the transfer of ownership of the notes on the ownership of the mortgages securing those notes, and the right of the transferee, under certain circumstances, to record its interest in the mortgage in the applicable real estate recording office.

This Report explains the application of the rules in both of those UCC Articles to provide guidance in:

- Identifying the person who is entitled to enforce the payment obligation of the maker⁹ of a mortgage note, and to whom the maker owes that obligation; and

⁴ Of course, the application of the UCC rules to particular factual circumstances depends on the nature of those circumstances. Facts raising legal issues other than those addressed in this Report can result in different rights and obligations than would be the case in the absence of those facts. Accordingly, this Report should not be read as a statement of the total legal implications of any factual scenario. Rather, the Report sets out the UCC rules that are common to the transactions discussed so as to provide a common basis for understanding the application of those rules. The impact of non-UCC law that applies to other aspects of such transactions is beyond the scope of this Report.

⁵ The requirements that must be satisfied in order for a note to be a negotiable instrument are set out in UCC § 3-104.

⁶ Except for New York, every state (as well as the District of Columbia, Puerto Rico, and the United States Virgin Islands) has enacted either the 1990 Official Text of Article 3 or the newer 2002 Official Text (the latter having been adopted in ten states as of the date of this Report). Unless indicated to the contrary all discussions of provisions in Article 3 apply equally to both versions. Much of the analysis of UCC Article 3 in this Report also applies under the older version of Article 3 in effect in New York, although many section numbers differ. The Report does not address those aspects of New York's Article 3 that are different from the 1990 or 2002 texts.

⁷ In this Report, such notes are sometimes referred to as "negotiable notes."

⁸ Unlike Article 3 (which has not been enacted in its modern form in New York), the current version of Article 9 has been enacted in all 50 states, the District of Columbia, and the United States Virgin Islands. Some states have enacted non-uniform provisions that are generally not relevant to the issues discussed in this Report (but see note 31 with respect to one relevant non-uniformity). A limited set of amendments to Article 9 was approved by the American Law Institute and the Uniform Law Commission in 2010. Except as noted in this Report, those amendments (which provide for a uniform effective date of July 1, 2013) are not germane to the matters addressed in this Report.

⁹ A note can have more than one obligor. In some cases, this is because there is more than one maker (in which case they are jointly and severally liable; see UCC § 3-116(a)). In other cases, there may be an indorser. The obligation

- Determining who owns the rights represented by the note and mortgage.

Together, the provisions in Articles 3 and 9 of the UCC (along with general principles that appear in Article 1 and that apply to all transactions governed by the UCC) provide legal rules that apply to these questions.¹⁰ Moreover, these rules displace any inconsistent common law rules that might have otherwise previously governed the same questions.¹¹

This Report does not, however, address all of the rules in the UCC relating to enforcement, transfer, and ownership of mortgage notes. Rather, it reviews the rules relating to four specific questions:

- Who is the person entitled to enforce a mortgage note and, correspondingly, to whom is the obligation to pay the note owed?
- How can the owner of a mortgage note effectively transfer ownership of that note to another person or effectively use that note as collateral for an obligation?
- What is the effect of transfer of an interest in a mortgage note on the mortgage securing it?
- May a person to whom an interest in a mortgage note has been transferred, but who has not taken a recordable assignment of the mortgage, take steps to become the assignee of record in the real estate recording system of the mortgage securing the note?¹²

of an indorser is different from that of a maker in that the indorser's obligation is triggered by dishonor of the note (see UCC § 3-415) and, unless waived, indorsers have additional procedural protections (such as notice of dishonor; see UCC § 3-503)). These differences do not affect the issues addressed in this Report. For simplicity, this Report uses the term "maker" to refer to both makers and indorsers.

¹⁰ Subject to limitations on the ability to affect the rights of third parties, the effect of these provisions may be varied by agreement. UCC § 1-302. Variation by agreement is not permitted when the variation would disclaim obligations of good faith, diligence, reasonableness, or care prescribed by the UCC or when the UCC otherwise so indicates (see, e.g., UCC § 9-602). But the meaning of the statute itself cannot be varied by agreement. Thus, for example, private parties cannot make a note negotiable unless it complies with UCC § 3-104. See Official Comment 1 to UCC § 1-302. Similarly, parties may not avoid the application of UCC Article 9 to a transaction that falls within its scope. See *id.* and Official Comment 2 to UCC § 9-109.

¹¹UCC § 1-103(b). As noted in Official Comment 2 to UCC § 1-103:

The Uniform Commercial Code was drafted against the backdrop of existing bodies of law, including the common law and equity, and relies on those bodies of law to supplement its provisions in many important ways. At the same time, the Uniform Commercial Code is the primary source of commercial law rules in areas that it governs, and its rules represent choices made by its drafters and the enacting legislatures about the appropriate policies to be furthered in the transactions it covers. Therefore, while principles of common law and equity may *supplement* provisions of the Uniform Commercial Code, they may not be used to *supplant* its provisions, or the purposes and policies those provisions reflect, unless a specific provision of the Uniform Commercial Code provides otherwise. In the absence of such a provision, the Uniform Commercial Code preempts principles of common law and equity that are inconsistent with either its provisions or its purposes and policies.

¹² The Report does not discuss the application of common law principles, such as the law of agency, that supplement the provisions of the UCC other than to note some situations in which the text or comments of the UCC identify such principles as being relevant. See UCC § 1-103(b).

Question One – To Whom is the Obligation to Pay a Mortgage Note Owed?

If the mortgage note is a negotiable instrument,¹³ Article 3 of the UCC provides a largely complete set of rules governing the obligations of parties on the note, including how to determine who may enforce those obligations and, thus, to whom those obligations are owed. The following discussion analyzes the application of these rules to that determination in the context of mortgage notes that are negotiable instruments.¹⁴

In the context of mortgage notes that have been sold or used as collateral to secure an obligation, the central concept for making that determination is identification of the “person entitled to enforce” the note.¹⁵ Several issues are resolved by that determination. Most particularly:

- (i) the maker’s obligation on the note is to pay the amount of the note to *the person entitled to enforce the note*,¹⁶
- (ii) the maker’s payment to *the person entitled to enforce the note* results in discharge of the maker’s obligation,¹⁷ and
- (iii) the maker’s failure to pay, when due, the amount of the note to *the person entitled to enforce the note* constitutes dishonor of the note.¹⁸

Thus, a person seeking to enforce rights based on the failure of the maker to pay a mortgage note must identify the person entitled to enforce the note and establish that that person has not been paid. This portion of this Report sets out the criteria for qualifying as a “person entitled to enforce” a mortgage note. The discussion of Question Two addresses how ownership of a mortgage note may be effectively transferred from an owner to another person.

¹³ See UCC § 3-104 for the requirements that must be fulfilled in order for a payment obligation to qualify as a negotiable instrument. It should not be assumed that all mortgage notes are negotiable instruments. The issue of the negotiability of a particular mortgage note, which requires application of the standards in UCC § 3-104 to the words of the particular note, is beyond the scope of this Report.

¹⁴ Law other than Article 3, including contract law, governs this determination for non-negotiable mortgage notes. That law is beyond the scope of this Report.

¹⁵ The concept of “person entitled to enforce” a note is not synonymous with “owner” of the note. See Official Comment 1 to UCC § 3-203. A person need not be the owner of a note to be the person entitled to enforce it, and not all owners will qualify as persons entitled to enforce. Rules that address transfer of ownership of a note are addressed in the discussion of Question 2 below.

¹⁶ UCC § 3-412. (If the note has been dishonored, and an indorser has paid the note to the person entitled to enforce it, the maker’s obligation runs to the indorser.)

¹⁷ UCC § 3-602. The law of agency is applicable in determining whether a payment has been made to a person entitled to enforce. See *id.*, Official Comment 3. Note that, in states that have enacted the 2002 Official Text of UCC Article 3, UCC § 3-602(b) provides that a maker is also discharged by paying a person formerly entitled to enforce the note if the maker has not received adequate notification that the note has been transferred and that payment is to be made to the transferee. This amendment aligns the protection afforded to makers of notes that have been assigned with comparable protection afforded to obligors on other payment rights that have been assigned. See, *e.g.*, UCC § 9-406(a); Restatement (Second), Contracts § 338(1).

¹⁸ See UCC § 3-502. See also UCC § 3-602.

UCC Section 3-301 provides only three ways in which a person may qualify as the person entitled to enforce a note, two of which require the person to be in possession of the note (which may include possession by a third party that possesses it for the person)¹⁹:

- The first way that a person may qualify as the person entitled to enforce a note is to be its “holder.” This familiar concept, set out in detail in UCC Section 1-201(b)(21)(A), requires that the person be in possession of the note and either (i) the note is payable to that person or (ii) the note is payable to bearer. Determining to whom a note is payable requires examination not only of the face of the note but also of any indorsements. This is because the party to whom a note is payable may be changed by indorsement²⁰ so that, for example, a note payable to the order of a named payee that is indorsed in blank by that payee becomes payable to bearer.²¹
- The second way that a person may be the person entitled to enforce a note is to be a “nonholder in possession of the [note] who has the rights of a holder.”
 - How can a person who is not the holder of a note have the rights of a holder? This can occur by operation of law outside the UCC, such as the law of subrogation or estate administration, by which one person is the successor to or acquires another person’s rights.²² It can also occur if the delivery of the note to that person constitutes a “transfer” (as that term is defined in UCC Section 3-203, see below) because transfer of a note “vests in the transferee any right of the transferor to enforce the instrument.”²³ Thus, if a holder (who, as seen above, is a person entitled to enforce a note) transfers the note to another person, that other person (the transferee) obtains from the holder the right to enforce the note even if the transferee does not become the holder (as in the example below). Similarly, a

¹⁹ See UCC § 1-103(b) (unless displaced by particular provisions of the UCC, the law of, *inter alia*, principal and agent supplements the provisions of the UCC). See also UCC § 3-420, Comment 1 (“Delivery to an agent [of a payee] is delivery to the payee.”). Note that “delivery” of a negotiable instrument is defined in UCC § 1-201(b)(15) as voluntary transfer of possession. This Report does not address the determination of whether a particular person is an agent of another person under the law of agency and the agency law implications of such a determination.

²⁰ “Indorsement,” as defined in UCC § 3-204(a), requires the signature of the indorser. The law of agency determines whether a signature made by a person purporting to act as a representative binds the represented person. UCC § 3-402(a); see note 12, *supra*. An indorsement may appear either on the instrument or on a separate piece of paper (usually referred to as an *allonge*) affixed to the instrument. See UCC § 3-204(a) and Comment 1, par. 4.

²¹ UCC Section 3-205 contains the rules concerning the effect of various types of indorsement on the party to whom a note is payable. Either a “special indorsement” (see UCC § 3-205(a)) or a “blank indorsement” (see UCC § 3-205(b)) can change the identity of the person to whom the note is payable. A special indorsement is an indorsement that identifies the person to whom it makes the note payable, while a blank indorsement is an indorsement that does not identify such a person and results in the instrument becoming payable to bearer. When an instrument is indorsed in blank (and, thus, is payable to bearer), it may be negotiated by transfer of possession alone until specially indorsed. UCC § 3-205(b).

²² See Official Comment to UCC § 3-301.

²³ UCC § 3-203(b).

subsequent transfer will result in the subsequent transferee being a person entitled to enforce the note.

- Under what circumstances does delivery of a note qualify as a transfer? As stated in UCC Section 3-203(a), a note is transferred “when it is delivered by a person other than its issuer for the purpose of giving to the person receiving delivery the right to enforce the instrument.” For example, assume that the payee of a note sells it to an assignee, intending to transfer all of the payee’s rights to the note, but delivers the note to the assignee without indorsing it. The assignee will not qualify as a holder (because the note is still payable to the payee) but, because the transaction between the payee and the assignee qualifies as a transfer, the assignee now has all of the payee’s rights to enforce the note and thereby qualifies as the person entitled to enforce it. Thus, the failure to obtain the indorsement of the payee does not prevent a person in possession of the note from being the person entitled to enforce it, but demonstrating that status is more difficult. This is because the person in possession of the note must also demonstrate the purpose of the delivery of the note to it in order to qualify as the person entitled to enforce.²⁴
- There is a third method of qualifying as a person entitled to enforce a note that, unlike the previous two methods, does not require possession of the note. This method is quite limited – it applies only in cases in which “the person cannot reasonably obtain possession of the instrument because the instrument was destroyed, its whereabouts cannot be determined, or it is in the wrongful possession of an unknown person or a person that cannot be found or is not amenable to service of process.”²⁵ In such a case, a person qualifies as a person entitled to enforce the note if the person demonstrates not only that one of those circumstances is present but also demonstrates that the person was formerly in possession of the note and entitled to enforce it when the loss of possession occurred and that the loss of possession was not as a result of transfer (as defined above) or lawful seizure. If the person proves those facts, as well as the terms of the note, the person is a person entitled to enforce the note and may seek to enforce it even though it is not in possession of the note,²⁶ but the court may not enter judgment in favor of the

²⁴ If the note was transferred for value and the transferee does not qualify as a holder because of the lack of indorsement by the transferor, “the transferee has a specifically enforceable right to the unqualified indorsement of the transferor.” See UCC § 3-203(c).

²⁵ UCC § 3-309(a)(iii) (1990 text), 3-309(a)(3) (2002 text). The 2002 text goes on to provide that a transferee from the person who lost possession of a note may also qualify as a person entitled to enforce it. See UCC § 3-309(a)(1)(B) (2002). This point was thought to be implicit in the 1990 text, but was rejected in some cases in which the issue was raised. The reasoning of those cases was rejected in Official Comment 5 to UCC § 9-109 and the point was made explicit in the 2002 text of Article 3.

²⁶ To prevail the person must establish not only that the person is a person entitled to enforce the note but also the other elements of the maker’s obligation to pay such a person. See generally UCC §§ 3-309(b), 3-412. Moreover, as is the case with respect to the enforcement of all rights under the UCC, the person enforcing the note must act in good faith in enforcing the note. UCC § 1-304.

person unless the court finds that the maker is adequately protected against loss that might occur if the note subsequently reappears.²⁷

Illustrations:

1. Maker issued a negotiable mortgage note payable to the order of Payee. Payee is in possession of the note, which has not been indorsed. Payee is the holder of the note and, therefore, is the person entitled to enforce it. UCC §§ 1-201(b)(21)(A), 3-301(i).
2. Maker issued a negotiable mortgage note payable to the order of Payee. Payee indorsed the note in blank and gave possession of it to Transferee. Transferee is the holder of the note and, therefore, is the person entitled to enforce it. UCC §§ 1-201(b)(21)(A), 3-301(i).
3. Maker issued a negotiable mortgage note payable to the order of Payee. Payee sold the note to Transferee and gave possession of it to Transferee for the purpose of giving Transferee the right to enforce the note. Payee did not, however, indorse the note. Transferee is not the holder of the note because, while Transferee is in possession of the note, it is payable neither to bearer nor to Transferee. UCC § 1-201(b)(21)(A). Nonetheless, Transferee is a person entitled to enforce the note. This is because the note was transferred to Transferee and the transfer vested in Transferee Payee's right to enforce the note. UCC § 3-203(a)-(b). As a result, Transferee is a nonholder in possession of the note with the rights of a holder and, accordingly, a person entitled to enforce the note. UCC § 3-301(ii).
4. Same facts as Illustrations 2 and 3, except that (i) under the law of agency, Agent is the agent of Transferee for purposes of possessing the note and (ii) it is Agent, rather than Transferee, to whom actual physical possession of the note is given by Payee. In the facts of Illustration 2, Transferee is a holder of the note and a person entitled to enforce it. In the context of Illustration 3, Transferee is a person entitled to enforce the note. Whether Agent may enforce the note or mortgage on behalf of Transferee depends in part on the law of agency and, in the case of the mortgage, real property law.
5. Same facts as Illustration 2, except that after obtaining possession of the note, Transferee lost the note and its whereabouts cannot be determined. Transferee is a person entitled to enforce the note even though Transferee does not have possession of it. UCC § 3-309(a). If Transferee brings an action on the note against Maker, Transferee must establish the terms of the note and the elements of Maker's obligation on it. The court may not enter judgment in favor of Transferee, however, unless the court finds that Maker is adequately protected against loss that might occur by reason of a claim of another person (such as the finder of the note) to enforce the note. UCC § 3-309(b).

²⁷ See *id.* UCC § 3-309(b) goes on to state that "Adequate protection may be provided by any reasonable means."

Question Two – What Steps Must be Taken for the Owner of a Mortgage Note to Transfer Ownership of the Note to Another Person or Use the Note as Collateral for an Obligation?

In the discussion of Question One, this Report addresses identification of the person who is entitled to enforce a note. That discussion does not address who “owns” the note. While, in many cases, the person entitled to enforce a note is also its owner, this need not be the case. The rules that determine whether a person is a person entitled to enforce a note do not require that person to be the owner of the note,²⁸ and a change in ownership of a note does not necessarily bring about a concomitant change in the identity of the person entitled to enforce the note. This is because the rules that determine who is entitled to enforce a note and the rules that determine whether the note, or an interest in it, have been effectively transferred serve different functions:

- The rules that determine who is entitled to enforce a note are concerned primarily with the maker of the note, providing the maker with a relatively simple way of determining to whom his or her obligation is owed and, thus, whom to pay in order to be discharged.
- The rules concerning transfer of ownership and other interests in a note, on the other hand, primarily relate to who, among competing claimants, is entitled to the economic value of the note.

In a typical transaction, when a note is issued to a payee, the note is initially owned by that payee. If that payee seeks either to use the note as collateral or sell the note outright, Article 9 of the UCC governs that transaction and determines whether the creditor or buyer has obtained a property right in the note. As is generally known, Article 9 governs transactions in which property is used as collateral for an obligation.²⁹ In addition, however, Article 9 governs the sale of most payment rights, including the sale of both negotiable and non-negotiable notes.³⁰ With very few exceptions, the same Article 9 rules that apply to transactions in which a payment right is collateral for an obligation also apply to transactions in which a payment right is sold. Rather than contain two parallel sets of rules – one for transactions in which payment rights are collateral and the other for sales of payment rights – Article 9 uses nomenclature conventions to apply one set of rules to both types of transactions. This is accomplished primarily by defining the term “security interest” to include not only an interest in property that secures an obligation

²⁸ See UCC § 3-301, which provides, in relevant part, that “A person may be a person entitled to enforce the instrument even though the person is not the owner of the instrument”

²⁹ UCC § 9-109(a)(1).

³⁰ With certain limited exceptions not germane to this Report, Article 9 governs the sale of accounts, chattel paper, payment intangibles, and promissory notes. UCC § 9-109(a)(3). The term “promissory note” includes not only notes that fulfill the requirements of a negotiable instrument under UCC § 3-104 but also notes that do not fulfill those requirements but nonetheless are of a “type that in ordinary business is transferred by delivery with any necessary indorsement or assignment.” See UCC §§ 9-102(a)(65) (definition of “promissory note”) and 9-102(a)(47) (definition of “instrument” as the term is used in Article 9).

but also the right of a buyer of a payment right in a transaction governed by Article 9.³¹ Similarly, definitional conventions denominate the seller of such a payment right as the “debtor,” the buyer as the “secured party,” and the sold payment right as the “collateral.”³² As a result, for purposes of Article 9, the buyer of a promissory note is a “secured party” that has acquired a “security interest” in the note from the “debtor,” and the rules that apply to security interests that secure an obligation generally also apply to transactions in which a promissory note is sold.

Section 9-203(b) of the Uniform Commercial Code provides that three criteria must be fulfilled in order for the owner of a mortgage note effectively to create a “security interest” (either an interest in the note securing an obligation or the outright sale of the note to a buyer) in it.

- The first two criteria are straightforward – “value” must be given³³ and the debtor/seller must have rights in the note or the power to transfer rights in the note to a third party.³⁴
- The third criterion may be fulfilled in either one of two ways. Either the debtor/seller must “authenticate”³⁵ a “security agreement”³⁶ that describes the note³⁷ or the secured party must take possession³⁸ of the note pursuant to the debtor’s security agreement.³⁹

³¹ See UCC § 1-201(b)(35) [UCC § 1-201(37) in states that have not yet enacted the 2001 revised text of UCC Article 1]. (For reasons that are not apparent, when South Carolina enacted the 1998 revised text of UCC Article 9, which included an amendment to UCC § 1-201 to expand the definition of “security interest” to include the right of a buyer of a promissory note, it did not enact the amendment to § 1-201. This Report does not address the effect of that omission.) The limitation to transactions governed by Article 9 refers to the exclusion, in cases not germane to this Report, of certain assignments of payment rights from the reach of Article 9.

³² UCC §§ 9-102(a)(28)(B); 9-102(a)(72)(D); 9-102(a)(12)(B).

³³ UCC § 9-203(b)(1). UCC § 1-204 provides that giving “value” for rights includes not only acquiring them for consideration but also acquiring them in return for a binding commitment to extend credit, as security for or in complete or partial satisfaction of a preexisting claim, or by accepting delivery of them under a preexisting contract for their purchase.

³⁴ UCC § 9-203(b)(2). Limited rights that are short of full ownership are sufficient for this purpose. See Official Comment 6 to UCC § 9-203.

³⁵ This term is defined to include signing and its electronic equivalent. See UCC § 9-102(a)(7).

³⁶ A “security agreement” is an agreement that creates or provides for a security interest (including the rights of a buyer arising upon the outright sale of a payment right). See UCC § 9-102(a)(73).

³⁷ Article 9’s criteria for descriptions of property in a security agreement are quite flexible. Generally speaking, any description suffices, whether or not specific, if it reasonably identifies the property. See UCC § 9-108(a)-(b). A “supergeneric” description consisting solely of words such as “all of the debtor’s assets” or “all of the debtor’s personal property” is not sufficient, however. UCC § 9-108(c). A narrower description, limiting the property to a particular category or type, such as “all notes,” is sufficient. For example, a description that refers to “all of the debtor’s notes” is sufficient.

³⁸ See UCC § 9-313. As noted in Official Comment 3 to UCC § 9-313, “in determining whether a particular person has possession, the principles of agency apply.” In addition, UCC § 9-313 also contains two special rules under which possession by a non-agent may constitute possession by the secured party. First, if a person who is not an agent is in possession of the collateral and the person authenticates a record acknowledging that the person holds the collateral for the secured party’s benefit, possession by that person constitutes possession by the secured party. UCC § 9-313(c). Second, a secured party that has possession of collateral does not relinquish possession by delivering the collateral to another person (other than the debtor or a lessee of the collateral from the debtor in the ordinary course of the debtor’s business) if the delivery is accompanied by instructions to that person to hold possession of the collateral for the benefit of the secured party or redeliver it to the secured party. UCC § 9-313(h).

- Thus, if the secured party (including a buyer) takes possession of the mortgage note pursuant to the security agreement of the debtor (including a seller), this criterion is satisfied even if that agreement is oral or otherwise not evidenced by an authenticated record.
- Alternatively, if the debtor authenticates a security agreement describing the note, this criterion is satisfied even if the secured party does *not* take possession of the note. (Note that in this situation, in which the seller of a note may retain possession of it, the owner of a note may be a different person than the person entitled to enforce the note.)⁴⁰

Satisfaction of these three criteria of Section 9-203(b) results in the secured party (including a buyer of the note) obtaining a property right (whether outright ownership or a security interest to secure an obligation) in the note from the debtor (including a seller of the note).⁴¹

Illustrations:

6. Maker issued a mortgage note payable to the order of Payee.⁴² Payee borrowed money from Funder and, to secure Payee's repayment obligation, Payee and Funder agreed that Funder would have a security interest in the note. Simultaneously with the funding of the loan, Payee gave possession of the note to Funder. Funder has an attached and

See also Official Comment 9 to UCC § 9-313 ("New subsections (h) and (i) address the practice of mortgage warehouse lenders.") Possession as contemplated by UCC § 9-313 is also possession for purposes of UCC § 9-203. See UCC § 9-203, Comment 4.

³⁹ UCC §§ 9-203(b)(3)(A)-(B).

⁴⁰ As noted in the discussion of Question One, payment by the maker of a negotiable note to the person entitled to enforce it discharges the maker's obligations on the note. UCC § 3-602. This is the case even if the person entitled to enforce the note is not its owner. As between the person entitled to enforce the note and the owner of the note, the right to the money paid by the maker is determined by the UCC and other applicable law, such as the law of contract and the law of restitution, as well as agency law. See, e.g., UCC §§ 3-306 and 9-315(a)(2). As noted in comment 3 to UCC § 3-602, "if the original payee of the note transfers ownership of the note to a third party but continues to service the obligation, the law of agency might treat payments made to the original payee as payments made to the third party."

⁴¹ For cases in which another person claims an interest in the note (whether as a result of another voluntary transfer by the debtor or otherwise), reference to Article 9's rules governing perfection and priority of security interests may be required in order to rank order those claims (and, in some cases, determine whether a party has taken the note free of competing claims to the note). In the case of notes that are negotiable instruments, the Article 3 concept of "holder in due course" (see UCC § 3-302) should be considered as well, because a holder in due course takes its rights in an instrument free of competing property claims to it (as well as free of most defenses to obligations on it). See UCC §§ 3-305 and 3-306. With respect to determining whether the owner of a note has effectively transferred a property interest to a transferee, however, the perfection and priority rules are largely irrelevant. (The application of the perfection and priority rules can result in the rights of the transferee either being subordinate to the rights of a competing claimant or being extinguished by the rights of the competing claimant. See, e.g., UCC §§ 9-317(b), 9-322(a), 9-330(d), and 9-331(a).)

⁴² For this Illustration, as well as Illustrations 7-11, the analysis under UCC Article 9 is the same whether the mortgage note is negotiable or non-negotiable. This is because, in either case, the mortgage note will qualify as a "promissory note" and, therefore, an "instrument" under UCC Article 9. See UCC §§ 9-102(a)(47), (65).

enforceable security interest in the note. UCC § 9-203(b). This is the case even if Payee's agreement is oral or otherwise not evidenced by an authenticated record. Payee is no longer a person entitled to enforce the note (because Payee is no longer in possession of it and it has not been lost, stolen, or destroyed). UCC § 3-301. Funder is a person entitled to enforce the note if either (i) Payee indorsed the note by blank indorsement or by a special indorsement identifying Funder as the person to whom the indorsement makes the note payable (because, in such cases, Funder would be the holder of the note), or (ii) the delivery of the note from Payee to Funder constitutes a transfer of the note under UCC § 3-203 (because, in such case, Funder would be a nonholder in possession of the note with the rights of a holder). See also UCC §§ 1-201(b)(21)(A), 3-205(a)-(b), and 3-301(i)-(ii).

7. Maker issued a mortgage note payable to the order of Payee. Payee borrowed money from Funder and, in a signed writing that reasonably identified the note (whether specifically or as part of a category or a type of property defined in the UCC), granted Funder a security interest in the note to secure Payee's repayment obligation. Payee, however, retained possession of the note. Funder has an attached and enforceable security interest in the note. UCC § 9-203(b). If the note is negotiable, Payee remains the holder and the person entitled to enforce the note because Payee is in possession of it and it is payable to the order of Payee. UCC §§ 1-201(b)(21)(A), 3-301(i).
8. Maker issued a mortgage note payable to the order of Payee. Payee sold the note to Funder, giving possession of the note to Funder in exchange for the purchase price. The sale of the note is governed by Article 9 and the rights of Funder as buyer constitute a "security interest." UCC §§ 9-109(a)(3), 1-201(b)(35). The security interest is attached and is enforceable. UCC § 9-203(b). This is the case even if the sales agreement was oral or otherwise not evidenced by an authenticated record. If the note is negotiable, Funder is also a person entitled to enforce the note, whether or not Payee indorsed it, because either (i) Funder is a holder of the note (if Payee indorsed it by blank indorsement or by a special indorsement identifying Funder as the person to whom the indorsement makes the note payable) or (ii) Funder is a nonholder in possession of the note (if there is no such indorsement) who has obtained the rights of Payee by transfer of the note pursuant to UCC § 3-203. See also UCC §§ 1-201(b)(21)(A), 3-205(a)-(b), and 3-301(i)-(ii).
9. Maker issued a mortgage note payable to the order of Payee. Pursuant to a signed writing that reasonably identified the note (whether specifically or as part of a category or a type of property defined in the UCC), Payee sold the note to Funder. Payee, however, retained possession of the note. The sale of the note is governed by Article 9 and the rights of Funder as buyer constitute a "security interest." UCC § 1-201(b)(35). The security interest is attached and is enforceable. UCC § 9-203(b). If the note is negotiable, Payee remains the holder and the person entitled to enforce the note (even though, as between Payee and Funder, Funder owns the note) because Payee is in

possession of it and it is payable to the order of Payee. UCC §§ 1-201(b)(21)(A), 3-301(i).

Question Three – What is the Effect of Transfer of an Interest in a Mortgage Note on the Mortgage Securing It?

What if a note secured by a mortgage is sold (or the note is used as collateral to secure an obligation), but the parties do not take any additional actions to assign the mortgage that secures payment of the note, such as execution of a recordable assignment of the mortgage? UCC Section 9-203(g) explicitly provides that, in such cases, the assignment of the interest of the seller or other grantor of a security interest in the note automatically transfers a corresponding interest in the mortgage to the assignee: “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.” (As noted previously, a “security interest” in a note includes the right of a buyer of the note.)

While this question has provoked some uncertainty and has given rise to some judicial analysis that disregards the impact of Article 9,⁴³ the UCC is unambiguous: the sale of a mortgage note (or other grant of a security interest in the note) not accompanied by a separate conveyance of the mortgage securing the note does not result in the mortgage being severed from the note.⁴⁴

It is important to note in this regard, however, that UCC Section 9-203(g) addresses only whether, as between the seller of a mortgage note (or a debtor who uses it as collateral) and the buyer or other secured party, the interest of the seller (or debtor) in the mortgage has been correspondingly transferred to the secured party. UCC Section 9-308(e) goes on to state that, if the secured party’s security interest in the note is perfected, the secured party’s security interest

⁴³See, e.g., the discussion of this issue in *U.S. Bank v. Ibanez*, 458 Mass. 637 at 652-53, 941 N.E.2d 40 at 53-54 (2011). In that discussion, the court cited Massachusetts common law precedents pre-dating the enactment of the current text of Article 9 to the effect that a mortgage does not follow a note in the absence of a separate assignment of the mortgage, but did not address the effect of Massachusetts’s subsequent enactment of UCC § 9-203(g) on those precedents. Under the rule in UCC § 9-203(g), if the holder of the note in question demonstrated that it had an attached security interest (including the interest of a buyer) in the note, the holder of the note in question would also have a security interest in the mortgage securing the note even in the absence of a separate assignment of the mortgage. (This Report does not address whether, under the facts of the *Ibanez* case, the holder of the note had an attached security interest in the note and, thus, qualified for the application of UCC § 9-203(g). Moreover, even if the holder had an attached security interest in the note and, thus, had a security interest in the mortgage, this would not, of itself, mean that the holder could enforce the mortgage without a recordable assignment of the mortgage to the holder. Whatever steps are required in order to enforce a mortgage in the absence of a recordable assignment are the province of real property law. The matter is addressed, in part, in the discussion of Question 4 below.)

⁴⁴ Official Comment 9 to UCC § 9-203 confirms this point: “Subsection (g) codifies the common-law rule that a transfer of an obligation secured by a security interest or other lien on personal or real property also transfers the security interest or lien.” Pursuant to UCC § 1-302(a), the parties to the transaction may agree that an interest in the mortgage securing the note does not accompany the note, but such an agreement is unlikely. See, e.g., Restatement (3d), Property (Mortgages) § 5.4, comment *a* (“It is conceivable that on rare occasions a mortgagee will wish to disassociate the obligation and the mortgage, but that result should follow only upon evidence that the parties to the transfer so agreed.”).

in the mortgage securing the note is also perfected,⁴⁵ with result that the right of the secured party is senior to the rights of a person who then or later becomes a lien creditor of the seller of (or other grantor of a security interest in) the note. Neither of these rules, however, determines the ranking of rights in the underlying real property itself, or the effect of recordation or non-recordation in the real property recording system on enforcement of the mortgage.⁴⁶

Illustration:

10. Same facts as Illustration 9. The signed writing was silent with respect to the mortgage securing the note and the parties made no other agreement with respect to the mortgage. The attachment of Funder's interest in the rights of Payee in the note also constitutes attachment of an interest in the rights of Payee in the mortgage. UCC § 9-203(g).

Question Four – What Actions May a Person to Whom an Interest in a Mortgage Note Has Been Transferred, but Who Has not Taken a Recordable Assignment of the Mortgage, Take in Order to Become the Assignee of Record of the Mortgage Securing the Note?

In some states, a party without a recorded interest in a mortgage may not enforce the mortgage non-judicially. In such states, even though the buyer of a mortgage note (or a creditor to whom a security interest in the note has been granted to secure an obligation) automatically obtains corresponding rights in the mortgage,⁴⁷ this may be insufficient as a matter of applicable real estate law to enable that buyer or secured creditor to enforce the mortgage upon default of the maker if the buyer or secured creditor does not have a recordable assignment. The buyer or other secured party may attempt to obtain such a recordable assignment from the seller or debtor at the time it seeks to enforce the mortgage, but such an attempt may be unsuccessful.⁴⁸

Article 9 of the UCC provides such a buyer or secured creditor a mechanism by which it can record its interest in the realty records in order to conduct a non-judicial foreclosure. UCC Section 9-607(b) provides that “if necessary to enable a secured party [including the buyer of a mortgage note] to exercise ... the right of [its transferor] to enforce a mortgage nonjudicially,” the secured party may record in the office in which the mortgage is recorded (i) a copy of the security agreement transferring an interest in the note to the secured party and (ii) the secured

⁴⁵ See Official Comment 6 to UCC § 9-308, which also observes that “this result helps prevent the separation of the mortgage (or other lien) from the note.” Note also that, as explained in Official Comment 7 to UCC § 9-109, “It also follows from [UCC § 9-109(b)] that an attempt to obtain or perfect a security interest in a secured obligation by complying with non-Article 9 law, as by an assignment of record of a real-property mortgage, would be ineffective.”

⁴⁶ Similarly, Official Comment 6 to UCC § 9-308 states that “this Article does not determine who has the power to release a mortgage of record. That issue is determined by real-property law.”

⁴⁷ See discussion of Question Three, *supra*.

⁴⁸ In some cases, the seller or debtor may no longer be in business. In other cases, it may simply be unresponsive to requests for execution of documents with respect to a transaction in which it no longer has an economic interest. Moreover, in cases in which mortgage note was collateral for an obligation owed to the secured party, the defaulting debtor may simply be unwilling to assist its secured party. See Official Comment 8 to UCC § 9-607.

party's sworn affidavit in recordable form stating that default has occurred⁴⁹ and that the secured party is entitled to enforce the mortgage non-judicially.⁵⁰

Illustration:

11. Same facts as Illustration 10. Maker has defaulted on the note and mortgage and Funder would like to enforce the mortgage non-judicially. In the relevant state, however, only a party with a recorded interest in a mortgage may enforce it non-judicially. Funder may record in the relevant mortgage recording office a copy of the signed writing pursuant to which the note was sold to Funder and a sworn affidavit stating that Maker has defaulted and that Funder is entitled to enforce the mortgage non-judicially. UCC § 9-607(b).

Summary

The Uniform Commercial Code provides four sets of rules that determine matters that are important in the context of enforcement of mortgage notes and the mortgages that secure them:

- First, in the case of a mortgage note that is a negotiable instrument, Article 3 of the UCC determines the identity of the person who is entitled to enforce the note and to whom the maker owes its payment obligation; payment to the person entitled to enforce the note discharges the maker's obligation, but failure to pay that party when the note is due constitutes dishonor.
- Second, for both negotiable and non-negotiable mortgage notes, Article 9 of the UCC determines whether a transferee of the note from its owner has obtained an attached property right in the note.
- Third, Article 9 of the UCC provides that a transferee of a mortgage note whose property right in the note has attached also automatically has an attached property right in the mortgage that secures the note.
- Finally, Article 9 of the UCC provides a mechanism by which the owner of a note and the mortgage securing it may, upon default of the maker of the note, record its interest in the mortgage in the realty records in order to conduct a non-judicial foreclosure.

As noted previously, these UCC rules do not resolve all issues in this field. The enforcement of real estate mortgages by foreclosure is primarily the province of a state's real property law, but legal determinations made pursuant to the four sets of UCC rules described in this Report will, in many cases, be central to administration of that law. In such cases, proper application of real property law requires proper application of the UCC rules discussed in this Report.

⁴⁹ The 2010 amendments to Article 9 (see fn. 8, *supra*) add language to this provision to clarify that "default," in this context, means default with respect to the note or other obligation secured by the mortgage.

⁵⁰ UCC § 9-607(b) does not address other conditions that must be satisfied for judicial or non-judicial enforcement of a mortgage.

APPENDIX A



King County Recorder's Office

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King County Recorder's Office
Administration Building
Room 311
500 4th Avenue
Seattle WA 98104

206-296-1570
206-205-8396 FAX

kcrocust@kingcounty.gov

Frequently asked questions

[I'm having problems connecting to the Records Search. Can you help me?](#)

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[There seems to be a problem when I access your site - when the disclaimer appears whether they select Accept or Decline they receive the Decline message.](#)

[Where can I purchase blank forms for recording?](#)

[Can I search property records to find the owner of a parcel if I have only the address? If so, how?](#)

Helpful Links

- [Property Tax Info](#)
- [Birth and Death Records](#)
- [Divorce Records](#)
- [Change your address](#)

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[I noticed my Social Security Number is visible on a document! What can I do?](#)

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I'm having problems connecting to the Records Search. Can you help me?

Here are a few tips to aid you in resolving your problem:

1. Make sure you meet the minimum system requirements.
Records Search requires Javascript support which is standard in Internet Explorer and Netscape Navigator, versions 4.0 and above.
Internet Explorer 4.0 - 6.0 are fully functional as well as Netscape 4.0 - 6.2 excluding version 6.0.
(Significant compatibility problems exist with Netscape 6.0; most appear to be resolved with version 6.2).
If you are using AOL or other alternate browsers and are experiencing problems, try using Internet Explorer.
Cookie's must be enabled, at least per session.
If you are able to get to the Legal Acceptance page but after clicking 'Accept' are given a message that the page cannot be displayed or are instead redirected to the declined page, check for cookie support. With Internet Explorer 6, go to 'Tools, Internet Options, Privacy' and make sure that the setting is not higher than Medium High or add it (146.129.54.93) to your trusted sites list under the Security tab.

To view online forms and standards (pdf) you need to download and install the Adobe Reader. To view document images you need an image viewer for the image format you choose. For pdf version, you will need Adobe Reader (external link on image format selection page). For the tif version you can use the Imaging for Windows viewer that comes with Windows98, NT4, or later.

2. Isolate the problem to one of three areas: your computer, your network, the King County Recorders website.
Are other people in your area able to access the records search? If so, problem is your computer.
Are people outside of your area able to access the records search but people within your area are not able or are denied access (home, other company, etc) ?
The most common problem is your network firewall blocking non-standard port 8193. We are obligated to use this port for security reasons. You will be able to view the King County Recorders Office main page but are not able to connect to the Records Search application. Contact your network support group about accessing ip/port:146.129.54.93:8193. (Network Admins - firewalls, proxy servers, content management servers, ICAP servers, etc.)
Are any users able to access the records search? System problems on any of three production servers may prevent access for a short period while problems are being resolved. If availability is anticipated to be limited for an extended period, an informational message will be posted on the top of the home page.
(<http://www.metrokc.gov/recelec/records/default.htm>)

3. Clear your local browser cache.
(Internet Explorer) Go to tools, internet options, general, delete files (temporary internet files). (Netscape) Go to edit, preferences, advanced, cache, clear disk cache.

4. Finally, if you are unable to resolve your problem, use the 'Customer Service Questions' link at the bottom of each page. Provide specifics for the operating system and version, browser and version, and internet connection method (corporate network, dial-up, highspeed-cable, etc) as well as results of testing from step 2.

5. The 'Comments' link at the very bottom of each page goes to the King County Web Team and is a required link on all King County web pages. These comments will be forwarded to us when they are reviewed.

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I keep trying to access the records search but it keeps not progressing to the next page, it just refreshes the current page and clears all entries after I click submit.

This problem occurs if you have disabled cookies. If you are using Internet Explorer version 6 or above, you can enable cookies for this site only by going to tools, internet options, privacy, edit and add 146.129.54.93 and click "allow". This will only allow cookies to be stored on your system from the records search application.

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Does the records search web site require that I allow cookies on my computer?

Yes, in order for you to be able to request individual searches, the application needs to be able to uniquely process these requests. The application assigns a random id number (session id) and uses this to identify and return results to the requester. This cookie is stored on your computer and is sent when you request data or images and expires each time your session ends. If you are concerned about allowing cookies on your system, you can turn on support for cookies when you visit this and other sites which require session id's by going to the security tab in your browser and adding (146.129.54.93) to the trusted sites list and deleting it when you have finished.

You can perform a test of cookie support by clicking here: [Cookie Test](#).

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Do you have any satellite offices?

No, but copies of recorded documents are also available at the [King County Archives](#).

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What is your address, hours, and phone number?

[Address, hours, phone number and contact info](#)

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Do you have birth and death records?

No. Please contact [Vital Statistics](#) at (206) 296-4768

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How do I get a copy of my deed? (or any other recorded instrument)

If the document was recorded from **1991 to present**, you can mail a [Copy Request Form](#) or visit the Recorder's Office in person. If mailing a request form, please furnish seller and/or buyer's name, date of purchase, and send the [correct fees](#) only if you know exactly how many pages the record is.

If the document was recorded from **1853 to present**, you can request copies from the [King County Archives](#).

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I tried to request a document from 1971 but got no results. Am I doing something wrong?

No, there are no indexes or images online for that time period. The online index is available from 1976 to present. Images of documents are available from 1991 to present. Indexes prior to 1976 and images prior to 1991 are on microfilm and must be requested from the [King County Archives](#).

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Do you have divorce records?

No. Divorce decrees are filed with the [King County Clerk](#). You may contact them at clerksofficecustomerservice@kingcounty.gov or 206-296-9300.

Additionally, divorce certificates (1968-present only) are available from the [Washington State Center for Health Statistics](#) (external link).

Divorce case files and decrees (1853-1971) are also available from the [Puget Sound Regional Branch of the Washington State Archives](#) (external link).

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How long is the lag between the time a document is recorded and when it is available on the website?

The website uses the same databases that our production application uses and indexing is available the second it is recorded using information that is entered at the time of recording. The image is available when the document is scanned sometime before the end of the day. Additional indexing information is available when the document has been through our indexing department.

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Why do some records return more detail than others?

Over the past 25 years, recording data has been collected from various computer systems. The detail captured by each varies. All information from old systems was transferred to new systems as it was entered in the past.

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I am trying to print an Excise Tax Affidavit but it keeps printing 8 x 11 (standard). How do I change the size to 8 x 14 (legal)?

This is a user selection the same as any word processing document or anything that is printed where you need to select the size of paper. Go to 'File;Print;Properties;Paper Size; Legal (8 1/2 X 14 in)' and then print. You need to have legal sized paper available in your printer.

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How can a person change names on a property title?

When adding someone to title, or changing names on title, people will generally record a conveyance document/deed. You can get blank legal documents at stationary or office supply stores. It needs to be completed and notarized. In addition to that, you will need to complete a Real Estate Excise Tax Affidavit and depending on the type of transaction, you may also need an Excise Tax Supplemental Statement. These two forms can be downloaded from our website Please carefully review the Supplemental Statement which determines whether or not your transaction is taxable.

Once completed, you would bring these forms in to be processed and recorded. Our fees, hours of operation and location can be found on our website. If you need legal advice, please contact an attorney. You can also contact a title insurance company for some assistance.

If you have any further questions for our office, please contact us at 206-296-1570.

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How long does it take for document recording and search requests to be returned by mail?

The turnaround time for recording is 1-2 weeks and for search requests 2-3 weeks.

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How do I get a document removed from public access?

Once a document is recorded with the Recorder's Office, it is part of permanent public record. However, if a document is recorded with a personal identifier such as social security number, mother's maiden name, or driver's license number, it can be restricted from access on our website.

If you have a document with one of these personal identifiers in the body of the document, you can have its access restricted by filling out the "Remove Image from Webpage" form available from our Online Forms and Document Standards page located at <http://www.kingcounty.gov/business/Recorders/OnlineFormsandDocumentStandards.aspx>. We will then record the form and restrict access to that specific document from our website.

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How can one get and record a quit-claim deed, and long will it take?

You can obtain blank Quit Claim Deed forms from office supply stores and some commercial websites. The fee for recording is \$62 for the first page and \$1 for each additional page. The turnaround time can vary depending on how the document is presented to us.

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What are some of the documents that the King County Recorder's Office restricts online?

Some records, including deeds of trust, are not available online to prevent misuse of any personal information they might contain. Copies of those records are available at the [King County Recorder's Office](#) or at the [King County Archives](#).

DOCUMENT TYPES CURRENTLY RESTRICTED:

DEATH CERTIFICATE
DEED OF TRUST
FEDERAL TAX LIEN-NOTICE OF
FTL REVOCATION OF RELEASE
FTL WITHDRAWAL
JUDGMENT
LIEN
LIS PENDENS
MARRIAGE LICENSE APP
MARRIAGE CERTIFICATE
NO FEE LIEN
POWER OF ATTORNEY
PARTIAL RELEASE
FTL RELEASE OF FEDERAL TAX LIEN
RELEASE OR SATISFACTION OF LIEN
RELEASE OF NO FEE LIEN
VETERAN SEPARATION
UCC FILING
UCC AMENDMENT
UCC CONTINUATION
UCC PARTIAL RELEASE
UCC TERMINATION

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Do you accept faxed requests or fax copies back?

No. We only accept mailed in requests that will be returned by mail. If you are mailing in a request for recording, please **do not** include a return envelope with your documents. It will be separated from the documents and discarded because of the high-speed scanning process we use to image your documents.

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Has the indexing of federal tax liens changed recently?

The King County Recorder's Office Web site clarified the term "federal tax lien" to "federal tax lien - notice of" on the Web site drop-down menu which is the title on the image of the document.

This minor change to the document description (not the actual document title) was done to facilitate public access. This in no way changes the document code, the functionality of the document or the intent of the recording and does not impact Federal Tax Lien documents already recorded.

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What are your fees?

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How do I get a copy of my marriage certificate?

In person:

Visit the [King County Recorder's Office](#) or the [King County Archives](#), and you can get your copies the same day. Certificates are available at \$3.00 per certified copy or \$1.00 per noncertified copy. Payment by cash, check or money order is accepted.

By mail:

Please fill out our [Copy Request Form](#) and include the names of the bride and groom and the date of marriage. Also include the correct fee (\$3.00 per certified copy or \$1.00 per noncertified copy) by check or money order only. Requests will be processed within 5 days of being received.

Online:

You can order marriage certificates online with a credit card from the [Washington State Digital Archives](#) for marriages from **1855 and 1989 only**. You must search for

and locate your record, prior to ordering a copy. They charge \$4.00 per certified copy and unofficial images are also available for download for free.

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What is the "National Mortgage Settlement," and how does it affect me?

Five of the nation's largest mortgage servicers recently reached a settlement with the federal government and 48 state attorneys general. This effort, called the National Mortgage Settlement, will provide up to \$25 billion in relief for distressed homeowners. The settlement provides benefits to borrowers whose loans are owned by the settling banks as well as to many of the borrowers whose loans they service.

The settlement provides assistance to:

- Homeowners needing immediate loan modifications
- Homeowners who are underwater on their mortgage, but current on their payment
- Borrowers who lost their home to foreclosure

For more information about the National Mortgage Settlement, visit the [Washington State Attorney General's website](#) or www.NationalMortgageSettlement.com.

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Are there any plans in the future to back scan older documents on microfilm?

Due to budgetary constraints, the County has no plans at this time to back-scan older documents. Requests for these documents are small compared to requests for more recent documents.

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In trying to retrieve a recorded document I got a message saying the doc was over 100 pages and therefore unavailable online.

We limit image retrieval to 100 pages because there are typically 400+ users on the website at any time and it takes a significant time to process these large documents. When this occurs, everyone on the website as well as everyone in the Records office has to wait until the one request is finished. If you click the message, an email will be sent to the Records webmaster who will manually process the document and reply by email when it is available online.

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I downloaded the editable excise tax affidavit and filled it out and printed it but the words are not separated by spaces and some of the boxes are not filled in.

Download the latest version of the free [Adobe Reader](#) (external link). If you still have problems, you can select 'Print As Image' when you print it. It will take a little longer but will almost always print correctly.

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There seems to be a problem when I access your site - when the disclaimer appears whether they select Accept or Decline they receive the Decline message.

This problem may occur if your internet traffic is being routed through a content management server which is stripping out the cookie section from your packets. Send an [email](#) to us and we will assist you making this determination.

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Where can I purchase blank forms for recording?

Office supply and stationery stores

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Can I search property records to find the owner of a parcel if I have only the address? If so, how?

We do not maintain an address field. Our index is by name (Grantor/Grantee) and/or by Instrument number. You can search on a date range by name, but not by address.

In order to find the current tax payer (usually the owner), please search on the [King County Parcel Viewer](#) website or contact the [King County Department of Assessments](#).

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Why isn't your site open 24 hours?

The website itself is usually available 24 hours; however, the two servers that contain the data and images used for Records Searches must be shut down each night at 11:55pm for backup. These servers may have long maintenance jobs scheduled for the weekends, so the search engine may only have partial functionality.

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I noticed my Social Security Number is visible on a document! What can I do?

The King County Recorder understands that while we are responsible for providing low or no-cost documents to the public, we are also keenly aware that privacy is of the utmost importance. Consequently, we do not display images of documents that almost always contain personal identifiers (ssn, Mother's maiden name, etc.) such as Liens, Federal Tax Liens, and marriage certificates. These documents are available from our office and can be requested either by mail or in person.

By law, we are required to make these documents available upon request either by mail or in person. In addition, we are prohibited from altering any record.

Some documents, however, may have been submitted to us for recording with a personal identifier embedded in the document. After reviewing your documents online at (<http://www.metrokc.gov/recelec/records/default.htm> Records Search) and determining that an image contains your Social Security Number, Driver's License Number, or Mother's Maiden Name, you may request that the image be removed from website viewing by doing the following:

1. From our main internet page at (<http://www.metrokc.gov/recelec/records/default.htm>) select from the left task bar the category [Online Forms and Document standards](#).
2. Click the link to the form called "Remove Image From Webpage".
3. Complete the form (please make sure you include ALL recording numbers that contain personal identifiers) and email it by clicking the "Submit by Email" button in the upper right corner or send as an attachment to [Customer Service Questions](#) or print and mail it to the Recorder's Office.

The document will be processed and returned to you when completed.

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Do you have property tax information?

No. Please contact the [King County Department of Finance](#) at (206) 296-3850.

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How do I transfer property?

King County cannot give legal advice. You may want to contact an attorney or title company for this information

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Why are documents watermarked with "Unofficial Document" ?

We are obligated by law ([RCW 36.18.010](#)) to collect fees for official copies of recorded documents. In addition, we have no way of controlling the validity of documents that are not reproduced by a lawful Deputy Recorder. With computer software available on most home computers, the document could be modified and without the watermark, could be presented as being a true and correct copy of an official public record. Our intent is to make available to the public the information contained in the documents that are filed in the Recorder's Office. If an official or certified copy is required, you can request one by completing the [Copy Request Form](#) and either mail it to us with the correct [fees](#) or request copies in person at the [King County Recorder's Office](#).

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Updated: April 12, 2011

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