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CERTIFICATION FROM UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF WASHINGTON AT SEATTLE
(CASE NO. C09-0149 JCC)

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SUPREME COURT
STATE OF WASHINGTON
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KRISTIN BAIN,

Plaintiff,

v.

MORTGAGE ELECTRONIC REGISTRATION SYSTEMS, INC. *et al,*

Defendants.

AMICUS BRIEF OF WASHINGTON BANKERS ASSOCIATION IN SUPPORT OF DEFENDANTS

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I. INTEREST AND IDENTITY OF AMICUS CURIAE

The Washington Bankers Association ("WBA"), founded in 1889, and incorporated in 1970, is an independent, nonprofit organization representing more than 80 member commercial banks operating in every county of the state. The WBA has separately filed a motion for leave to file this brief, which provides additional information on the WBA's identity, its interest in this case, its familiarity with the issues in this case, and why additional argument will assist the Court in deciding the certified questions. The WBA incorporates that motion here.

II. INTRODUCTION

In enacting the Deed of Trust Act ("DTA"), RCW 61.24.005-177, the Washington Legislature carefully balanced three competing goals: "(1) that the nonjudicial foreclosure process should be efficient and inexpensive; (2) that the process should result in interested parties having an adequate opportunity to prevent wrongful foreclosure; and (3) that the process should promote stability of land titles." *Plein v. Lackey*, 149 Wn.2d 214, 225, 67 P.3d 1061 (2003). Plaintiffs ask this Court to upset this balance by adopting a flawed interpretation of the DTA that would defeat the settled expectations of lenders, borrowers, and investors, and interfere with the foreclosure process specifically authorized by the Legislature.

The District Court certified three questions to this Court. In response to the first question, this Court should uphold the designation of Mortgage Electronic Registration Systems, Inc. ("MERS") as beneficiary in deeds of trust, as nominee for the lender and its successors and assigns. The designation of MERS as beneficiary—a common practice here and nationwide—fully complies with the specific language of the DTA and the public policy behind it.

The determination that MERS is a proper beneficiary under the DTA renders moot the second and third certified questions. But if the Court were to reach the second question, it should hold that lenders (or their successors) are proper beneficiaries and may foreclose, judicially or nonjudicially, consistent with the clear intent of the parties, the terms of the loan documents, and the text and goals of the DTA and other principles of Washington law.

The third certified question, whether there is a cause of action against MERS under the Consumer Protection Act ("CPA"), relates only to MERS, and so the WBA does not address it in this brief. Consistent with the certified question, the WBA requests that any ruling on this question be limited to the availability of a CPA claim against MERS.

III. STATEMENT OF THE CASE

Mortgage lenders provide an important service to the American economy. Mortgage loans make home ownership possible for hundreds of thousands of families in Washington and millions of families nationwide, and also enable families to obtain financing to improve their homes, pay off other obligations, or make other purchases. Nationally, mortgage lenders extended over $1.5 trillion of loans in just 2010, and there is an aggregate of more than $13 trillion in outstanding mortgage obligations.[1]

There is always some incidence of default, even in good economic times.[2] The most common causes include the range of unfortunate events that can sometimes disrupt income or repayment ability—unemployment, medical emergencies, and divorce—and not causes attributable to lenders.[3]

Foreclosures are unfortunate but necessary, enabling lenders to recoup funds, engage in new lending, and keep costs low for new borrowers. Unwarranted foreclosure delays, in contrast, hamper the ability of lenders to make new loans and increase costs for borrowers. This reduces demand in the housing market, impairs construction of new homes, reduces consumer spending and investment, reduces access to credit, and limits economic growth.[4] The current foreclosure backlog "now presents the greatest obstacle to a housing market recovery."[5]

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[1] Joel Kan & Mike Fratantoni, *Overcast but Clearing in 2011*, Mortgage Banking, Jan. 2011 (Ex. 1); Mortgage Debt Outstanding, Federal Reserve (Dec. 2011), http://www.federalreserve.gov/econresdata/releases/mortoutstand/current.htm (Ex. 2).

[2] Susan Graham, *Servicing Technology is Getting a WORKOUT*, Mortgage Banking, Mar. 2011 (noting average 4.5 percent default rate from 1990 to 2006) (Ex. 3).

[3] Dep't of Hous. & Urban Dev., Office of Policy Dev. & Research, "Report to Congress on the Root Causes of the Foreclosure Crisis" at 15 (2010) (Ex. 4).

[4] Charles W. Calomiris, Eric James Higgins, and Joseph R. Mason, "The Economics of the Proposed Mortgage Servicer Settlement" at 14 (May 6, 2011), http://ssrn.com/abstract=1833729.

[5] Alex Veiga, *Mortgage Default Warnings Surged in August*, Associated Press, Sept. 15, 2011 (Ex. 5); *Professor Says We Need Faster Foreclosures*, Consumer Bankruptcy News, July 26, 2011 at 5-6 (Ex. 6).

The DTA sets an orderly process for nonjudicial foreclosures. *See* RCW 61.24.005-146. When that process is unduly obstructed, lenders are impaired in obtaining title to the property and reconveying the property to a new buyer who can pay for it. In responding to the certified questions here, the Court has the opportunity to ensure that the DTA continues to operate effectively and within the scope contemplated by the Legislature.

As MERS explains in its brief, the MERS system allows the home mortgage industry to operate more efficiently, providing benefits to both consumers and industry participants. *See also Cervantes v. Countrywide Home Loans, Inc.*, 656 F.3d 1034, 1038-40 (9th Cir. 2011) (describing operation of MERS system). MERS has been accepted in the mortgage industry in Washington and across the country, and MERS appears on some sixty million deeds of trust and mortgages nationwide.

IV. ARGUMENT

A. MERS Is a Proper Beneficiary Under the DTA.

1. The DTA Allows MERS To Serve As A Beneficiary.

For at least three independent reasons, MERS can serve as a beneficiary of a deed of trust under the plain language of the DTA.

First, Washington law expressly contemplates the use of agents in a nominee capacity. MERS is designated in the deed of trust as beneficiary in the capacity as nominee (agent) of the lender and its successors. Plaintiffs concede that the lender could be beneficiary under the deeds of trust but provide no reason why the lender, as principal, cannot authorize an agent to serve as beneficiary on its behalf. And, indeed, such a delegation of authority to an agent is entirely consistent with black letter Washington contract and agency law. *See Sherman v. Millikin*, 9 Wn.2d 339, 341, 114 P.2d 989 (1941).

Moreover, a deed of trust is a type of mortgage, and Washington's mortgage statute (expressly incorporated into the DTA, *see* RCW 61.24.020) provides that that parties to a mortgage "may insert in such mortgage any lawful agreement or condition." RCW 61.12.020. Under Washington law, "[t]here is hardly a limit to the imaginable clauses that may be added to a mortgage or to the accompanying obligation, usually clauses for the protection of the mortgagee." 18 Wm. B. Stoebuck, Wash. Prac., Real Estate § 17.8 (2d ed. 2011). There is certainly no reason in the text or the policy of the DTA that would allow a creditor to act through an agent such as MERS with respect to a mortgage, but not with respect to a Deed of Trust. *See Buse v. First Am. Title Ins. Co.*, 2009 WL 1543994, at *2 (W.D. Wash. 2009) (DTA incorporates agency principles).

Similarly, Washington's Uniform Commercial Code ("UCC") expressly incorporates agency principles for negotiable instruments (like Plaintiffs' promissory notes), and contemplates use of agents in connection with recording transfers of property interests—MERS's role here. RCW 62A.1-103 (incorporating agency principles); RCW 62A.9A-502(a) (financing statement sufficient if it identifies debtor, the "name of the secured party ***or a representative of the secured party***," and identifies covered collateral) (emphasis added).

MERS's role is consistent with Washington common law as well, which has endorsed the MERS-type agency model for more than a century. Washington courts have consistently held that agents may enforce the rights of principals even when the agent does not own the debt, and even in the context of foreclosure. *See, e.g., Carr v. Cohn*, 44 Wash. 586, 588, 87 P. 926 (1906) (nominee to whom property has been deeded without consideration and merely as title-holder for grantors, to convey as they might direct, can bring quiet title action on deed); *Andrews v. Kelleher*, 124 Wash. 517, 534-36, 214 P. 1056 (1923) (agent for bond holders had authority to prosecute suit foreclosing mortgage). The clause in Plaintiffs' deeds of trust identifying MERS as the nominal beneficiary (agent) of the lender (principal) complies with Washington law.

Second, although no more is needed, MERS falls within the plain language of RCW 61.24.005(2), in which the definition of "beneficiary" is not limited to just the note holder.

Third, the definition of "beneficiary" in RCW 61.24.005(2) contemplates flexibility in its application by virtue of the language "unless the context clearly requires otherwise." Here, "the context clearly requires" that MERS be the beneficiary: that is what the plaintiffs and the lenders unequivocally and unambiguously agreed to.[6]

[6] *See, e.g., Torgerson v. One Lincoln Tower, LLC*, 166 Wn.2d 510, 517, 210 P.3d 318 (2009) ("It is black letter law of contracts that the parties to a contract shall be bound by its terms."); *Corales v. Flagstar Bank, FSB*, 2011 WL 4899957, at *5 (W.D. Wash. 2011) ("This court has repeatedly rejected the argument that MERS is not a proper beneficiary under a Deed of Trust where the plaintiff has executed a deed which expressly acknowledges MERS's status as a beneficiary.").

The second and third arguments are articulated at length in MERS' briefs, and the WBA references but does not repeat them here.

2. Sound Public Policy Supports MERS's Role as a Proper "Beneficiary" Under the DTA.

As noted above, the Legislature enacted the DTA to promote three goals: (1) to erect an efficient and inexpensive nonjudicial foreclosure process; (2) to provide an adequate opportunity for interested parties to prevent wrongful foreclosure; and (3) to foster the stability of land titles. *Plein*, 149 Wn.2d at 225; *see also* Joseph L. Hoffmann, Comment, *Court Actions Contesting The Nonjudicial Foreclosure of Deeds of Trust in Washington*, 59 WASH. L. REV. 323, 330 (1984). To achieve these goals, the DTA establishes "a comprehensive scheme for the nonjudicial foreclosure process, including specific remedies for grantors and borrowers facing the potential loss of their homes." *Vawter v. Quality Loan Serv. Corp.*, 707 F. Supp. 2d 1115, 1123 (W.D. Wash. 2010). But, as courts have recognized, "[e]njoining facially legitimate foreclosure sales is not in the public interest." *Kudina v. CitiMortgage, Inc.*, 2011 WL 5101760, at *2 (W.D. Wash. 2011).

Adopting plaintiffs' strained interpretation of the DTA could lead to widespread delays or deferrals of legitimate foreclosures, where loans are in irreconcilable default. This result looms because such a ruling would raise questions about the ability to foreclose a MERS deed of trust nonjudicially. The ruling that plaintiffs seek could delay or prevent lenders from reselling the properties securing loans which are in default, thus hampering lenders from making new loans to borrowers who can repay them, impairing the construction of new homes, reducing consumer spending and investment, reducing access to credit, and limiting economic growth.[7]

The result that plaintiffs seek could also have yet another unintended result: creating confusion and potentially clouding title to many parcels of real estate now or previously secured by MERS deeds of trust throughout Washington, interfering with the stability of the State's land records, contrary to the third primary goal of the DTA. The WBA's concern is real: confusion and market illiquidity is precisely what happened in Michigan for six months after a divided appellate court upset longstanding Michigan law by holding that MERS foreclosures were

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[7] The creation of improper impediments to nonjudicial foreclosures could lead to more judicial foreclosures, burdening courts and increasing costs for borrowers and lenders alike. This would be plainly contrary to the purpose of the DTA. *See* Final Bill Report, ESSB 6191 (June 11, 1998) ("The Deed of Trust Act ... was designed to avoid time consuming and expensive judicial foreclosure proceedings and to save time and money for both the borrower and lender."). And judicial foreclosures delay the recovery of the housing market due to the post-sale redemption period that keeps properties in limbo for a year after a foreclosure judgment, delaying the transfer of properties to owners who can pay for them. RCW 6.23.020(1).

Increased reliance upon judicial foreclosures would not only potentially harm the already fragile economy of the State but it would do so without creating any corresponding material benefit to borrowers. The DTA's nonjudicial foreclosure provisions protect borrowers by allowing them to cure their default by coming current on the loan (plus costs and fees), rather than being required to repay the entire amount of the accelerated principal balance, as borrowers must do in judicial foreclosure proceedings. RCW 61.24.090. In addition, in a nonjudicial foreclosure, borrowers are protected against deficiency judgments, but no such protections apply to judicial foreclosures. RCW 61.24.100.

Regardless of the merits of judicial versus nonjudicial foreclosure, the Legislature made a calculated decision to allow nonjudicial foreclosure, and Plaintiffs agreed to it in their deeds of trust. Any decision improperly interfering with nonjudicial foreclosure would upset that Legislative determination.

invalid. Title insurers stopped insuring properties, making it difficult for buyers to purchase, live in, renovate, or otherwise invest in property,[8] and plaintiffs filed eleven putative class action lawsuits (and numerous individual lawsuits) seeking to overturn completed foreclosures, even where third parties had purchased the foreclosed properties.[9] Although those issues dissipated after the Michigan Supreme Court reversed the appellate court and upheld the validity of MERS foreclosures, *Residential Funding Co., LLC v. Saurman*, 490 Mich. 909, 805 N.W.2d 183 (2011), the experience in Michigan shows the very real potential for confusion and uncertainty that could result here from an incorrect and overly narrow interpretation of the DTA. Even borrowers who satisfied their mortgage loan obligations could face legal difficulties with title where MERS executed the satisfactions or reconveyances.

The State's land records would further be negatively affected if the Court holds that lenders may not designate MERS or any other agent as beneficiary.[10] Such a ruling would have both short-term effects—requiring assignments out of MERS—and long-term impacts—causing county recorders to become overburdened with documents reflecting every

[8]Cami Reister, *Home sales stay steady; But for just June, closed deals were 20 percent lower than a year ago*, Grand Rapid Press (July 14, 2011) (Ex. 7); Nick Tirimaos & Ruth Simon, *Effort on Home Loans Stalls*, Wall Street Journal (Sept. 19, 2011) (Ex. 8)

[9] *Banacki v. OneWest Bank, FSB*, 2011 U.S. Dist. LEXIS 119906, at *2-3 (E.D. Mich. 2011).

[10] Taking title to real property by deed as nominee for an undisclosed principal is common and recognized in Washington law. *See, e.g.*, RCW 11.98.070(8) (trustee of trust may take title to assets in the name of nominee); WAC 458-61A-214 (real estate excise tax provides exemption for transfer of real property from nominee to principal).

change in a loan's ownership. Before the creation of MERS, the high volume of loan sale transactions resulted in the creation of millions of assignments that were tendered to county recorders for processing. This flood of paperwork, perhaps predictably, led to errors in recorders' offices, where missing and erroneous assignments "threaten[ed] the integrity of the lending process."[11] Because of the voluminous paperwork, "[a]ssignments were late, in the wrong sequence, or not made, all of which caused huge problems."[12] Recording error rates as high as 33% were common, and resulted in clouding title to property.[13] MERS "greatly simplif[ied] a terribly cumbersome, paper-intensive, error-prone, and therefore costly process for transferring and tracking mortgage rights."[14] Prohibiting the designation of MERS (or any agent) as beneficiary would be a step backward, forcing county recorders' offices to return to the pre-MERS days of unnecessary but inevitable errors, backlogs, and delays.

MERS was created by a joint effort of lending industry participants and regulators.[15] MERS deeds of trust have been filed in public land records since 1997, and the Legislature has never amended the DTA to

[11] Allen H. Jones, *Setting the Record Straight on MERS*, Mortg. Banking, May 2011 at 34 (Ex. 9).

[12] Katie Oppy, *The MERS Reality: The Electronic Tracking of Mortgage Rights in the United States*, 15(4) HOUSING FINANCE INTERNATIONAL 41 (June 2001) (Ex. 10).

[13] R.K. Arnold, *Yes, There Is Life on MERS*, 11 Prob. & Prop. 33, 33-34 (1997).

[14] Slesinger, Phyllis K., Daniel McLaughlin, *Mortgage Electronic Registration System*, 31 IDAHO L. REV. 805, 808 (1994-95).

[15] Howard Schneider, *MERS Aids Electronic Mortgage Market*, Mortgage Banking (Jan. 1, 1997) (Ex. 11); Carson Mullen, *MERS: Tracking Loans Electronically*, MORTGAGE BANKING at 64 (May 2000) (Ex. 12).

forbid MERS from operating in this capacity. A ruling resulting in a practical inability of MERS to serve as beneficiary would upset the settled expectations that have resulted from the widespread acceptance of MERS deeds of trust throughout the past fifteen years.

3. Prohibiting the Use of an Agent Raises Issues Beyond the Role of MERS.

The question of whether an agent may be used as a deed of trust beneficiary raises issues that go far beyond the role of MERS, upsetting myriad common commercial transactions. In many municipal and corporate bond transactions, an indenture trustee is appointed to act for a large group of widely dispersed bondholders and, if there is real property collateral for the bonds, the indenture trustee is named as beneficiary of the deeds of trust securing the bonds. Similarly, in large multi-bank commercial loans, the lead bank is generally appointed as the "administrative agent" and is named as the secured party under the security agreements and as beneficiary under any deeds of trust. In that capacity, the lead bank has the power to act for the entire bank group in matters relating to the collateral. For example, *Andrews v. Kelleher*, *supra*, dealt with a mortgage held by a bond trustee for the benefit of a group of bondholders and the court treated that as an unremarkable situation. *See* 124 Wn. 517, 534-36, 214 P. 1056 (1923).

If creditors in these types of arrangements are not allowed to act through an agent as beneficiary, management of deeds of trust securing bonds and syndicated credit facilities would become unwieldy to the detriment of both borrowers and creditors. Indeed, if every bondholder must be named individually as one of a group of beneficiaries consisting of all the bondholders, ***every*** bondholder would have to sign any request for reconveyance upon payoff of the debt—potentially many hundreds of bondholders, or in the case of a syndicated commercial credit facility, often dozens of banks. This impractical requirement would throw commercial transactions into chaos and disadvantage all parties. *See* Special Report of the WSBA Legal Op. Comm.: Op. on Deeds of Trust in Favor of Agents, Tr. and Nominees (July 12, 2011) (Ex. 13)[16] ("In sophisticated commercial financings, it is common for a deed of trust to name a beneficiary that may not be the holder of the secured obligations. … In some situations (e.g., widely held secured bond obligations), there is no practical alternative."). Thus, a ruling invalidating MERS's role as an agent for the beneficiary could have widespread and detrimental consequences beyond the residential real estate market.

4. Significant Judicial Authority Recognizes MERS's Status As Beneficiary Or Mortgagee.

In recent months, a number of State Supreme Courts have held that MERS can exercise the rights of a beneficiary or mortgagee under state law, even though MERS does not hold or own the promissory note. *E.g., Trotter v. Bank of N.Y. Mellon*, --- P.3d ----, 2012 WL 206004 (Idaho Jan. 25, 2012); *RMS Residential Props., LLC v. Miller*, 303 Conn. 224, 32 A.3d 307 (2011); *Residential Funding Co.*, 490 Mich. at 909. Indeed, in

[16] Also available at www.wabuslaw.org/Documents/LegalOpinions/Deeds_Of_Trust.pdf.

Michigan, the state that plaintiffs argue has "the statute most analogous to Washington's deed of trust statute" (Bain Opening Br. at 38; *see also* Selkowitz Opening Br. at 22), the Supreme Court recently held that MERS could conduct foreclosures despite not owning loans, reversing an aberrant appellate ruling. *Residential Funding Co.*, 490 Mich. at 909.

In addition, the vast majority of appellate courts in both the state and federal systems have repeatedly rejected claims similar to plaintiffs', holding that MERS may be designated beneficiary or mortgagee even though it does not own loans.[17]

B. Even if the Court Were To Find that MERS Is Not a Proper Beneficiary, Promissory Notes Remain Secured and Properly Authorized Parties Can Initiate and Complete Foreclosures.

For all of the reasons stated above, the Court should conclude that MERS is a proper beneficiary under the DTA, thereby mooting the second certified question. But if the Court were to reach the second question, it should hold that the loans at issue remain secured and subject to the non-judicial foreclosure rights of lenders. Any other result would upset the expectations of both lenders and borrowers, would be contrary to public policy, and would be damaging to the state and national economies.

[17] *E.g.*, *Commonwealth Prop. Advocates, LLC v. Mortg. Elec. Registration Sys., Inc.*, --- F.3d ----, 2011 WL 6739431, at *7 (10th Cir. 2011); *Cervantes*, 656 F.3d at 1042; *Horvath v. Bank of N.Y., N.A.*, 641 F.3d 617, 620 (4th Cir. 2011); *Trent v. Mortg. Elec. Registration Sys., Inc.*, 288 F. App'x 571, 572 (11th Cir. 2008); *Commonwealth Prop. Advocates v. Mortg. Elec. Registration Sys., Inc.*, 263 P.3d 397 (Utah Ct. App. 2011); *Calvo v. HSBC Bank USA, N.A.*, 199 Cal. App. 4th 118, 125, 130 Cal. Rptr. 3d 815 (2011); *Athey v. Mortg. Elec. Registration Sys., Inc.*, 314 S.W.3d 161, 166 (Tex. App. 2010).

In a residential loan transaction, a lender gives money to a borrower to buy a property, and the borrower signs a note promising repayment and a deed of trust (or mortgage) giving a security interest in the property in case of default. *Cervantes*, 656 F.3d at 1039. Lenders would not have made unsecured loans without the ability to enforce the security interest by exercising the power of sale if the loan is not repaid.

The allegedly improper act here is the designation of MERS, as an agent of the lender—rather than the lender itself—as beneficiary under the deeds of trust. The deeds of trust also contain a severability clause, stating that if any term in the contract is determined to be invalid, the remainder of the contract will remain valid and enforceable.[18]

Under these circumstances, if the Court determines that the designation of MERS as beneficiary is ineffective under the DTA, the Court should give effect to the expressed intent of the parties, strike the invalid portion, and enforce the remainder of the contract. *See Zuver v. Airtouch Communications, Inc.*, 153 Wn.2d 293, 320, 103 P.3d 753, 768 (2004) ("when parties have agreed to a severability clause in [a contract], courts often strike the [invalid] provisions to preserve the contract's essential [terms of agreement]") (citations omitted). Because the only defect alleged here is the designation of the lender's agent—

[18] No. 2:09-cv-149, Dkt. # 131-2 at 11 of 18; No. 3:10-cv-5523, Dkt. # 9-1 at 12 of 34.

rather than the lender itself—as beneficiary under the deed of trust, this would leave the lender as the designated beneficiary under the trust deed.[19]

This result is consistent with the intent of the parties, which was to create a secured loan subject to a valid security instrument protecting the interests of the lender. It is also consistent with the well-established principle that the security follows the debt, and that a transfer of the promissory note evidencing the debt carries with it the deed of trust, regardless of whether a deed of trust assignment is created. *Fidelity and Deposit Co. of Md. v. Ticor Title Ins. Co.*, 88 Wn. App. 64, 943 P.2d 710 (1997); *see also Cervantes*, 656 F.3d at 1044 ("Even if MERS were a sham beneficiary, the *lenders* would still be entitled to repayment of the loans and would be the proper parties to initiate foreclosure after the plaintiffs defaulted on their loans.") (emphasis added).

Alternatively, as MERS proposes, MERS could cure any technical violation of the DTA by assigning its interest in the trust deeds to the lender. This would allow the lender to serve as beneficiary of record—which plaintiffs concede is proper—during the foreclosure process.

It is apparent is what the remedy should *not* be: a wholesale retroactive invalidation of tens or hundreds of thousands of trust deeds. Such a result would create a destructive windfall that is repugnant not only

[19] This could be accomplished easily enough. The deeds of trust state, in relevant part, that "the beneficiary of this Security Instrument is MERS (solely as nominee for Lender and Lender's successors and assigns)." After striking the allegedly invalid provision—the phrase "MERS solely as nominee for"—the provision in question would read, "the beneficiary of this Security Instrument is Lender and Lender's successors and assigns."

to the DTA but also to basic principles of contract law. *Cf. Lunsford v. Saberhagen Holdings, Inc.*, 166 Wn.2d 264, 278, 208 P.3d 1092 (2009) ("Where changes in the law cannot be made without undue hardship, we have discretion to apply a new rule of law purely prospectively[.]").

Indeed, it is unclear whether plaintiffs seek such an extreme result. Apart from asserting that the designation the MERS violates the CPA, Plaintiff Bain does not directly address the remedy issue. *See generally* Bain Opening Br. at 38-43. Plaintiff Selkowitz's proposed remedy is rescission, Selkowitz Opening Br. at 38-43, but that remedy is improper because the purportedly ineffective act—the lender's decision to designate an agent to serve as beneficiary (with the consent of the borrower) rather than the lender serving as beneficiary itself—did not "vitally affect the basis upon which the parties contract[ed]." *Public Util. Dist. No. 1 v. Wash. Public Power Supply Sys.*, 104 Wn.2d 353, 362, 705 P.2d 1195 (1985). Because the identity of the beneficiary was not at the core of the parties' exchange, and the borrowers received the benefit of their bargains, rescission is not a proper remedy. *Simonson v. Fendell*, 101 Wn.2d 88, 92, 675 P.2d 1218 (1984); *see Denaxas v. Sandstone Court of Bellevue, LLC*, 148 Wn.2d 654, 668-69, 63 P.3d 125 (2003).[20]

[20] Even if rescission were available, it would be inappropriate as to Plaintiffs, who have not alleged their ability or willingness to repay their loans. *Simonson*, 101 Wn.2d at 93 ("The general principle is that rescission contemplates restoration of the parties to as near their former position as possible or practical."); *Yamamoto v. Bank of N.Y.*, 329 F.3d 1167, 1171 (9th Cir. 2003).

C. Unwarranted Assertions About MERS Should Not Factor in this Court's Decision.

In his briefs, Plaintiff Selkowitz makes a series of unwarranted assertions about MERS that are not supported by the record and are, in fact, wrong. These claims should have no effect on the Court's consideration of the certified questions. And, in any event, as the Ninth Circuit has held, the designation of MERS as beneficiary in deeds of trust does not harm borrowers. *Cervantes*, 656 F.3d at 1042 ("[T]he plaintiffs have failed to show that the designation of MERS as a beneficiary caused them any injury by, for example, affecting the terms of their loans, their ability to repay the loans, or their obligations as borrowers.").

For example, Plaintiff Selkowitz, citing nothing, contends that MERS was developed to conceal "the identity of the true note holder." Selkowitz Opening Br. at 15. But county land records are not a clearinghouse for loan ownership information;[21] rather, land records provide notice of liens and establish their priority. RCW 65.08.070; *Bank of Am., N.A. v. Prestance Corp.*, 160 Wn.2d 560, 570, 160 P.3d 17 (2007); *Kim v. Lee*, 145 Wn.2d 79, 86, 31 P.3d 665 (2001) ("The purpose of the recording statute is to make the deed first recorded superior to any outstanding unrecorded conveyance of the same property unless the mortgagee or purchaser had actual knowledge of the transfer not filed of record."). Indeed, recording is not mandatory, and plaintiffs have no standing to complain about how lenders choose to protect their security

[21] *See In re Cushman Bakery*, 526 F. 2d 23, 30 (1st Cir. 1975).

interests. *See Bates v. Mortg. Elec. Registration Sys., Inc.*, 2011 WL 1304486, at *3 (D. Nev. 2011) (challenge to alleged failure to record deed of trust assignments is "legally frivolous").

Built on his erroneous understanding of land records, Selkowitz draws conclusions—such as that MERS was designed to avoid lender liability for predatory loans and makes wrongful foreclosure claims "almost impossible to litigate"—that are entirely mistaken and unsupported. Selkowitz Opening Br. at 15 & 16. Borrowers know who they borrowed money from. And they know who is foreclosing on the property. *See* RCW 61.24.040(b), (f). Nothing about MERS serving as beneficiary prevents a plaintiff from suing to stop foreclosure (as Selkowitz has done).

Moreover, Selkowitz's focus on loan ownership is misguided because mortgage loans are serviced by a bank or servicing company. Servicers, not owners, typically handle interactions with borrowers and are generally responsible for loan modifications, short sales, and foreclosures. *See Cervantes*, 656 F.3d at 1039; 12 U.S.C. §§ 2605(i)(2), (3) (defining loan servicers and servicing).[22] That is why borrowers "should not care who actually owns the Note ... so long as they do know who they should

[22] *See, e.g.*, Fannie Mae Single Family Servicing Guide, June 2011 at 800-1 et seq. (defining tasks of servicer to carry out foreclosure), *available at* https://www.efanniemae.com/sf/guides/ssg/svcg/svc061011.pdf; Freddie Mac Single-Family Seller/Servicer Guide at chs. 64-69 (providing guidelines on delinquencies, loss mitigation through loan modification or short sale, foreclosure, and other relevant tasks), *available at* http://www.allregs.com/tpl/Main.aspx; 15 U.S.C. § 1639a (establishing duties for mortgage servicers engaged in loss mitigation).

pay." *In re Veal*, 450 B.R. 897, 912 (B.A.P. 9th Cir. 2011). The identity of the servicer is on every monthly statement or other letter the consumer receives, and federal law requires notice of the identity of the servicer and, in some instances, of the note holder as well. 12 U.S.C. §§ 2605(b), (c); 15 U.S.C. §§ 1641(f)(2), (g)(1).[23]

Selkowitz also blames MERS for the "marketing and securitization of subprime loans," Selkowitz Opening Br. at 19, but Selkowitz does not allege that he received a subprime loan and relies entirely on law review articles by a financially-interested law professor.[24] Selkowitz even blames MERS for the "mortgage banking melt-down and related problems" (Selkowitz Reply at 8-9), but he relies entirely on two articles that *do not even mention MERS.* The WBA strongly disagrees with his assertions. The secondary market arose decades before MERS was created, as part of a national policy goal set by Congress.[25] In the experience of the WBA and its members, the secondary market has enabled the growth of

[23] Selkowitz's assertion that lack of ownership information in land records prevents borrowers from exercising rescission rights is also false. Selkowitz Opening Br. at 28-30. As he acknowledges, since 2004 borrowers have been expressly permitted to exercise their right to rescind by serving an agent of the loan owner, such as the servicer. *Id.* at 30.

[24] Petersen Dep. at 69:7-19 (Ex. 14) (professor stands to gain up to $5 million if his anti-MERS theories gain acceptance).

[25] Thomas P. Lemke, Gerald T. Lins, and Rita J. Kummer, "Mortgage-Backed Securities: Developments and Trends in the Secondary Mortgage Market" (2011-12 ed.) §§ 1:6, 1:7, 1:11, 1:13; *see also In re Fannie Mae Sec. Litig.*, 247 F.R.D. 32, 34 (D.D.C. 2008) ("Fannie Mae is one of two (the other being Freddie Mac) federally-chartered government-sponsored enterprises that serve the public policy of expanding home ownership to moderate and low-income families, in part, by supplying capital and liquidity for residential mortgages.")

mortgage credit such that thousands of Washingtonians and millions of Americans own homes today because of modern lending innovations. But, ultimately, the issues in this case require interpretation of the DTA, not a subjective judgment about perceived benefits or detriments of the secondary market.[26]

In another speculative and unsupported concern, Selkowitz raises the "threat of double liability." Nothing in the record supports this "threat," and, in any event, the DTA prohibits deficiency judgments on nonjudicially foreclosed residential loans (RCW 61.24.100) and any Deed of Trust can be foreclosed on only once. Selkowitz identifies not one instance of double liability in the fifteen years since MERS was created.

V. CONCLUSION

For the foregoing reasons, the WBA respectfully requests that the Court answer the first certified question in the affirmative, holding that MERS is a proper beneficiary under the DTA. This would moot the second certified question. Alternatively, if the Court were to reach the second certified question, the WBA respectfully requests that the Court hold that the loans remain secured and subject to foreclosure under the DTA, with the lender (or its successors) designated as beneficiary.

[26] Plaintiff Bain's assertion that MERS deeds of trust are "true contracts of adhesion" relates to concepts of unconscionability and are irrelevant to the analysis of the questions certified to the Court. Bain Reply at 8.

RESPECTFULLY SUBMITTED this 14th day of February, 2012

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CERTIFICATE OF SERVICE

I hereby certify that on February 14, 2012, I caused to be served a copy of the foregoing document on the following person(s) in the manner indicated below at the following address(es):

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I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

Executed on this 14th day of February, 2012, at Seattle, Washington.

Leah Burrus

Exhibit 1

FOCUS - 4 of 44 DOCUMENTS

Mortgage Banking

January 2011

SECTION: COVER REPORT: BUSINESS OUTLOOK; Pg. 26 Vol. 71 No. 4 ISSN: 0730-0212

ACC-NO: 21937

LENGTH: 3524 words

HEADLINE: OVERCAST but CLEARING in 2011

BYLINE: Kan, Joel; Fratantoni, Mike.

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BODY:

ABSTRACT

Gross domestic product (GDP) growth has been revised up for the third quarter and most forecasts will likely reflect stronger growth into next year. The stronger growth has been partially driven by increased consumer spending -- as overall conditions and expectations improve, people are gaining confidence and spending again. Moreover, businesses continue to spend on capital goods and information technology, albeit at a slower rate than in recent months. The Federal Reserve is a rather unusual institution -- an independent agency within the executive branch, with significant ability to impact the economy, but substantially insulated from political pressure by design and historical tradition. Inflation continued to decline, leading many economists to fear that the US might actually experience deflation, with prices -- rather than just inflation -- falling. The US is currently running budget deficits in the range of 9% to 10% of national income.

FULL TEXT

There are a few good signs of better economic times ahead. But next year also promises to bring higher mortgage rates. This review of the Fed's policy moves, budget deficits and the housing forecast concludes the sun may start peeking out in late 2011.

As of this writing, we continue to slowly emerge from the deepest recession in years. Most economic indicators point to a slightly better picture than they did last summer. Although the sun is not yet shining, economically speaking, there are patches of lighter gray amidst the overcast sky. And the sun may begin peeking out in late 2011 and early 2012. * Gross domestic product (GDP) growth has been revised up for the third quarter and most forecasts, including ours (the Mortgage Bankers Association's research division), will likely reflect stronger growth into next year. The stronger growth has been partially driven by increased consumer spending - as overall conditions and expectations improve, people are gaining confidence and spending again.

* Job growth appears to be picking up, with the October and November employment situation reports showing significant payroll increases in the private sector and weekly jobless claims at their lowest levels in more than two years. Moreover, businesses continue to spend on capital goods and information technology (IT), albeit at a slower rate than in recent months. I Despite this job growth, unemployment and labor underutilization remain high. We expect that given the current path of economic growth, the unemployment rate will remain above 9 percent in 2011, and over 8 percent well through 2012. There are still large numbers of workers who are discouraged, marginally attached to the work force, or who have been forced to take a temporary job. As of November, about 42 percent of the unemployed have been looking for a job for more than six months. * The job market is instrumental in the recovery of the housing sector because homeownership and mortgage performance hinge directly on households' incomes. A loss of employment or income is one of the "trigger" events for mortgage delinquency, and in a declining home-price environment homeowners cannot easily sell their homes if they are no longer able to afford their mortgage payments. And those who can afford their mortgage payments may be faced with a loan balance that is still greater than the value of their home.

The housing sector is still crawling along the bottom, as home prices continue to fall by most measures. A large inventory overhang of unsold homes remains, as well as a significant "shadow inventory" - homes that are either in foreclosure or with mortgages that are delinquent and that could potentially come onto the market as a result of their nonperforming mortgage status.

Purchase application data are just beginning to reattain levels last seen in early May, immediately following the expiration of the homebuyer tax credit. Until we see a sustainable and significant rate of job and income growth, as well as a better consumer outlook for the future, home-price growth will continue to either decline or grow slowly, with variations by market increasing as the recovery develops.

Finally, there are risks also from abroad - specifically the possibility of a currency war as other countries move to devalue their currencies relative to the U.S. dollar and more sovereign debt crises in other European countries, as seen most recently in the case of Ireland.

Given this economic backdrop, prices and wages are unlikely to increase, and inflation will remain contained for now. However, we think that the recovery is for real, and coupled with the end of the Fed's most aggressive actions to jump-start the economy, rates are likely on a slow uphill climb from here.

We anticipate that the ??-year Treasury is likely to be at 3.5 percent by the end of 2011 and 4 percent by the end of 2012. We expect the 30-year mortgage rate will move above 5 percent by the end of 2011 and push closer to 6 percent by the end of 2012 (see Figure 1).

In the remainder of this article, we review the Fed's recent actions, discuss the outlook for the federal budget and examine the implications of both in the context of our economic forecast. We also examine the outlook for mortgage originations in the year ahead.

Monetary policy considerations

Monetary policy has typically been shrouded in mystery. How can the Federal Reserve "manage" the economy through the setting of a single short-term interest rate? As in other settings, no two economists will give you exactly the same answer on this.

The Federal Reserve is a rather unusual institution - an independent agency within the executive branch, with significant ability to impact the economy, but substantially insulated from political pressure by design and historical tradition.

Even with this background, the Fed's actions over the past few years have been extraordinary and perhaps more perplexing to the "uninitiated" outside of the central bank. Consider the following:

* The Federal Reserve's balance sheet swelled from roughly $700 billion in early 2008 to more than $2 trillion by the end of that year (see Figure 2).

* The Fed's holdings expanded from being primarily short-term Treasury securities and discount-window loans to banks, to include commercial paper and other money market instruments, loans to broker-dealers, swaps with other central banks, longer-term Treasuries, and significant holdings of mortgages and agency debt.

* During a relatively short period at the end of 2008 and into 2009, the Federal Reserve loaned in excess of $3 trillion to virtually every sector of the U.S. economy, and to many foreign entities as well. Without this lending, it appears, some of the biggest names in finance and industry would not have been able to survive.

Arguably, of greatest interest to the mortgage industry, were the Fed's purchases of mortgage assets - $1.25 trillion of agency mortgage-backed securities (MBS) purchased through 2009 and into the first quarter of 2010, which led to record low mortgage rates. (The Fed also purchased $170 billion of agency debt securities, which provided further indirect support to the mortgage market.) The rate on 30-year fixed loans remained within a narrow band of 4.8 percent to 5.1 percent for much of that 15-month period.

This venture into "quantitative easing," targeting a quantity of asset purchases rather than a rate, was an untested monetary policy tool. However, as the shortterm rate target was already as low as it could go (the Federal Funds rate had been at essentially o percent since the beginning of 2009) and the economy was in free fall and losing hundreds of thousands of jobs per month, the Fed must have determined such a move was absolutely necessary.

Adjustments to the program were made along the way, notably extending the program through the first quarter of 2010 and allowing for a gradual tapering off oi purchases to allow the private sector time to get back in. As a result, when the Fed left the mortgage market at the end of March, there was little reaction evidenced in either the level or the volatility of mortgage rates.

The European sovereign debt crisis, with Greece at the forefront in early 2010, led to a global flight to quality. That brought U.S. Treasury rates significantly lower, and mortgage rates followed them down. Despite these unprecedented low rates, the job market in the United States continued to sag, with the unemployment rate remaining near 10 percent.

Meanwhile, inflation continued to decline, leading many economists to fear that the United States might actually experience deflation, with prices - rather than just inflation - falling. (The United States during the Great Depression, and Japan over the past two decades, were caught in a debt-deflation spiral as prices and incomes dropped, and borrower defaults increased, which led to further drops in asset prices and further reductions in other prices and incomes.)

Moreover, growing concern regarding outsized budget deficits and accumulating public debt, (something policymakers encountered during midterm elections), meant that it was infeasible to suggest another fiscal stimulus either through additional spending or tax cuts.

We discuss the budget outlook in the next section, but suffice it to say, monetary policymakers at the Fed did not believe that fiscal policy measures were available to help the economy, and believed they needed to step into the breach to try to increase aggregate demand.

Beginning as early as the middle of the summer of 2010, Federal Reserve officials began to hint that another round of asset purchases by the central bank could be used to try to bring interest rates down further. This was seen as a way to potentially stimulate households and businesses to increase their spending either through new financing or through refinancing at lower rates. By early fall, the Fed had signaled it was certainly going to start a new round of purchases, and it would likely be limited to the purchase of longer-term Treasury securities, but it did not clearly indicate the size of QE2 - the second round of quantitative easing.

Just this announcement that the Fed would be acting to buy Treasuries brought longer-term rates down, and mortgage rates reached new record lows. However, uncertainty remained regarding the specifics of the QE2 program. Some Fed officials indicated that the program could be incremental, with perhaps S 100 billion of purchases announced at their November meeting, with clear indications that additional purchases would be dependent upon economic developments. Others indicated the Fed's purchases could be substantially larger, perhaps exceeding Si trillion and taking place over more than a year.

The November meeting announcement, indicating that $600 billion would be purchased over eight months, was quite close to market expectations, and interest rates actually increased slightly that day.

Subsequently, the level of uncertainty regarding the future of QE2 has only increased.

Kevin Warsh, a governor of the Federal Reserve, indicated in a Wall Street Journal op-ed that the program would be subject to ongoing review. With the G-20 international meetings as a backstop, finance ministers around the world criticized the Fed's actions, fearing that it would weaken the dollar and increase U.S. exports at the expense of their countries.

And in mid-November, many conservative U.S. economists signed a letter indicating that the policy was misguided and inherently inflationary. The net result of all this noise is investors have come to doubt the resolve of the Fed, and longer-term rates have risen as a result - as of Thanksgiving week, 30-year fixed mortgage rates were at their highest level since June 2010.

Our outlook is that the unemployment rate will remain high over the medium term, likely above 8 percent at the end of 2012. With that level of unemployment, inflation is likely to remain low, and thus the Fed will be unlikely to raise short-term rates over this time period. However, at some point, it will need to unwind the growth in its portfolio and reduce the level of excess bank reserves currently in the system.

Fed officials insist that they have the means to do this. The Fed is already allowing its mortgage assets to run off as loans amortize or prepay, replacing the MBS with longer-term Treasuries. At some point, it will more actively reduce these holdings through large-scale repurchase agreements or outright sales. The Fed also has developed a term deposit program as another means of tying up bank reserves to forestall a jump in lending that could spark inflation.

The Federal Reserve System is filled with remarkably talented and dedicated individuals. But no central bank has ever attempted such a maneuver on this scale. And the costs of getting it wrong are huge - essentially a return to levels of inflation that we have spent the past 30 years painfully wringing out of our economy. Investors are not sending a signal of no confidence, but they are appropriately wary.

The federal budget outlook and longer-term rates

Perhaps the most worrisome aspect to some regarding QE2 is that the popular shorthand for the program, "the Fed is printing money to buy government debt," conjures fears that the United States may end up repeating some of the worst episodes in economic history. In the past, countries that could not sell their debt to any investor forced their central bank to buy it, which led to hyperinflation à la Weimar Germany.

No one is seriously suggesting that hyperinflation is a risk here. However, any serious analyst who looks at the U.S. budget situation is right to be worried.

The United States is currently running budget deficits in the range of 9 percent to 10 percent of national income (see Figure 3). The publicly held debt has increased from about 45 percent of national income to more than 60 percent, and is headed toward 70 percent by 2020 even if significant spending cuts and/or tax increases are made. It could go much higher - 80 percent to 100 percent - if such heroic spending and tax changes are not made.

As indicated by Congressional Budget Office (CBO) Director Douglas Elmendorf, "Those are numbers that are not very common among developed countries. We are pushing our way toward debt levels that we don't have experience with in this country, [and that raises the risk that] people will be concerned enough not to want to buy so much U.S. debt at current interest rates."

President Obama's National Commission on Fiscal Responsibility and Reform suggested a range of deep spending cuts, large tax increases and major reductions in existing entitlement programs. Other parties have suggested complementary plans. Even were these draconian plans to be enacted, there would still be upward pressure on longer-term rates over the medium term. These pressures are reflected in our outlook for rates - namely that longer-term rates have turned a corner and are going to be headed higher.

Without a serious change in the deficit and debt outlook, there is a risk that longer-term rates could head much higher than we envision currently.

The sovereign debt crises experienced to date by Greece, Ireland, Portugal and Spain, and the dramatic cuts in government spending adopted by the United Kingdom and others are wake-up calls to the United States. Market confidence can turn on a dime, sending rates spiking higher or shutting off credit to countries.

We do not think this will happen to the United States, but policymakers need to act to bring deficits down and curtail the growth in debt before we reach a crisis point.

The outlook for mortgage originations

Rising mortgage rates will slow refinance volumes, while a gradually improving housing market should lead to only a modest increase in purchase activity. Complicating this picture is the fact that underwriting standards remain quite tight, and regulatory activity around the definition of a qualified residential mortgage (QRM) and other new rules stemming from the Dodd-Frank Wall Street Reform and Consumer Protection Act are likely to only further tighten standards.

We expect total mortgage originations of roughly $1 trillion in 2011 - a significant drop from $1.5 trillion in 2010 and $2 trillion in 2009.

There were repeated refinance wavelets as rates fell during the past two years, and most borrowers who had an incentive and were able to refinance (i.e., to lower their monthly payments, lock in a fixed rate or refinance into a mortgage product more suited to their financial goals) have already done so. The contract rate for a 30year fixed-rate mortgage (FRM) averaged a little over 5 percent in 2009 and is around 4.7 percent to date in 2010. The rate has been below 5 percent for the past seven months.

For borrowers ineligible to refinance based on their credit profile, lack of equity in their home or employment situation, rates will likely remain relatively low for the next year, so opportunities should continue to exist if their situations change.

As shown in Figure 4, there are a considerable number of agency mortgages outstanding with a significant refinance incentive. Those with coupons higher than 5 percent, roughly $2 trillion, represent a portion of those unable to refinance. Most in the non-agency universe, another $500 billion in loans, have also been largely locked out.

Refinance originations will decline sharply in 2011 as the pool of eligible borrowers and borrowers who stand to benefit from a refinance shrinks. The refinance wave persisted longer into 2010 than we had first anticipated,, as lenders had to extend refinance timelines to process the high volume of purchase transactions earlier in the year - many of which had to be done in advance of the tax credit deadline.

Additionally, with much of their resources devoted to other industry efforts (modifications, reporting and compliance), lenders faced some staffing constraints that also hampered processing of originations in general.

As rates continue to rise, refinance activity will fall through 2012.

Purchase originations are closely tied to the health of the housing sector - both the volume of sales and the path of home prices. A large excess supply of homes remains on the market. The stock of existing homes for sale remains high, coupled with the threat of additional inventory from homes tied to loans that are seriously delinquent. This keeps downward pressure on home prices, even though housing starts have remained at extraordinarily low levels.

For households with a secure income, however, the lower prices combined with historically low mortgage rates may prove to be a good incentive for them to purchase a home. We have seen some life of late in mortgage applications for home-purchase transactions, existing-home sales and pending-home sales (see Figure 5).

We expect that purchase originations will fall in 2010 relative to 2009, given that the second phase of the homebuyer tax-credit program expired in the spring of 2010, after which home sales fell 25 percent between the second and third quarters. Sales have not really picked up significantly since.

Purchase originations should increase in 2011 and 2012 as home sales and housing starts begin to strengthen again.

An improving economy, rising rates and a tougher year

In summary, the net effect of these factors - frustratingly slow improvements in the economy and housing markets, an overextended federal government and a Fed that has run out of options - means that mortgage rates are likely to rise. This will cause refinance volumes to plum met, but purchase volumes are unlikely to increase much due to the lingering weakness in the job market.

Those patches of light gray in the still-dark sky are promising, but more so for 2012 and beyond than for 2011.

There are, of course, both upside and downside risks to the current outlook. At press time, one immediate threat to growth is the fact that the issue of extension of the Bush-era tax cuts had not yet been fully resolved. It appears possible that a deal negotiated between the White House and congressional Republicans could get enacted, but if the tax cuts are not extended, consumers will undoubtedly receive a hit to their paychecks in January - and they would cut back their spending in the near future as a consequence.

If this were to lead to renewed fears of deflation or even a double-dip, rates could drop again and refinance volumes could end up higher than what we're currently forecasting.

On the other hand, both business and consumer spending are lagging due to lack of confidence in the future. Expectations about future demand can turn quickly, and can create virtuous cycles that could accelerate the rate of growth in both the housing market and the broader economy. Of course, this would mean higher mortgage rates and lower refinance volumes, only partially offset by an increase in purchase activity.

Happy New Year!

SIDEBAR

The European sovereign debt crisis, with Greece at the forefront in early 2010, led to a global flight to quality.

SIDEBAR

Those patches of light gray in the still-dark sky are promising, but more so for 2012 and beyond than for 2011.

GRAPHIC: Illustrations
IMAGE GRAPH, Figure 1 Mortgage and Treasury Rate Forecast, Figure 2 Federal Reserve's Balance Sheet
IMAGE TABLE, Figure 3 Projected Budget Deficits and Surpluses in CBOs Baseline (S Billions)
IMAGE GRAPH, Figure 4 Mortgage-Backed Securities (MBS) Outstanding by Coupon (as of Sept. 30, 2010), Figure 5 Mortgage Originations

LOAD-DATE: February 1, 2011

Exhibit 2

Board of Governors of the Federal Reserve System

Mortgage Debt Outstanding

Release Date: December 2011

Mortgage Debt Outstanding (1.54)

Millions of dollars, end of period

	Type of holder and property	2007	2008	2009	2010Q3	2010Q4	2011Q1	2011Q2	2011Q3
1	All holders	14,512,918	14,604,569	14,321,810	13,910,266	13,813,196	13,718,721	13,641,306	13,559,119
	By type of property								
2	One- to four- family residences	11,167,755	11,067,436	10,864,711	10,581,357	10,522,012	10,450,441	10,395,496	10,336,091
3	Multifamily residences [1]	784,628	837,674	846,966	839,553	837,698	838,909	839,705	840,904
4	Nonfarm, nonresidential	2,447,854	2,566,444	2,478,077	2,354,377	2,317,257	2,294,164	2,271,929	2,248,993
5	Farm	112,682	133,015	132,056	134,979	136,228	135,208	134,175	133;131
	By type of holder								
6	Major financial institutions	5,064,584	5,044,358	4,778,069	4,610,344	4,583,535	4,469,555	4,435,959	4,433,847
7	Commercial banks [2]	3,644,402	3,841,344	3,818,641	3,674,367	3,651,215	3,550,914	3,521,933	3,515,315

8	One- to four-family	2,210,542	2,247,146	2,261,515	2,194,805	2,204,761	2,128,423	2,116,488	2,130,454
9	Multifamily residences	168,407	215,118	211,035	204,254	197,149	193,788	192,508	189,825
10	Nonfarm, nonresidential	1,223,569	1,328,516	1,296,007	1,223,890	1,197,438	1,177,224	1,161,850	1,144,345
11	Farm	41,884	50,564	50,084	51,418	51,867	51,479	51,087	50,691
12	Savings Institutions [3]	1,094,009	860,586	633,327	617,809	614,839	600,216	590,881	589,331
13	One- to four-family	878,958	666,338	448,633	436,982	430,480	419,312	412,845	410,869
14	Multifamily residences	92,705	65,199	59,897	59,453	61,248	61,237	60,999	61,731
15	Nonfarm, nonresidential	121,464	128,130	123,913	120,499	122,217	118,771	116,152	115,792
16	Farm	882	919	884	875	894	896	885	939
17	Life insurance companies	326,173	342,428	326,101	318,168	317,481	318,425	323,145	329,201
18	One- to four-family	9,393	10,177	5,627	5,772	6,163	6,316	6,704	7,175
19	Multifamily residences	51,837	51,755	48,507	47,420	47,246	47,386	48,087	48,986
20	Nonfarm, nonresidential	252,193	267,106	257,721	252,034	251,310	252,056	255,784	260,567
21	Farm	12,750	13,390	14,246	12,942	12,762	12,667	12,570	12,473
22	Federal and related agencies	725,455	801,153	816,071	5,142,366	5,127,547	5,162,350	5,127,767	5,073,942
23	Government National Mortgage Association	22	41	152	4,499	5,277	5,793	6,205	6,585
24	One- to four-family	22	41	152	4,499	5,277	5,793	6,205	6,585
25	Multifamily residences	0	0	0	0	0	0	0	0
26	Farmers Home Administration[4]	78,411	82,517	88,364	90,733	91,533	92,030	93,678	95,120
27	One- to four-family	13,024	13,288	14,062	14,952	15,109	15,130	15,267	15,387
28	Multifamily residences	11,282	11,069	10,980	10,912	10,910	10,883	10,862	10,835
29	Nonfarm, nonresidential	50,839	54,670	59,444	60,690	61,254	61,811	63,207	64,469
30	Farm	3,266	3,490	3,878	4,179	4,260	4,206	4,342	4,429
31	Feder Housing Admin. and Dept. of Veterans Affairs	3,700	3,464	4,257	3,962	4,076	4,181	4,250	4,305
32	One- to four-family	553	176	608	729	803	948	1,064	1,150

33	Multifamily residences	3,147	3,287	3,650	3,233	3,273	3,234	3,187	3,155
34	Resolution Trust Corporation	0	0	0	0	0	0	0	0
35	One- to four-family	0	0	0	0	0	0	0	0
36	Multifamily residences	0	0	0	0	0	0	0	0
37	Nonfarm, nonresidential	0	0	0	0	0	0	0	0
38	Farm	0	0	0	0	0	0	0	0
39	Federal Deposit Insurance Corporation	226	9,808	15,613	7,370	5,683	5,779	5,211	3,302
40	One- to four-family	67	2,890	7,239	3,403	2,686	2,455	2,383	1,418
41	Multifamily residences	0	175	37	185	181	194	67	99
42	Nonfarm, nonresidential	160	6,743	8,337	3,782	2,815	3,131	2,762	1,785
43	Farm	0	0	0	0	0	0	0	0
44	Federal National Mortgage Association	403,577	429,493	416,543	2,977,037	2,989,997	3,023,731	3,001,252	2,969,447
45	One- to four-family	311,831	312,052	296,129	2,808,621	2,819,447	2,851,853	2,828,462	2,794,668
46	Multifamily residences	91,746	117,441	120,414	168,416	170,550	171,878	172,790	174,779
47	Federal Land Banks	67,423	76,503	80,329	81,706	83,496	83,422	84,221	85,134
48	One- to four-family	20,630	18,802	23,148	21,154	21,808	22,195	23,460	24,845
49	Farm	46,793	57,701	57,181	60,552	61,688	61,227	60,761	60,289
50	Federal Home Loan Mortgage Corporation	79,776	111,476	138,816	1,911,897	1,885,139	1,887,589	1,875,571	1,853,308
51	One- to four-family	23,876	38,755	54,878	1,829,006	1,799,256	1,803,437	1,793,769	1,771,717
52	Multifamily residences	55,900	72,721	83,938	82,891	85,883	84,152	81,802	81,591
53	Federal Agricultural Mortgage Corporation	768	786	760	1,070	1,303	1,502	1,616	1,669
54	Farm	768	786	760	1,070	1,303	1,502	1,616	1,669
55	Mortgage pools or trusts[5]	7,401,163	7,547,558	7,595,967	3,066,041	3,038,647	3,033,237	3,024,415	3,011,967
56	Government National Mortgage Association	443,461	636,612	880,270	1,046,179	1,089,761	1,135,597	1,180,598	1,221,685
57	One- to four-family	405,818	597,206	836,761	996,463	1,037,538	1,081,813	1,124,607	1,163,646

58	Multifamily residences	37,643	39,406	43,509	49,716	52,223	53,784	55,991	58,039
59	Federal Home Loan Mortgage Corporation	1,717,342	1,801,735	1,838,919	16,440	17,081	19,813	23,367	25,248
60	One- to four-family	1,706,684	1,786,906	1,824,656	4,344	4,243	4,146	4,038	3,932
61	Multifamily residences	10,658	14,829	14,263	12,096	12,838	15,667	19,329	21,316
62	Federal National Mortgage Association	2,299,072	2,518,408	2,653,034	29,540	28,872	28,349	28,831	28,652
63	One- to four-family	2,259,257	2,479,878	2,605,083	27,646	27,015	26,519	27,018	26,898
64	Multifamily residences	39,815	38,530	47,951	1,894	1,857	1,830	1,813	1,754
65	Farmers Home Administration[4]	0	0	0	0	0	0	0	0
66	One- to four-family	0	0	0	0	0	0	0	0
67	Multifamily residences	0	0	0	0	0	0	0	0
68	Nonfarm, nonresidential	0	0	0	0	0	0	0	0
69	Farm	0	0	0	0	0	0	0	0
70	Private mortgage conduits	2,936,745	2,586,130	2,219,258	1,970,080	1,899,174	1,846,248	1,788,415	1,734,687
71	One- to four-family[5]	2,179,131	1,868,204	1,548,532	1,338,182	1,277,170	1,223,042	1,174,498	1,128,186
72	Multifamily residences	123,994	113,241	107,393	102,663	98,724	98,036	96,286	94,110
73	Nonfarm, nonresidential	633,620	604,685	563,333	529,235	523,280	525,170	517,631	512,391
74	Farm	0	0	0	0	0	0	0	0
75	Federal Agricultural Mortgage Corporation	4,543	4,673	4,486	3,802	3,759	3,230	3,204	1,695
76	Farm	4,543	4,673	4,486	3,802	3,759	3,230	3,204	1,695
77	Individuals and others [7]	1,321,716	1,211,501	1,131,703	1,091,515	1,063,467	1,053,579	1,053,165	1,039,363
78	One- to four-family	1,056,445	938,538	866,478	830,732	809,237	800,759	802,948	794,110
79	Multifamily residences	97,465	94,876	95,366	96,395	95,591	96,819	95,964	94,662
80	Nonfarm, nonresidential	166,009	176,595	169,322	164,247	158,944	156,000	154,543	149,644
81	Farm	1,796	1,492	537	141	-305	1	-290	946

1. Multifamily debt refers to loans on structures of five or more units. Return to table
2. Includes loans held by nondeposit trust companies but not loans held by bank trust departments. Return to table

3. Includes savings banks and savings and loan associations. Return to table
4. FmHA-guaranteed securities sold to the Federal Financing Bank were reallocated from FmHA mortgage pools to FmHA mortgage holdings in 1986:Q4 because of accounting changes by the Farmers Home Administration. Return to table
5. Outstanding principal balances of mortgage-backed securities insured or guaranteed by the agency indicated. Return to table
6. Includes securitized home equity loans. Return to table
7. Other holders include mortgage companies, real estate investment trusts, state and local credit agencies, state and local retirement funds, noninsured pension funds, credit unions, and finance companies. Return to table

Source: Based on data from various institutional and government sources. Separation of nonfarm mortgage debt by type of property, if not reported directly, and interpolations and extrapolations, when required for some quarters, are estimated in part by the Federal Reserve. Line 70 from LoanPerformance Corporation and other sources.

Last update: December 23, 2011

Exhibit 3

FOCUS - 1 of 2 DOCUMENTS

Mortgage Banking

March 2011

SECTION: COVER REPORT: TECHNOLOGY; Pg. 46 Vol. 71 No. 6 ISSN: 0730-0212

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HEADLINE: Servicing Technology Is Getting a WORKOUT

BYLINE: Graham, Susan.

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BODY:

ABSTRACT

The evolution of human society has been a story of constantly adapting new technologies and tools to overcome physical limitations. In the past century, most of these developments enhanced the way people communicate or simplified an increasingly complex workflow. In the mortgage industry, technological advancement has been primarily driven by the need to simplify labor-intensive processes and enhance communications. But that innovation was almost exclusively built around streamlining mortgage originations -- not servicing. Servicing departments require not only software to manage payments and escrow, but also tools to handle default situations, analyze data and properly report to investors and regulatory agencies. Any discussion of servicing technology challenges in 2011 begins with the ongoing default crisis facing America's lenders. Servicers need software that can dig deeply into a portfolio's loan data. No matter what features a servicing department selects for its software platform, one of the primary considerations is the integrity of the borrower data.

FULL TEXT

Servicing technology is handling a heavy workload in the current demanding default environment. Here are some quick ways to evaluate if your platform is up to today's challenges.

The evolution of human society has been a story of constantly adapting new technologies and tools to overcome our physical limitations. In the past century, most of these developments enhanced the way we communicate or simplified an increasingly complex workflow. * Just as manufacturers adopted machinery and robotics into their assembly lines, we witnessed communications evolve from the written letter to the telephone to the digital network. * In the mortgage industry, technological advancement has been primarily driven by the need to simplify labor-intensive processes and enhance communications. But that innovation was almost exclusively built around streamlining mortgage originations - not servicing.

* During the 1990s, the federal government encouraged the government-sponsored enterprises (GSEs) to expand their role in providing home loans for lower-income borrowers. In 2003, Congress passed the American Dream Down Payment Act and in 2004 it passed the Zero-Down Payment Initiative, which paved the way for low-down-payment purchases by first-time homebuyers using GSE financing. * Lenders - and the technology providers supporting them - responded with gusto. * Automated underwriting engines made it easier for lenders to manage a larger selection of loan products by enabling a single loan officer to input specific data and get an almost instantaneous response regarding the particular loan products for which a borrower qualified. Soon lenders were automating everything from the generation of documents to compliance checks to secondary market preparations.

Yet while it seemed the very DNA of loan origination was changing rapidly, the rate of change within the servicing industry was more deliberate and slow, and the technologies driving servicing departments kept pace.

However, the economic realities of the past few years have pushed the need for servicing innovations to the forefront.

Evolving from payments to risk management

On the servicing side of the mortgage process, the technology needs have always required a different approach due to the long-term nature of the servicing relationship among borrowers, lenders and investors.

Servicing departments require not only software to manage payments and escrow, but also tools to handle default situations, analyze data and properly report to investors and regulatory agencies.

Originally, servicing platforms were designed to simply automate the workflow needed to process mortgage payments, with default rates hovering around 4.5 percent. With loans performing at a fairly predictable rate, innovations within servicing software were developed to meet the needs of the times - primarily automating the processing of payments and management of escrow accounts.

Servicing platforms developed in the 1990s and early 2000s focused primarily on speed and efficiency because servicers were always looking for ways to successfully manage the most loans with as few resources as possible.

The next major development in servicing software came about to support the need for communications between servicers and investors. As mortgage-backed securities (MBS) became more complex, servicers demanded more reporting capabilities from their systems. These resources enabled servicers to give investors deeper insight into the performance of individual loans, as well as portfolio-wide performance.

In 201 1, the challenges posed by the servicing side of the mortgage business will continue to push the capabilities of servicing software platforms. Servicing platforms will be required to better manage defaults, communicate with investors and borrowers, and provide the flexibility to handle rapidly changing compliance demands.

Challenge: Getting a handle on defaults

Any discussion of servicing technology challenges in 201 1 begins with the ongoing default crisis facing America's lenders. While economists continue to debate the particulars of the housing market collapse in 2007, the fallout was immediate and severe.

Historically, default rates for mortgages remained steady, with the U.S. Census Bureau showing that 30-day default rates averaged 4.5 percent from 1990 to 2006. However, in 2007, the 30-day default rate rose quickly to 5.4 percent, then 6.9 percent in 2008 and 9.3 percent in 2009.

The Mortgage Bankers Association's (MBA's) November 2010 National Delinquency Survey found that 30-day delinquencies had dropped back slightly to 9.1 percent at the end of the third quarter of last year. While this is a modestly positive sign that defaults may be trending back toward historical levels, this still represents a default rate of nearly twice the average seen in the previous two decades.

How best to handle the high number of defaults remains open to debate. The private sector, government and consumer advocates all have proposed various suggestions on the best way to manage the more than 6.8 million homes that are in some stage of default.

These proposals range from temporary foreclosure freezes, such as the one adopted by Charlotte, North Carolina-based Bank of America and other lenders in October 2010 in response to the "robo-signing" controversy, to government-backed modification programs such as the Home Affordable Modification Program (HAMP) implemented by the federal government in 2009.

Regardless of the method used to manage defaults, servicers must rely on their technology platforms to help manage the complicated process of evaluating, modifying, servicing and disposing of loans in default.

The key to managing defaults is first and foremost one of evaluation. Servicers need software that can dig deeply into a portfolio's loan data. Using business rules and filtering, these loans then can he sorted into risk categories. These programs can also help provide insight into the best course of action regarding a particular default.

Challenge: Keeping investors happy

Working with investors has become more difficult as well. Many private-label mortgage-backed security issuers pulled out of the market in 2007, and government-backed loans now dominate the marketplace.

Servicers' software platforms must support compliance with investor guidelines and facilitate reporting on a regular basis to investors in both the private and public sectors.

Today, the overwhelming need is for software that can communicate and comply with government-backed secondary mortgage market investors. According to National Mortgage News, the combined market share of Fannie Mae, Freddie Mac and Ginnie Mae was 91 percent of every new mortgage funded in the first half of 2010.

Robert Arellano, chief financial officer for El Paso, Texas-based Rocky Mountain Mortgage, says that government investor functionality is a primary consideration in the selection of servicing software. Governmentbacked investors such as Ginnie Mae require very specific reporting and accounting standards. Meeting the guidelines and reporting using the required formats are challenging without the functionality built into the servicing platform.

"Ginnie Mae servicing is very complex and, if it is not done correctly, the agency can end their relationship with the lender," he says. "We use our servicing platform to automate the reporting and to ensure that all the standards the investor demands are met."

Challenge: Communicating with borrowers

Communication challenges are not limited to just investors, however. Servicers must still communicate effectively with borrowers, and their needs and preferences are evolving as well.

In some cases, borrowers are walking away from a mortgage in complete frustration. They can't get their servicer on the phone. They don't know what their options are. They don't know the consequences of defaulting. So when borrowers are severely underwater on their loan, some walk away without ever speaking to their servicer.

And communication is not limited to inbound phone calls. Today's borrowers expect and demand constant access to information via the Internet or a mobile device. Online banking research firm Online Financial Innovations, Seattle, said in a January report, Online Banking Report: 201 1 to 2020 Online & Mobile Banking Forecast, "Through the end of 2020, we project an increase of 40 [million] to 45 million U.S. households using mobile banking, to a total of nearly 60 million."

Consumers are more closely monitoring their personal finances, and many are choosing to do so online. Having online access to account data is no longer a luxury in today's marketplace - it is expected. It is necessary for servicers to make payment details, escrow account information, loan balances and payment histories, as well as ways to contact the lender, easily available in a secure online location if they wish to maintain effective communications with borrowers.

This becomes even more important when working with at-risk borrowers. New Orleans-based Standard Mortgage uses its servicing platform to run regular reports to identify those borrowers who display signs of possible default, and then proactively contacts them via a number of communications channels.

"Once we identify at-risk borrowers, we proactively reach out to these borrowers by e-mail, mail and phone to begin identifying loss-mitigation options that they may be eligible for," says Glenn Weiler, senior vice president for Standard Mortgage Corporation.

"But we don't limit our communications to at-risk borrowers. Customers can log onto a secure website to check their statements, review escrow activity and make both single payments or schedule recurring payments." Weller adds that more than 21,000 of Standard Mortgage's customers are registered to use the online loan portal.

Servicers can also use online communications as a means to provide more tracking of required documents. For those customers who are willing to communicate via e-mail, digital documents provide a traceable method of sending loan statements, adjustable-rate mortgage (ARM) change notices, year-end statements and other communications.

The cost savings of electronic communication can be a significant benefit as well. Servicers can realize significant savings on printing and postage alone by shifting more communications online. This can also reduce a lender's environmental impact - an issue that is very important to a significant portion of the consumer marketplace.

There will always be a portion of the customer base that still prefers paper-based statements and phone support. Be sure to consider how well your servicing software will export statement and loan data to the many vendors that offer services to generate the statements and coupon books. Ensure call centers have full and immediate access to loan information and real-time payment applications to provide customers with the tools necessary to exceed their expectations.

Challenge: Keeping the regulators satisfied

This year is already shaping up to be another year marked by a host of new regulatory changes. While servicers have always had to work within a specific regulatory framework, the challenge in 2011 is keeping up with new compliance guidelines and laws that, in some cases, seem to change on a regular basis.

The Dodd-Frank Wall Street Reform and Consumer Protection Act, passed in 2010, will play the largest role as new implementing rules are proposed and finalized throughout the year. Servicers will also need to comply with ongoing government efforts to reduce foreclosures and keep borrowers in their homes.

Servicers typically undergo formal reviews or audits, depending on the agency responsible for oversight. These reviews can be a more subjective, comprehensive analysis of the health of the lender's servicing department. Some exams look at the technologies, processes and outputs related to the soundness of business practices, while other exams are more data-driven, with examiners determining whether loans are being serviced within established guidelines.

One of the keys to compliance and avoiding issues in regulatory and investor reviews is to have a servicing system in place that supports timely and accurate reporting. Servicing software should provide an automated means to aid in compliance and have reporting capabilities to easily provide the required paper trail that examiners and auditors need to verify compliance.

Ensuring the integrity of loan data

No matter what features a servicing department selects for its software platform, one of the primary considerations is the integrity of the borrower data. Servicers need access to, and control of, all of the loan file data in a database. Being able to completely access the data enables servicers to customize reports, set up business rules and configure the software to present proprietary or situation-specific loan data. There are many vendors offering a wide range of services, so accessing all database information is crucial to cost-efficiently create interfaces and extract the necessary data.

The issue of data is an important one, since many software companies are changing the structure of software. Hosted software and software as a service (SaaS) models often provide the advantages of lower implementation costs, but the issue of how data are stored and how much control the lender has over the data varies greatly.

Eric Haines, managing director of operations for Irving, Texas-based iServe Servicing Inc., says full access to data makes everything from better customer communications to investor reporting more manageable.

"A lot of servicing shops are not set up to have interaction with investors," Haines says. "The linkage of technology is tremendously important, and accessing and working with customer data in our servicing platform is critical to working with our investor base and ensuring the homeowner, investors and servicing work toward the same goals."

The security of the data must also be heavily considered. For servicers that choose to host their own databases, they will have internal processes in place to ensure security. This process works especially well for financial institutions with multiple borrower relationships, since the customer data provides a broad picture of the total accounts, from mortgages to deposit accounts.

Security through hosted providers varies. The best companies take security very seriously and employ neeessary safeguards, but others leave room for improvement. This means the servicer must do the due diligence needed to ensure that data will be secure from identity theft, fraud or loss.

Consider all the factors when selecting a platform

Every lender has a different set of needs and demands in its servicing shop. While there are several options that can provide the basic ability to process payments and escrow, servicers need to evaluate what their needs truly are and select a servicing platform that best fits their needs and budget.

One of the first factors most servicers will have to account for is that the servicing platform integrates smoothly with existing software. This is especially critical for the loan origination software, since a strong integration can eliminate data re-entry and ensure better accuracy between the systems.

Beyond functionality, though, lenders should also examine how the company providing the software will work with the lender.

Key questions that need to be answered include how training is handled, how the software is updated, what other hardware or network purchases will be required and how the vendor will provide ongoing support.

Kay Shelley, vice president and mortgage servicing manager for Fort Worth, Texas-based Texas Banc Mortgage Co., says the strong ongoing support provided by her company's servicing software vendor was a key factor in its purchase.

"When you can get immediate feedback and answers to your questions every time you call, it shows that the vendor cares about their product and cares about their customers," Shelley says. "The software itself is very easy to use and meets our needs, but it is the outstanding service and training that makes using our system a truly positive experience."

The greatest innovations typically come at the time of greatest need. While the mortgage crisis - and the resulting defaults, regulatory changes and investor demands - have dramatically increased the pressure on servicing departments, the technology available to meet these challenges is evolving rapidly. Servicers that select servicing platforms featuring full data control, compliance safeguards and investor support will likely be more prepared to handle whatever changes come barreling down the road in 2011.

SIDEBAR

The key to managin defaults is first and foremost one of evaluation.

SIDEBAR

There will always be a portion of the customer base that still prefers paperbased statements and phone support.

SIDEBAR

The greatest innovations typically come at the time of greatest need.

GRAPHIC: Illustrations

LOAD-DATE: March 26, 2011

Exhibit 4

Report to Congress on the Root Causes of the Foreclosure Crisis

U.S. Department of Housing and Urban Development
Office of Policy Development and Research

2. Literature Review

2.1 General Literature on Causes of Foreclosures and Delinquencies

There is a rich economics literature examining the cause of mortgage foreclosures, generally referred to as "default" in the literature.[26] As noted in detailed reviews of this literature by Quercia and Stegman (1992) and Vandell (1995), since the 1980s, this literature has been dominated by an option-based theory of mortgage default, where the mortgage contract is viewed as giving homeowners an option to "put" the home back to lenders by defaulting on their mortgage. In an option-theoretic view, the primary factor driving defaults is the value of the home relative to the value of the outstanding mortgage; when the home value falls substantially below the mortgage debt, owners are better off by ceding the home to the lender.[27] This type of situation has been characterized in the literature as a "ruthless default," where borrowers simply walk away from their mortgage obligations when it is in their financial interest to do so.

However, as argued most prominently by Vandell (1995) and Elmer and Seelig (1999), a lack of housing equity by itself generally does a poor job of predicting mortgage delinquencies, which are a necessary precursor to foreclosures. As these papers point out, it is generally understood that most borrowers become delinquent due to a change in their financial circumstances that make them no longer able to meet their monthly mortgage obligations. These so called "trigger events" commonly include job loss or other income curtailment, health problems, or divorce. Both Vandell and Elmer and Seelig argue that foreclosures are most accurately thought of as being driven by a two-stage process: a first trigger event that produces financial illiquidity among borrowers which is then coupled with a lack of home equity that makes it impossible for the borrower to either sell their home to meet their mortgage obligation or refinance into a mortgage that is affordable given their change in financial circumstances. In this view, a lack of home equity is an important determinant of foreclosures as it precludes other means that borrowers can take to resolve an inability to meet their mortgage obligations, but foreclosures are most commonly triggered by some other event that makes borrowers financially insolvent.

For the most part, the literature provides numerous examples to support the view that most defaults are not ruthlessly driven by falling house prices. One of the first articles to put forth an option-theoretic view of mortgage default was Foster and Van Order (1984, 1985). However, the data on Federal Housing Administration (FHA) borrowers used in their analysis show that only 4.2 percent of borrowers with estimated loan-to-value ratios of 110 percent or higher actually defaulted on their mortgage. Ambrose and Capone (1998), again examining data on FHA borrowers, find that loans with negative equity accounted for a small share of all loans that became seriously delinquent and also a minority of loans that ended in foreclosure. More recently, Foote, Girardi, and Willen (2008) examine data on all homeowners in Massachusetts over a 20-year period and found

[26] Technically, mortgage "default" occurs when a borrower has missed three payments and a fourth is due. The default leads lenders to initiate the foreclosure process, but historically a majority of defaults are resolved without a foreclosure occurring.

[27] Option-theory also focuses on borrowers' ability to exercise a "call" option by prepaying the mortgage when interest rates fall. Thus, pure option-theoretic models focus heavily on trends in house prices and interest rates to explain both defaults and prepayments.

Exhibit 5

About AP

Essential News from The Associated Press

Sep. 15, 2011 12:29 AM ET

AAA

Mortgage default warnings surged in August

ALEX VEIGA, AP Real Estate Writer

AIM Share

LOS ANGELES (AP) — Banks have stepped up their actions against homeowners who have fallen behind on their mortgage payments, setting the stage for a fresh wave of foreclosures.

The number of U.S. homes that received an initial default notice — the first step in the foreclosure process — jumped 33 percent in August from July, foreclosure listing firm RealtyTrac Inc. said Thursday.

The increase represents a nine-month high and the biggest monthly gain in four years. The spike signals banks are starting to take swifter action against homeowners, nearly a year after processing issues led to a sharp slowdown in foreclosures.

"This is really the first time we've seen a significant increase in the number of new foreclosure actions," said Rick Sharga, a senior vice president at RealtyTrac. "It's still possible this is a blip, but I think it's much more likely we're seeing the beginning of a trend here."

Foreclosure activity began to slow last fall after problems surfaced with the way many lenders were handling foreclosure paperwork, namely shoddy mortgage paperwork comprising several shortcuts known collectively as robo-signing.

Many of the nation's largest banks reacted by temporarily ceasing all foreclosures, re-filing previously filed foreclosure cases and revisiting pending cases to prevent errors.

Other factors have also worked to stall the pace of new foreclosures this year. The process has been held up by court delays in states where judges play a role in the foreclosure process, a possible settlement of government probes into the industry's mortgage-lending practices, and lenders' reluctance to take back properties amid slowing home sales.

A pickup in foreclosure activity also means a potentially faster turnaround for the U.S. housing market. Experts say a revival isn't likely to occur as long as there remains a glut of potential foreclosures hovering over the market.

Foreclosures weigh down home values and create uncertainty among would-be homebuyers who fret over prospects that prices may further decline as more foreclosures hit the market. There are about 3.7 million more homes in some stage of foreclosure now than there would be in a normal housing market, according to Citi analyst Josh Levin.

"This bloated foreclosure pipeline now presents the greatest obstacle to a housing market recovery," Levin said in a client note this week.

Banks have been working through a backlog of properties that first entered the foreclosure process months, if not years ago. But the August increase in homes entering that process sets the stage for a host of new properties being targeted for foreclosure.

That's bad news for homeowners who may have grown accustomed to missing payments for several months without the threat of foreclosure bearing down on them. In states such as New York and Florida, for instance, processing delays have

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Exhibit 6

RESEARCH

CANCER SURVIVAL LINKED TO FOURFOLD INCREASE IN BANKRUPTCY RATE

A recent study funded by the National Cancer Institute found that bankruptcy rates were nearly twice as high among cancer patients one year after diagnosis, when compared to the general population. Within five years of a cancer diagnosis, the rate rises fourfold. The median time to bankruptcy was 2½ years after diagnosis.

Dr. Scott Ramsey, a health care economist at the Fred Hutchinson Cancer Research Center in Seattle, presented his team's findings June 6 at the 2011 annual meeting of the American Society of Clinical Oncology in Chicago.

The researchers linked Washington state cancer registry data from nearly 232,000 adult cancer cases in Western Washington during a 14-year period, with bankruptcy filing data from the U.S. Bankruptcy Court, Western District of Washington.

Insolvency rates were found to increase alongside length of survival. Further, bankruptcy rates among cancer patients have increased significantly since the U.S. financial crisis, according to the researchers, who included Ramsey's colleagues at the center, as well as researchers from the University of Washington and University of Bristol.

"The risk of bankruptcy for cancer patients is not well known, and previous studies have relied on individual self-reports about medically related reasons for bankruptcy filing," Ramsey said. "By linking two irrefutable government records of cancer and bankruptcy, we are able to determine how financial insolvency risk varies by cancer type, treatment and other factors."

Prior research on the relationship between illness and bankruptcy has largely come from the bankruptcy side of the aisle. A team of researchers, including Elizabeth Warren, released a study in 2009 finding that medical issues contributed to 62.1 percent of bankruptcies nationally in 2007. Nearly 80 percent of those who filed for bankruptcy at least in part because of medical problems had health insurance at the start of the bankrupting illness, including 60.3 percent who had private coverage, the study concluded. Most filers were solidly middle class before financial disaster hit — two-thirds were homeowners and three-fifths had a college education.

PROFESSOR SAYS WE NEED FASTER FORECLOSURES

The best way to stimulate the housing market is to stop delaying foreclosures, says Kansas State University professor Eric Higgins. While negotiations continue between state attorneys general and banks over a settlement that will revamp foreclosure practices, Higgins warns that some of the settlement proposals under consideration may backfire.

The terms of the proposed servicer settlement call for banks to do more on forgiving mortgages, but Higgins' research indicates that doing so would only encourage more homeowners to strategically default on their loans. Delaying or prolonging the foreclosure process doesn't help either because it prevents the market from recovering.

Higgins co-authored studies with Charles Calomiris, a professor at Columbia Business School, and Joseph Mason, finance professor at Louisiana State University, in response to current negotiations that have delayed many foreclosures.

"In no way do our studies suggest that foreclosure is a good thing," said Higgins, who is the head of the university's department of finance. "It is very unfortunate, but to delay the foreclosure process doesn't help anybody. It doesn't help the homeowner who is in debt and can't get out of debt. It's not helping the economy because we can't find the bottom of the housing market. And it's not helping neighborhoods because you have neglected houses."

It's also not fair to point to the banks as being the "bad guys" who caused the housing market fiasco, Higgins said.

"Of course, there's blame to be had by the banks," Higgins said. "But there's also blame to be had by the people who knew that they were borrowing too much. There's blame to be had for investors who bought these mortgage-backed securities without performing adequate diligence. And there's blame on the regulators who overlooked many problems in the housing market."

Higgins also said that the current drop in residential property values is not indicative of a double dip in the market. Rather, it's due to the fact that the market has not yet hit bottom.

"The reason it appears to be a double dip is because foreclosures stopped due to the uproar over robo-signing practices," Higgins said. "So, what we were seeing for home prices at that time wasn't really a true price. Once a true regulatory settlement was reached with mortgage servicers, the foreclosure process began again, the inventory of houses increased and prices dropped."

Completing foreclosures and clearing bad mortgages is the best way to help the market improve, Higgins said. According to the studies it takes an average of 17 months for a foreclosure to happen — and during that time, the home can be sitting, becoming run down and declining in value.

"By delaying foreclosures and modifying mortgages, all you are doing is prolonging the borrower's problems," Higgins said. "Statistics show that mortgage modifications don't really work and people are eventually going to be in a situation where they are unable to pay the adjusted mortgages. It gives borrowers who are in trouble a sense of a false hope and encourages other borrowers to engage in strategic default."

It may all seem doom and gloom, but Higgins has hope in a market recovery as long as banks can begin to process foreclosures. While home prices may drop even more when these foreclosures are processed, doing so will help give the market a clean slate so it can begin the slow trek to recovery.

"A lot of pain is going to happen, but the market needs to clear," Higgins said. "Once it clears, new construction can start. When construction starts, we create jobs in that area and then things might be able to pick back up."

Exhibit 7

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Grand Rapid Press (Michigan)

July 14, 2011 Thursday
1 EDITION

SECTION: BUSINESS; Pg. A14

LENGTH: 715 words

HEADLINE: Home sales stay steady ;
But for just June, closed deals were 20 percent lower than a year ago

BYLINE: Cami Reister / The Grand Rapids Press

BODY:

Halfway through the year, Grand Rapids area home sales are nearly on pace with last year, coming in 4 percent lower than the first six months of 2010.

That is a much more positive picture than the one given by looking at closed deals for June alone. They came in 20 percent lower than June 2010, which was inflated because of the home buyer tax credits.

"We were still closing tax credit transactions that were written prior to April 30, 2010, but not closed until May or June," said Julie Rietberg, CEO of the Grand Rapids Association of Realtors.

But Rietberg said she sees signs of hope in the 997 pending sales recorded last month. That is up 50 percent from a year ago and shows a market more stable than last year's tax-credit-fueled frenzy.

Julie Grevengoed, of JGR Real Estate in East Hills, said there's good news in the declining inventory.

Last month, 5,553 homes were for sale, which means less than six months of inventory. That is down significantly from the 12 months of inventory in June 2008 and the nine months in June 2009.

"There are more sales and less homes available," Grevengoed said. "Limiting supply makes prices go up, in theory."

The average sale price for closed deals last month was $132,045, up 7 percent from June 2010. Year to date, the price on closed deals is $118,240, up almost 1 percent from this time last year.

But Grevengoed sees a market still dominated by distressed properties -- foreclosures or short sales. Of the 817 deals closed last month in Kent County and surrounding areas, 22 percent were priced below $50,000 and 45 percent were below $100,000.

She said buyers are reluctant. Investors are paying less and less for troubled properties, and traditional buyers don't want to do the work most require.

"There's a shortage of nice houses on the market right now," she said. "A lot of people want a turn-key, move-in ready home, and it's hard to find that."

Denise Maghielse, a broker for a Five Star Real Estate office in Rockford, said she sees the same thing. But nicer homes won't hit the market until potential sellers get off the fence, something she predicts will happen either this year or next.

"People are going to stop putting their lives on hold, and they're going to come to the realization that our general market is not going to do a turn-around with house values going up 10 percent," she said. "But it still makes sense to make that residential move."

That's because the price drops are found in move-up homes as well as starter homes, and interest rates continue to favor buyers. But Maghielse is not ready to predict a long-term rise in home prices yet.

"The banks have inventory that they are just sitting on," she said. "I don't feel that has slowed down."

California-based RealtyTrac reported today a national drop of 29 percent in foreclosure filings in the first six months of the year compared to 2010. Michigan saw a decline of 22 percent and West Michigan counties saw year-over-year drops, too. Muskegon went down 15 percent, and Kent, Ottawa and Kalamazoo all dropped more than 20 percent.

"It would be nice to report that foreclosure activity is dropping as a result of improvements in the economy or the housing market," RealtyTrac CEO James J. Saccacio said in a statement. "Unfortunately, this doesn't seem to be the case."

Saccacio said processing and procedural delays are to blame, stretching out the foreclosure process. As many as 1 million foreclosure actions that should have happened this year won't take place until 2012 or later.

"This casts an ominous shadow over the housing market, where recovery is unlikely to happen until the current and forthcoming inventory of distressed properties can be whittled down to a manageable number," he said.

While the shadow inventory is something to consider, Maghielse's husband and fellow Realtor, Steve Maghielse, said the current situation still is favorable.

He admitted that real estate agents have been telling people it's a great time to buy for quite a while. But for people who want to live in their house long term and not use it as a short-term investment, the prices and interest rates are so low, they can only go up. And rental rates are higher than what monthly mortgage payments would be.

"If you're going to buy, now is the time," he said.

Email: creister@grpress.com

LOAD-DATE: July 18, 2011

Exhibit 8

BUSINESS | SEPTEMBER 19, 2011

Effort on Home Loans Stalls

By NICK TIMIRAOS And RUTH SIMON

A year after U.S. banks slowed down the foreclosure machine as a result of pressure from judges and regulators, the foreclosure process remains snarled.

Last September, GMAC Mortgage LLC, one of the nation's largest servicers of home loans, suspended sales of some foreclosed homes and put a moratorium on evictions of many borrowers behind on their payments. Other financial firms soon made similar moves, embarrassed by revelations of "robo-signing" by employees who signed off on hundreds of loans a day and falsely claimed they had personally reviewed documents giving the bank the right to foreclose.

Enlarge Image

Fabrizio Costantini for The Wall Street Journal

Stuart White beside the foreclosed house in East Lansing, Mich., that he's been trying to buy.

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- Courts Hamstrung in Foreclosure Cases
- GMAC Takes Steps to Fix Its Problems

The mess deepened as judges raised questions about how banks documented their ownership of loans and whether financial firms fabricated other paperwork. Regulators have found what they said are widespread weaknesses in mortgage-servicing operations.

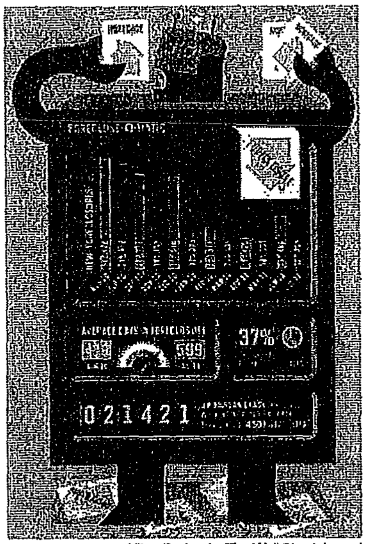
Lenders are back in the foreclosure business, and loan servicers say they have been working hard to improve their systems. But many mortgage-servicing companies are moving so cautiously that the number of properties entering the foreclosure pipeline is outpacing the total sold or taken back by banks. In June, just 3.6% of loans in foreclosure were liquidated, down from 5.7% in August 2010, according to 1010data Inc. and CoreLogic Inc.

The slowdown in the foreclosure process means banks are taking back fewer homes for now, leaving them with fewer to sell. That is seen as good for the economy in the short run because it has shrunk the supply of distressed houses, condominiums and other properties flooding the housing market. Banks held about 493,000 properties at the end of June, according to Barclays Capital, down 17% since September.

But delays in the foreclosure process also mean it is taking longer for foreclosed homes to be sold to new buyers and cleared out of the housing market.

Across the U.S., the average loan that completed foreclosure in July had no payments for 599 days, up 25% from 478 days in August 2010, according to Lender Processing Services Inc.

"If the lender doesn't have the ability to repossess the home for three or four years, it's very hard to clear the excess supply," says Jonah Green, director of mortgage analytics at 1010data, a technology and analysis firm in New York.



Mikey Burton for The Wall Street Journal

The robo-signing controversy unleashed a legal, regulatory and public-relations nightmare that still haunts the nation's largest home-loan servicers, including Bank of America Corp., J.P. Morgan Chase & Co. and Wells Fargo & Co. Banks say their reviews haven't uncovered evidence of wrongful foreclosures but have acknowledged weaknesses in their processes. A widely expected settlement of a probe of foreclosure procedures by U.S. regulators and state attorneys general could cost servicers as much as $25 billion, according officials involved in the talks. But the talks have stalled over the extent of any release that would protect banks from additional legal claims.

In addition, consent orders issued by federal banking regulators require 14 financial firms to create a single point of contact for borrowers and make other changes.

Banks will soon roll out a single website and phone number for borrowers whose loans were handled by the 14 servicers to request an internal review of their foreclosures. Loan servicers are hiring or redeploying thousands of employees to handle the additional workload. Fixing all the problems found by the U.S. government "is a multiyear process," says a spokesman for the Office of the Comptroller of the Currency.

"You have a number of places in the country where the banks don't know what to do or continue to violate the law. The courts are all over the map," says Ira Rheingold, executive director of the National Association of Consumer Advocates, a group of lawyers and consumer advocates who work with homeowners. "I wish I could tell you I see much of a difference."

The mortgage industry says it has been working hard to improve the handling of shaky loans. Industry practices are "far better today than a year ago," says Ed Delgado, a former Wells Fargo senior vice president who leads the Five Star Institute, mortgage-training provider.

The snags are a temporary reprieve for some troubled borrowers who are desperate to hang onto their homes. Other borrowers have seen their negotiations with lenders stall.

For would-be buyers of foreclosed properties like Stuart White, the limbo and uncertainty are causing unwelcome surprises.

The 62-year-old Mr. White, who works as a consultant for nonprofit organizations, signed a contract in May to buy a foreclosed duplex in East Lansing, Mich., for $135,000. He spent $1,000 on a loan application and property inspections. Then the mortgage company in charge of the property, Litton Loan Servicing LP, called off the sale, according to Mr. White and his real-estate agent.

A spokeswoman for Litton, owned by Ocwen Financial Corp., declined to comment.

The property was among hundreds in Michigan that mortgage companies pulled off the market after a state appeals court ruled that certain foreclosures hadn't satisfied state legal requirements. The court ruling prompted title insurers to stop underwriting policies for some bank-owned properties, and mortgage companies began ``re-foreclosing" on those houses to correct potential title problems.

At issue in the Michigan case was the Mortgage Electronic Registration System, or MERS, an electronic clearinghouse created by the mortgage industry in the late 1990s to bypass the traditional chore of recording every transfer of a mortgage assignment in local courthouses.

The appeals court ruled that certain foreclosures processed in the name of MERS weren't valid because the clearinghouse didn't have an interest in the underlying debt.

A MERS spokeswoman said the Michigan ruling "has a very limited applicability," adding that U.S. and state courts "all around the nation have issued rulings that uphold the MERS business model."

The decision has been appealed to the state supreme court.

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value of the vacant duplex he tried to buy will "continue to erode while we wait for some litigious process to be completed."

The foreclosure system has slowed most of all in states where courts are aggressively scrutinizing paperwork submitted by loan servicers when they move to seize homes. In New York, Chief Judge Jonathan Lippman issued an order last October requiring lawyers for mortgage companies to sign affidavits affirming that documents from their clients were accurate.

New York State has the lowest foreclosure-completion rate in the U.S., according to 1010data.

U.S. officials say the legal settlement they hope to reach with the banks will help the nation's housing market heal by allowing banks to eventually rev up foreclosures. But loan servicers still will clash with some judges who scrutinize whether foreclosure paperwork meets state requirements.

"I don't see how any settlement is going to ... bind a judge anywhere," says O. Max Gardner III, a lawyer in Shelby, N.C., who represents borrowers in bankruptcy cases.

Write to Nick Timiraos at nick.timiraos@wsj.com and Ruth Simon at ruth.simon@wsj.com

Exhibit 9

Mortgage Banking

May 2011

SECTION: COVER REPORT: REGULATORY COMPLIANCE; Pg. 34 Vol. 71 No. 8 ISSN: 0730-0212

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HEADLINE: SETTING THE RECORD STRAIGHT ON MERS

BYLINE: Jones, Allen H.

Allen H. Jones is chief operating officer of RiskSpan Inc., a mortgage valuation technology and advisory consulting services firm based in New York and Washington. D.C. He can be reached at ajones@riskspan.com

BODY:

ABSTRACT

Mortgage Electronic Registration Systems Inc (MERS) is a wholly owned subsidiary of MERSCORP. The subsidiary's sole purpose is to serve as beneficiary or mortgagee in the land records, while the electronic registry was designed to track the transfer of beneficial ownership interests in and servicing rights to mortgage loans. This article reviews the establishment of MERS, documents its founding premise, explores how it has been used since 1995, evaluates its real impact on the foreclosure crisis, considers the impact of the consent order and shares a perspective on MERS' continued role in the future. Up until the nations foreclosure crisis emerged MERS remained largely absent from the public eye. However, with the dawning of the Foreclosure-Gate crisis, the business model of MERS came under scrutiny. The mention of MERS in the AG draft agreement signifies that its utilization may become a matter that is settled between servicers and regulators, rather than litigated or legislated.

FULL TEXT

The foreclosure crisis ignited a media firestorm around the legitimacy of an electronic registry built by the industry to track ownership of mortgages and servicing. It's taking a while to get to the truth.

It has been decried as a shell corporation. Deemed a destroyer of the Colonialera land-records system. Its most outspoken critics have argued its very existence marks the demise of the institution of property rights. I Despite the unforgiving censure of Reston, Virginia-based Mortgage Electronic Registration Systems Inc. (MERS) in the media, its right to exist, to hold legal title to a mortgage and to foreclose all have been maintained by numerous local and state courts. These decisions, along with recent organizational transformation and procedural changes within MERSCORP Inc., MERS' parent company, could mean the storm of litigation challenging its standing is finally tapering off. But MERS remains largely misunderstood by the public, and is almost regularly berated by the media. As a result, politicians are distancing

themselves from MERS. Do such maneuvers indicate awareness of a potential liability or is it simply that the public relations risk is just not worth the cost?

Amidst the din, it is hard to tell. Absent from most of the discourse is an unbiased portrait of MERS, with a history of how and why it emerged, the value it confers to the mortgage lending supply chain and the real problems it faces today with respect to a recent regulatory consent order.

The MERS® System is the registry operated by MERSCORP. MERS is a wholly owned subsidiary of MERSCORP. References in this article to MERS are to the subsidiary. The subsidiary's sole purpose is to serve as beneficiary or mortgagee in the land records, while the electronic registry was designed to track the transfer of beneficial ownership interests in and servicing rights to mortgage loans.

Where things stand

As the summer approaches, the housing finance industry is anticipating significant changes in housing policy designed to mend the loose practices that steered Fannie Mae and Freddie Mac into conservatorship. As the administration and Congress attempt to wind down the mortgage giants and attract private capital back into the markets, the inventory of homes for sale and pending shadow real estate-owned (REO) inventory continues to remain at record levels. In fact, the backlog of delayed foreclosures positions the economy to face a new record volume of foreclosures in 201 1.

It was the spike in foreclosure activity in 2009 and 2010 that revealed false affidavits and other improper paperwork tied to foreclosures.

Some were carried out by "robo-signers." Others were executed with improper documentation. A few had even been carried out on the wrong house altogether. The discovery became the catalyst for a national foreclosure processing crisis that prompted several large servicers to temporarily suspend their foreclosure proceedings.

On some of those properties foreclosed with improper or incomplete paperwork, MERS was listed as the mortgagee or beneficiary of record. As a theretofore relatively unfamiliar entity, with the power to foreclose, the mortgage lien holder (MERS) unwittingly fanned the fires of the foreclosure crisis. Though numerous court rulings have since vindicated MERS, recognizing its authority to foreclose, many parties remain unconvinced.

During a self-imposed foreclosure moratorium, servicers revisited their loss-mitigation procedures and default-management practices. After conceding the challenges, many servicing institutions announced that additional remedies had been implemented to ensure that borrowers in default are evaluated for all available lossmitigation options.

Further, servicers pledged that in the event of a foreclosure, their internal reviews had resulted in new operational procedures that would be meticulously followed in the future. But the consternation and uproar caused by the so-called Foreclosure-Gate has not yet fully settled.

That's not to say MERS has not been without some serious setbacks. On April 13, the results of an interagency horizontal examination conducted by federal regulators were released to the public. The report revealed a concerted effort by the Federal Reserve System, the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC) and the Office of Thrift Supervision (OTS) to review the safety and soundness of mortgage servicing and foreclosure processes at 14 major mortgage servicers as well as a number of third-party vendors that provide significant services to lenders and servicers - including MERSCORP and MERS. The review has resulted in a formal consent order against the two entities.

This article reviews the establishment of MERS, documents its founding premise, explores how it has been used since 1995, evaluates its real impact on the foreclosure crisis, considers the impact of the consent order and shares a perspective on MERS' continued role in the future. The hope is that by providing this account the record will be set straight.

Background

Originally conceived in the late 1980s, the concept for an electronic clearinghouse of critical mortgage information was explained in an October 1993 white paper entitled the Whole Loan Book Entry iWLBEJ Concept for the Mortgage Finance Industry. The idea was developed by the I nter Agency Technology Task Force (IAT), a group composed of prominent industry leaders - the Mortgage Bankers Association (MBA), Fannie Mae, Freddie Mac, Ginnie Mae and servicing executives.

Their vision was simple - use modem-based electronic data interchange (EDI) to allow mortgage loan sellers, warehouse lenders, mortgage loan investors and servicers to "obtain, transfer and track interests in mortgages, essentially on a real-time basis," regardless of any internal proprietary systems that supported their business operations.

Up until then, liens were tracked by local land records offices, with varying and often antiquated systems. Though seldom recognized, the purpose of the land records was not to track mortgage ownership rights, but to provide public notice of liens to protect the lien holder.

While other aspects of the mortgage lending supply chain were being digitized, including the 1990s development of automated underwriting systems (AUS) and loan origination systems (LOS), the recordation of the mortgagee or agent for the mortgagee in local land records remained a manual process.

Well-intentioned staff at bustling offices struggled to manage the congestion caused by the growing volume of mortgage loans. Missing and erroneous assignments caused gaps in the chain of title, threatening the integrity of the lending process. The late 20th-century prevalence of secondary market transactions and advancement of management information systems pushed the industry to pursue a more efficient solution.

Process

Traditionally, the borrower executes two essential documents at closing. These two documents make up the mortgage loan. Although the legal distinction between them is fundamental, it is often overlooked in common parlance. The first document is the promissory note, which signifies the borrower's promise to repay the loan over a period of time under stated terms. Notes can technically exist without collateral, so the second document, the mortgage, secures the promissory note by placing a lien on the real property as security for the loan's repayment.

The note is typically endorsed "in blank" and delivered from the lender to the mortgage loan aggregator and/or securitization trust. The note is intended to be a fluid, negotiable instrument in trade where possession is sufficient to confer the right to enforce ownership interest.

The mortgage follows the note. That is to say that a transfer in the ownership of the promissory note also transfers with it the underlying secured obligation to pay.

Traditionally, when a loan was sold to another lender - for example, an aggregator - the mortgage was "assigned" to the purchaser and recorded in the purchaser's name. However, if the servicing remained with the seller, as was often the case, the mortgage usually continued to be recorded under the servicer's name.

The seller would then prepare a "recordable assignment in blank" and deliver it to the trust. Where MERS is the mortgagee of record, subsequent assignments of the mortgage no longer need to be recorded at the local recorders' offices because MERS holds the mortgage in trust on behalf of its member, who owns the note.

The land records have never been an authoritative source for who owns beneficial interests and servicing rights to mortgages. The assignment, which is usually recorded to protect the lien holder, is generally not required by the county, and has nothing to do with the sale of servicing rights. If the servicing rights changed hands, then the county land records were updated if the new servicer desired to receive service of process in order to fully perform under its servicing agreement with the investor. The advent of MERS enhanced this last step.

A predecessor to the current configuration of MERS and MERSCORP was officially created in 1995 as an industrywide utility to hold mortgage liens in an agency capacity on behalf of participants in the mortgage banking industry, and to track the changes in the ownership and servicing of any registered loan.

At closing, the lender and borrower make MERS the mortgagee of record, and all subsequent changes in the mortgage loan ownership and servicing rights of the loan are updated in the database provided the loan continues to be registered in the MERS System. Moreover, MERS was established as a part of a tri-party organization managed by the limited staff of MERSCORP, the lender participant and the founding agencies. Accordingly, all three legs of the tri-party stool contribute to the accuracy and maintenance of the registry in addition to serving as checkpoints.

The efficiencies realized by the registry provided incremental value to lenders that sold loans into the secondary market. Mortgage banking was a process that frequently required several assignments, and even before MERS, there was already an active attempt to minimize assignment costs and third-party fees. Lenders had already begun preparing mortgage assignments in blank to enable fluid transmissions, and attempted to immobilize mortgage notes at the original clearinghouse member custodian to avoid future file movement and recertification. These practices merely continued with the introduction of MERS.

'Vault' idea

Because the original WLBE system was closely modeled after the electronic stock and bond registration model implemented by the Depository Trust Company (DTC) a couple of decades earlier, some industry participants in the early 1990s suggested that loan documents, like physical stock and bond certificates, should also be stored in a vault. The idea of a central vault was one of many ideas circulated as the clearinghouse was being brainstormed, although it never became an official feature of the clearinghouse upon its official conception.

The vault idea was forgone presumably because loan document immobilization was already taking place. The Depository Trust and Clearing Corporation's (DTCCs) depository vaults, for instance, immobilized stock and bond certificates. As a result of electronic registrations and transfers, futures, options and bonds are now issued electronically.

But the vault idea did not totally disappear - the mortgage industry continued to pursue the vault concept with the advent of the electronic mortgage (eMortgage). Prior to conservatorship, both Fannie Mae and Freddie Mac pursued initiatives for the electronic storage of eMortgages originated and closed by their approved seller/servicers and signed electronically.

Legal structure

MERS was designed to operate in accordance with existing real property law and the Uniform Commercial Code (UCC). MERS acts as mortgagee in the land records in a nominee (agent) capacity for the originating lender and the lender's successors and assigns.

The MERS System exists so MERSCORP knows who to send the service of process to because, under the MERS process, the current servicer continues to handle the day-to-day servicing responsibilities as it did prior to the advent of MERS.

When the underlying mortgage loan indebtedness (in the form of the promissory note) was sold from one lender to the next, the purchasing lender's interest would continue to be secured because MERS held legal record title for the benefit of the lender. MERS' role as agent for the promissory note owner in the land records is supported by both agency and contract law.

As mentioned earlier, it is not generally necessary to record an assignment to demonstrate mortgage loan ownership or convey a security interest. The benefit of recordation is to ensure that interested parties are apprised of existing liens or other legal encumbrances. Assignments are recorded so that subsequent servicers receive service of process for legal actions affecting the property that is encumbered by the lien.

Because mortgagee-of-record status renders MERS responsible to different parties in the mortgage loan ownership chain, contract agreements are prudently crafted between MERS, MERSCORP and third parties to establish loan ownership and security interests that retain the integrity of the original documents and have legal force.

Legal challenges and victories

Up until the nation's foreclosure crisis emerged, MERS remained largely absent from the public eye. However, with the dawning of the Foreclosure-Gate crisis, the business model of MERS came under scrutiny.

The defects in servicer foreclosure procedures were admittedly serious, and included the robo-signing of affidavits and improper notarization, but investigations did not demonstrate that the vast majority of these foreclosures were otherwise invalid. Nevertheless, the legal right of MERS to commence foreclosure action came under fire in numerous states, where plaintiffs filed suits questioning MERS' authority to foreclose as an entity that was not the actual owner of the loan.

In October 2010, Washington, D.C. Attorney General Peter Nickles issued an enforcement statement declaring foreclosures may not be initiated against a District of Columbia homeowner unless the security interest of the current noteholder is also reflected in the local recorder's office.

As a relatively unknown entity with the power to foreclose, MERS and the MERS System became the focus of intense scrutiny. However, the past couple of years have unleashed a flood of cases in judicial and non-judicial foreclosure states that were adjudicated in MERS' favor.

* Utah: Two March 2011 rulings (Wade v. Meridias Capital Inc., MERS et al; and Wareing v. Meridias Capital) in Utah, a non-judicial foreclosure state, have affirmed MERS' ability to act as the beneficiary of the deed of trust and nominee of the lender and its successors and assigns. The judges confirmed that this authority is conferred when a borrower signs a deed of trust on which MERS is expressly appointed the beneficiary. As such, mortgage assignments by MERS are valid and its execution of foreclosure is legal. These two cases were a small number of the many court decisions and orders in Utah that have upheld MERS' ability to be the beneficiary on a deed of trust and which dismissed challenges to MERS' authority to foreclose or assign.

* Wyoming: A similar memorandum (In re Martinez) followed in March 2011 in Wyoming, where the authority of MERS relative to assigning a mortgage had likewise been contested. The argument failed because the borrower signed a mortgage at closing expressly authorizing MERS "to take any action required of the lender."

* California: Also in March 2011, a plaintiff filed a claim under the California False Claims Act (CFCA), asserting MERS has made false representations in order to circumvent payment of recording fees required to reflect security interests in real property. The suit (Bates v. MERS) was dismissed by the District Court for the Eastern District of California, which determined it was without jurisdiction over the plaintiff's action because the plaintiff was not an original source of the information as required under the CFCA.

Further rulings recognizing MERS as the beneficiary of the mortgage or deed of trust, similar to those found in Utah and Wyoming, have also been made in Oregon, New York, Massachusetts, Georgia, New Hampshire, California, Alabama, Nevada, Virginia, Rhode Island, Michigan and Kansas this year. As the mortgagee of record and holder of the original note endorsed in blank, the cases support MERS' legal standing to initiate foreclosure proceedings.

Laurence E. Piatt, a partner with K&L Gates LLP in Washington, D.C. with expertise in real estate finance who has worked on MERS issues over the years, acknowledges the significance of the rulings: "With favorable decisions in multiple states, it is clear that the basis for which MERS was founded is valid, and that MERS has the affirmation of the overwhelming majority of courts to act as the lender's nominee as provided in the mortgage documents," he says.

"MERS was created to enable efficiencies in a paper-based business. MERS continues to achieve its objectives, and if an entity like MERS did not exist today, it would have to be created to enable the efficient operation of the capital markets," Piatt says.

Corporate governance challenges

While MERS' legal standing has been vindicated by state and district courts, its corporate governance structure recently came under the review of federal regulators. The Interagency Review of Foreclosure Policies and Practices and consent order for MERS were posted to the Federal Reserve Board's website on April 13.

In testimony before the Senate Committee on Banking, Housing and Urban Affairs on Feb. 17, 2011, Acting Comptroller of the Currency John Walsh explained to the Congress that an interagency examination of MERS' operations, procedures and controls had been under way.

The recent consent order between MERS and federal regulators follows several organizational changes already taking place within MERSCORP. On Jan. 22, 2011, R.K. Arnold, president and chief executive officer of MERS and MERSCORP, resigned. MERSCORP issued a statement on its website acknowledging the resignation and announcing an interim replacement. "MERSCORP Inc. . . . today announced the retirement of President and [Chief Executive Officer] R.K. Arnold. Arnold joined the company at its inception and has been instrumental in the development of the MERS System, a registry of ownership and other mortgage rights for more than half of all outstanding residential mortgages in the United States. . . . Arnold is succeeded on an interim basis by financial services industry veteran Paul Bognanno," the company announced. An announcement on a permanent successor has yet to be made.

While Walsh made general remarks on the review of MERS and MERSCORP in his testimony, he did not mention Arnold's resignation: "[T]he agencies [OCC, the Federal Reserve Board (FRB), FDIC, OTS] conducted interagency examinations of MERSCORP and its wholly owned subsidiary, Mortgage Electronic Registration Systems Inc. . . . which provide[s] significant services to support mortgage servicing and foreclosure processing across the industry. The primary objective of the examinations was to evaluate the adequacy of controls and governance over bank foreclosure processes, including compliance with applicable federal and state law. Examiners also . . . assessed foreclosure operating procedures and controls, interviewed bank staff involved in the preparation of foreclosure documents, and reviewed approximately 2,800 borrower foreclosure cases in various stages of foreclosure. Examiners focused on foreclosure policies and procedures, organizational structure and staffing, vendor management including use of third parties, including foreclosure attorneys, quality control and audits, accuracy and appropriateness of foreclosure filings, and loan document control, endorsement and assignment."

Many of the lapses in safety and soundness cited in the final interagency review were ascribed to servicer performance in the oversight and quality control of MERS. But the agencies also identified non-servicer-related deficiencies that presented "financial, operational, compliance, legal and reputational risks to MERSCORP and MERS, and to the participating members." When the consent order was issued, it was publicly announced that MERSCORP and MERS had already begun implementing remedial procedures.

Moving forward, MERSCORP and MERS have committed to the following actions:

* Forming a compliance committee to monitor compliance with the terms of the consent order;

* Formulating an action plan with a complete description of the actions necessary to comply with the order;

* Engaging an independent third party to assess board, management, officer and staffing needs in order to operate safely and soundly;

* Formulating a communications plan with members to establish a standard protocol for dealing with significant legal matters;

* Formulating a governance plan to strengthen processes as they relate to authorizing MERS certifying officers; and

* Obtaining an independent third party to review the effective operations of the eRegistry system of recording electronic notes.

Financial sanctions against MERSCORP and MERS were not imposed by regulators in the consent order.

MERS: 'No more foreclosures in the MERS name*

Before the consent order was issued, a number of policy changes were announced by MERSCORP. The most notable was published in Policy Bulletin 2011-2 on March 8, 2011, announcing the revocation of member authority to commence foreclosures in the MERS name.

According to the Policy Bulletin, the policy would become effective Aug. i, 2011, upon approval by the board of directors of MERS and MERSCORP: "The authority to conduct foreclosures in the name of MERS granted to a member's certifying officers under the member's MERS Corporate Resolution is revoked. Effective Aug. I1 2011, the member shall be sanctioned $10,000.00 per violation for commencing a foreclosure in the name of MERS. The member will automatically be in violation of this rule and subject to the enforcement of the fine when the first legal action is taken in MERS name."

Although recent litigation has upheld the permissibility of MERS to commence foreclosure action, the practice is slated to come to an end where it has not already ended. (Where the practice ends depends on servicer policy and/or whether the securities are Fannie and Freddie securitizations, not on market/jurisdiction.)

Tri-party management allows swift policy change

Concurrent with discussions over Policy Bulletin 2011-2, several major servicers, including Charlotte, North Carolina-based Bank of America, New York-based JPMorgan Chase and San Francisco-based Wells Fargo & Co. implemented internal policy changes requiring the de-registration of loans that were in the MERS name before initiating foreclosure. The purpose of the change was to provide clarity to the defaulted mortgagor and minimize legal and compliance risk to the servicer.

Furthermore, any Fannie Mae and Freddie Mac servicers that did not implement the policy on their own are now required to do so. That change was implemented via the following policy directives:

* Freddie Mac Bulletin 2011-5, March 23, 2011: Eliminated the option of Freddie Mac servicers to foreclose in the MERS name. Going forward, the securitization must be assigned from MERS back to the servicer by means of recordation where required by law.

* Fannie Mae Announcement 2010-05, March 30, 2010: MERS may not be named as the plaintiff of any mortgage loan owned or securitized by Fannie Mae. The servicer must prepare an assignment via recordation to transfer the security interest from MERS to the servicer. Effective May 1, 2010.

The politics of MERS in the housing crisis

Even as MERS turns the tide by prevailing in state courthouses around the country, the challenges the mortgage industry faces post-boom as a result of the widespread destruction of home values remains a political nightmare.

In addition to the agency consent order, a 50-state attorneys general (AG) task force contends it is negotiating a 27-point draft servicer settlement (or term sheet) with a handful of megaservicers. Conspicuously present in that draft agreement is language stating that the subject of MERS is held for separate review. It appears that the agency consent order has addressed the AG task force reference to MERS and its organizational structure.

The mention of MERS in the AG draft agreement signifies that its utilization may become a matter that is settled between servicers and regulators, rather than litigated or legislated. In light of this possibility, in my view, the probability that MERS will end up a political casualty may be lowered.

The ongoing need for an electronic registry

By serving as the mortgagee in the county land records on behalf of its members, MERS has become a critical component of housing finance. Since its inception, MERS has enabled fluent commerce in the housing finance markets, much like the advent of electronic registration in lieu of stock certificates enabled fluent commerce in an age of trading stocks online.

The soundness of a borrower's property rights is far from compromised by the frugality of paperless business; instead, it is improved, as the enormous volume of mortgages issued and transferred could not be sustained by congesting the land records with reassignments.

In fact, the services of MERSCORP have not been exploited to their full, value-adding potential. If the traditional, paper-based format of the promissory note and the mortgage document were produced electronically (versus manually) at closing and registered within a single system like MERSCORP's MERS eRegistry, it would be virtually impossible to create duplicate notes.

The incidence of fraud would be reduced by the instant visibility conferred by a system like the MERS eRegistry. The legal underpinnings necessary to realize such a system have been in place since 2000, when the Clinton administration passed the Electronic Signatures in Global and National Commerce Act (E-SIGN), recognizing the equivalence of authenticity and enforceability between electronic and paper signatures.

In addition to federal law, 47 states and the District of Columbia have enacted Uniform Electronic Transactions Act (UETA) laws in their own statutes, acknowledging the validity of electronic signatures. The three remaining states - Illinois, New York and Washington - have adopted separate laws recognizing the validity of digital signatures as well.

Chris Christensen, an attorney with PeirsonPatterson LLP law firm in Dallas, has closely followed the foreclosure crisis. Christensen says, "The MERS® eRegistry is the key to solving the lost document problem. As a critical piece of eCommerce infrastructure, the eRegistry is also key to solving the industry's data problem. These two problems have largely contributed to the housing crisis. The good news is that they are not permanent problems if the industry acts now to implement the appropriate solutions. The MERS eRegistry is part of the solution and not the problem."

Christensen adds, "Had the industry focused on understanding the MERS value proposition with its electronic registry, we could have avoided the lost-document and data-based issues at the heart of the foreclosure crisis. But hindsight is always 20/20."

SIDEBAR

All three legs of the tri-party stool contribute to the accuracy and maintenance of the registry in addition to serving as checkpoints.

SIDEBAR

Although recent litigation has upheld the permissibility of MERS to commence foreclosure action, the practice is slated to come to an end where it has not already ended.

GRAPHIC: Illustrations

LOAD-DATE: May 19, 2011

Exhibit 10

The MERS reality: The electronic tracking of mortgage rights in the United States
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ABSTRACT

The goal of **MERS, Mortgage Electronic Registration** Systems, is to track the servicing and beneficial ownership rights for every loan in the US. When a mortgage is originated in the US, the lender often sells the loan to generate funds for further lending. Two aspects of a loan - servicing and beneficial rights - can be sold. **MERS** works closely to identify and implement the most cost effective use of **MERS** for its members.

FULL TEXT

UNITED STATES

INTRODUCTION

Scenario 1: A mortgage closing table in a lawyer's office in any American town. The buyer and seller are attending with their legal representatives. The sellers lawyer is on the phone, obviously agitated. The problem: the chain of title for her clients property is not complete, and the last company listed as mortgagee of record went out of business two years ago. This situation will take time to sort and contact the current mortgagee of record to prepare and record the lien release. The closing likely won't take place today.

Scenario 2: Mortgage Servicer A plans to sell the servicing rights for 10,000 loans to Servicer B. While conducting the due diligence on the loan files, Servicer A discovered more than 2,000 assignment errors. According to the terms of the sale, Servicer A must correct the errors prior to the sale. Servicer A must hire a specialist to track and correct them. Each missing assignment will cost an average $22 to record. Each correction will cost an extra $10. Additionally, when Servicer B assumes the servicing rights, it must record a new assignment for each loan.

These scenarios and other assignment-related complications happen with alarming regularity in the United States. The good news is they are happening less frequently. A 25-employee-company named **MERS, the Mortgage Electronic Registration** Systems, whose goal is to track the servicing and beneficial ownership rights for every loan in the U.S., is the driving force behind the improvement.

Overview of Mortgage Rights in the US.

When a mortgage is originated in the U.S., the lender often sells the loan to generate funds for further lending. Two aspects of a loan-servicing and beneficial rights-can be sold. Servicing is the contractual right to collect the monthly escrow, principal and interest payments. The beneficial right is the right to receive full repayment of the loan. The beneficiary legally holds the promissory note, although a custodian often physically has the note for safekeeping. These rights can be sold together or separately. In the U.S., servicing rights often are treated as separate financial assets bought and sold as a servicer adjusts its portfolio size and type to meet risk positions, capital requirements, and other criteria. Although beneficial rights seldom are traded, the promissory note can change hands two or three times before settling with the ultimate investor. For example:

Lender A originates a loan and, before the first loan payment is collected, sells Mortgage Bank S the loan's servicing and beneficial rights. Mortgage Bank S decides to retain servicing rights, but sells the beneficial rights to Investor F. As the servicer, Mortgage Bank S collects the monthly mortgage payment and keeps a percentage of the payment as a fee for servicing the loan. Mortgage Bank S sends the balance of the loan payment to Investor F, which holds the mortgage's beneficial rights.

Public Records

Public records are another important aspect of the loan origination process in the U.S. Once the loan is closed, the security instrument (mortgage or deed of trust) is recorded in the county land records, which creates a public notice of the lien on the underlying property. This recordation protects the lender by establishing a first lien on the property. Thereafter, anyone who needs property information can search the local public records. If a security instrument isn't recorded, the loan could be sold fraudulently to an unwitting party, who could record a security instrument and be in the first lien position. In the event of borrower default, the court first will pay foreclosure claims to the first lien holder, and then to any second or third lien holders of recorded security instruments. Therefore, it's critical that changes in loan ownership be recorded.

The Problems **MERS** was Created to Correct

In the early 1990s, trading or selling servicing rights became a huge business. (See Figure 1.) With the increased volume, came a mountain of paperwork to prepare and record the required assignments that accompany the transfer of loan-servicing rights from one servicer to another. Assignment preparers and county **recorders** couldn't keep pace. Assignments were late, in the wrong sequence, or not made, all of which caused huge problems (two examples were described at the beginning of this article). In 1993, a mortgage industry task force of Mortgage Bankers Association of America (MBA) member companies recommended an electronic registry to eliminate the need to prepare and record assignments. Thus, the idea of **MERS** was born. The **MERS** concept would allow mortgage lenders, servicers, warehouse banks and investors to reduce or eliminate their paperwork burdens.

The task force decided the Depository Trust Company (DTC), a participant-owned corporation which records securities transactions electronically, provided a good model. The DTC was created for the U.S. securities markets to eliminate paper certificates that recorded the purchase and sale of stocks, bonds and other securities. Today, it is difficult to imagine accommodating the volume of securities trading on U.S. stock exchanges if traders were required to use paper certificates to pass ownership rights.

The **MERS** System was designed to perform similar functions for the real estate finance industry. However, the task force decided **MERS** should concentrate on eliminating loan assignments by providing an electronic registry to track the servicing and beneficial ownership rights transfers. After a loan is registered on the **MERS** System, transfers of beneficial ownership and servicing rights between members are tracked electronically. An 18-digit mortgage identification number (MIN) tracks mortgages registered on the **MERS** System throughout the life of the loan. The MIN is placed on the security instrument prior to loan closing. **MERS** remains the mortgagee of record in the county land records as long as the beneficial ownership and servicing rights are sold to another **MERS** member. If those rights are sold to a non-**MERS** member, a traditional assignment out of **MERS** must be recorded in the county land records.

"The benefit to the mortgage company that registers its loans on the **MERS** System is that it can then sell loans to another **MERS** member without requiring the recordation of a paper assignment in the county land records," explained Dan McLaughlin, **MERS** executive vice president, product division. "That benefits the seller."

McLaughlin added: 'The mortgage buyer benefits from eliminating the need to ensure the assignment was recorded property So if you eliminate the assignment, you eliminate the follow-up work and paperwork costs."

To ensure widespread acceptance within the industry, **MERS** sought to have security instruments modified to contain **MERS** as the original mortgagee (MOM) language. **MERS** began to change decades of business practices after the two biggest mortgage funders in the U.S., the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal National Mortgage Association (Fannie Mae) modified their Uniform Security Instruments to include MOM language. Their approval opened the door for **MERS** to be incorporated into the loan at origination. The security instruments clearly define what company is the initial lender and that **MERS** holds only legal title to the interest granted by the borrower. But if necessary, **MERS** (as lender nominee) can exercise any or all of those interests, including the right to foreclose, to release and cancel the security instrument, and to take any other action required of the lender.

U.S. government agencies like the Veterans Administration, Federal Housing Administration, and Government National Mortgage Association (Ginnie Mae) followed Fannie Mae and Freddie Mac and approved **MERS**. Several state housing agencies also approved **MERS** language in their states' security instruments.

The California Housing Finance Agency (CHFA) took the approval a step further and mandated that it will buy only **MERS**-registered loans beginning January 1, 2002. California is the first member of the mortgage industry to mandate **MERS**.

"Our conversion to **MERS** does two things that strengthen CHFA's portfolio," said Clint Ingle, manager of the agency's $5.5 billion portfolio. "It allows us to absolutely verify we have deeds of trust in the CHFA name. That's something we can't do now, although we have checks and balances in place.

"The conversion also protects our bondholders. We can now verify the loan is recorded in **MERS** prior to purchase and we can stop the purchase if needed and require the deed of trust to reflect **MERS**," Ingle said.

MERS and Mortgage-Backed Securities

The mortgage-backed security (MBS) sector tested the viability of the **MERS** concept because a substantial number of mortgages are securitized in the secondary market (see Figure 2). In February 1999, Lehman Brothers was the first company to include MERSregistered loans in a MBS. The Wall Streetrating agencies found **MERS** loans didn't affect the MBS rating. Since then, Standard & Poors, and Fitch IBCA have all rated securities containing loans that name **MERS** as mortgagee of record.

Moody's Investor Service issued an independent Structured Finance special report, "**Mortgage Electronic Registration** Systems, Inc. (**MERS**): Its Impact on the Credit Quality of First-Mortgage Jumbo MBS Transactions." The report states the "impact on the credit quality of jumbo first-mortgage MBS transactions will be negligible." The most significant report finding specified that in transactions where the securitizer used **MERS**, new assignments of mortgages to the trustee of MBS transactions aren't necessary. The report also identified several areas that wouldn't be affected, such as the legal mechanism to put creditors on notice of a mortgage, the ability to foreclose and take real estate in lieu of foreclosure isn't materially affected, and credit enhancement levels for first-lien jumbo mortgages aren't increased.

Real-Cost Savings

When loan servicing is sold, an assignment of the mortgage to the new servicer is recorded in the county land records. The paperwork can take from one to 12 months and cost an average of $22 per assignment. For a one-time $3.50 **MERS** registration fee, that $22 assignment fee is eliminated regardless of how often rights are sold.

As **MERS** becomes more widespread, the cost-saving opportunities increase. In a May 2000 Mortgage Banking article, the mortgage banking firm Residential Funding Corporation estimated that purchasing MERSregistered loans saved the company $15 to $17 per loan. The amounts reflect the company's particular assignment savings minus the **MERS** registration fees. In the same article, Norwest Mortgage calculated an annual saving of $300,000 to $500,000. Norwest's savings included process improvements and the elimination of the need to track, correct and record missing or incorrect assignments.

Rick Scogg, president of Aurora Loan Services, estimated **MERS** saved his company hundreds of thousands of dollars annually. 'We buy and sell servicing frequently. When we buy portfolios, there are payoffs and foreclosures the next day and therefore there is a delay in the lien-release process (for nonMERS loans). With **MERS**, we don't need to get attorneys to correct these, and that saves us thousands of dollars a year," Scogg said.

In special cases, assignments are prepared, but not recorded, for the transfer of rights to some investors. Some investors require these "ready to use" assignments to protect their interests if a servicer went bankrupt. Warehouse banks that lend money temporarily to a mortgage originator often require these assignments (warehouse banks are repaid when the loan is sold). The warehouse bank considers the unrecorded assignment as protection in the event the lender fails to repay the temporary loan. If that happens, the warehouse bank would record the assignment, which would transfer ownership of the loan from the lender to the warehouse bank.

However, **MERS** offers an alternative to the unrecorded assignment-the electronic tracking agreement (ETA). The ETA is an agreement between **MERS**, the warehouse bank and the originator, that, should the originator default, **MERS** will become the nominee for the interim funder in the public land records, thus perfecting the security interest of the warehouse lender.

MERS members realize additional cost savings in unexpected areas too. For example, when a check issued to pay the recording fee on a loan doesn't clear (known as a stale check), it must be tracked and possibly reissued. With **MERS**, the number of times this happens is substantially reduced along with a lower number of checks being cut for recording fees. One **MERS** member, Alliance Mortgage Company, estimates an additional $20 cost savings per loan when considering the time spent tracking and verifying stale checks. Before implementing **MERS**, Alliance pursued stale checks on approximately 25% of the checks sent to **recorders** offices.

MERS also benefits title companies. Title companies verify the title chain and insure against defects, so they're particularly sensitive to the problems in the assignment process. With **MERS** as original mortgagee, thumbing through paper-based records at the local county court house is reduced. Equipped with a MIN, title companies can verify the title chain electronically, and find very quickly which companies hold the servicing and beneficial ownership rights.

Who Owns **MERS?**

MERS is a member-owned and funded company based in McLean, Virginia. One of the unique and noteworthy characteristics of **MERS** is that in an industry known for its fierce competitiveness, industry players created a utility that benefits everyone. The **MERS** executive team reports to a board of directors that represents large, medium and small real estate finance industry firms. **MERS** is truly a member-driven organization and seeks input from its members before making policy and system changes.

Another unique **MERS** characteristic is the initial arrangement with Electronic Data Systems (EDS), its technology partner. EDS agreed to fund the **MERS** System development for a percentage of the transaction fees. This arrangement was necessary because the real-estate finance industry was reluctant to fund the concept although the industry agreed **MERS** solved the paper problem. **MERS** owns the system and now funds enhancements.

Other Important MERS Information

The MERS System started life on a client/server-based platform. The system has since migrated to a web-based system that supports all functionality, including registering new loans, updating records, performing transfers of servicing and beneficial ownership rights, generating reports and running database queries. For members who have large volumes (registering or servicing over 1,000 loans per month), the system supports EDI X12 or flat-file transmissions.

The first two loans were registered on the MERS system April 29,1997. A year later, the system only had about 59,000 registered loans. A year later, MERS ended 1999 with more than one million loans on the system, and by the end of 2000, MERS had 3 million registered loans. By April 2001, there were 4 million registered loans on the system, and daily loan registrations averaged more than 9,500 (see Figure 3). MERS President and CEO R.K. Arnold said, "We've achieved a solid 15% of the residential market, and we've generated enough momentum to hit a 30% share by the end of the year. Our mission is to register every loan in the United States on the MERS System."

MERS membership is increasing too. At the end of 1997, there were seven members. Currently, there are more than 230 member companies registering loans, 83 being integrated (integration can take between one week and nine months), and more than 100 waiting to become members. "Twenty three of the top 30 lenders in the U. S. are actively doing business with MERS in one or more of their lines of business,' said Carson Mullen, MERS executive vice president, customer division. "In most cases, these lenders have multiple lines of business being registered on MERS including correspondent loans, wholesale acquisitions and retail production of their own. The mixture varies, but the trend is toward increased use of MERS.

"We realized early that we must clearly define the excellent MERS value proposition and deliver up-front cash savings for originators to interest them in adopting MERS into their operations," said Mullen.

Redefining this emphasis on the production side of the business almost always involves trading partner relationships and has resulted in more rapid adoption of MERS as original mortgagee security instruments across the nation.

Mullen added: "Frankly, we've employed every type of peer pressure, economics and trading partner encouragement that we could. Most of our members have multiple trading partner relationships. Each new active MERS member has meant another link in what has become a very long value chain. We've got a lot more to do. In future years, we hope that MERS is able to squeeze out inefficiencies in the mortgage process and offer e-commerce benefits in a much wider range of mortgage processes." After much work by the MERS team and early supporters of MERS to get the word out, this effort is now being done by an increasing number of mortgage aggregators (mortgage firms that purchase closed loans from lenders) and others. Many aggregators are encouraging the use of MERS, and some have decided to purchase only MERS loans, which means their trading partners must be MERS members too.

In an effort to stay sensitive to industry needs and changes, MERS entered a cooperative effort with the American Land and Title Association (ALTA), which represents U.S. title companies. The effort produced MERS Link, a browser-based service that queries the MERS System for information important to title companies. Settlement agents can quickly determine the correct current servicer of loans by entering the property address, borrower name, borrower social security number or the loan's MIN. MERSE Link also allows the retrieval of information on more than one loan at a time, and a "hot link" to a servicer's web site if furnished.

MERS also offers a voice response unit (VRU) that settlement agents and consumers can access via the telephone. Once in the VRU system, users key in a MIN or applicable social security number to learn the name and telephone number of the current servicer of a loan registered on MERS.

How Does MERS Work?

There are several ways to incorporate MERS into a mortgage company's business practice. A typical scenario:

1. Close the loan on a security instrument that names MERS as the nominee for the lender and assign the loan a MIN.

2. Sell the servicing and beneficial ownership rights to an investor.

3. Once that sale is final, the lender registers the loan on the MERS System, naming the investor as the beneficial and servicing rights owner. Registration is done via a web-based system called MERS) OnLine, or by uploading a batch file to the MERS System.

4. The new investor/servicer takes responsibility for updating the loan record with information from county recorders' offices, along with any servicing event, such as a payoff or foreclosure. The system is updated using MERS OnLine or batch files.

5. If the investor/servicer sells servicing or beneficial ownership rights to another investor and a separate servicer, the new servicer (assuming it is also a MERS member) is responsible for maintaining the information on MERS for that loan.

6. Only member companies that have a current interest in the loan can access full information about it. In this case, the lender in Step 1 and the investor/servicer in Step 4 no longer have access to the information.

As the above scenario illustrates, MERS doesn't depend on automated county recorders offices or those with online capabilities. A 1999 survey by the National Task Force on Property Records found most offices were paper-based. About 25% of the more than 3,100 county recorders offices in the U.S. responded. The survey concluded that less than 4% of the respondents had Internet access, and that 20% planned to acquire access in the future.

Who Signs For It?

When a servicing event occurs, like a payoff, how does the current servicer process the lien release if the mortgage or deed names MERS as the mortgagee? If the loan goes into foreclosure, how does MERS execute the necessary documents?

The answer is a corporate resolution. The corporate resolution is a formal corporate act by the MERS board of directors, which authorize& members to act as an officer for MERS. Member company employees named in the resolution are known as certifying officers of MERS, and are typically the same employees who sign foreclosure and lien releases for the member. The corporate resolution has proven to be a very convenient, time-efficient and sensible method for handling servicing-associated documents.

What MERS is Not

MERS is not the owner of beneficial or servicing rights for loans registered on the MERS System. MERS doesn't collect or lend money. MERS doesn't create or transfer interests in loans or create electronic assignments.

The Future of MERS

The 26 employees of MERS share a common goal: they want to see MERS as the mortgagee of record for every housing loan in the U.S. This includes multifamily, homeequity loans, reverse mortgages and all other home loan variations. That is when all MERS members, and others with a need for the information on the MERS system, will get the most benefit.

MERS Outside the U.S.

Currently, MERS is focused on the U.S. market. The domestic focus allows MERS to gain expertise in the legal, operational, and financial aspects of the concept. MERS also gains experience in introducing the concept to a marketplace, and making plans and adjustments for dealing with MERS as a mature and accepted standard. However, it is understood that the MERS concept may work outside the U.S. The ability to serve as a single point of reference for property ownership information, and the ability to electronically track changes to ownership, might have appeal in other countries. Like the U.S., if property rights are tracked on paper, the MERS concept could automate those records. Alternatively, if the existing paper-based system remains, MERS could sit over the separate recording districts and offer one-point of reference for researching property rights nationwide.

For countries that have developed or are developing secondary mortgage markets, and the ownership change is accomplished through paper assignments, MERS could improve that process. In the event property rights tracking is embryonic, a MERS-type system could facilitate that growth.

Certainly, there are barriers to applying MERS outside the U.S., just as there were within the U.S. Successful introduction of an automated property rights system requires a level of technology acceptance and readiness by a country's mortgage finance industry. The legal framework must be in place so that property rights, changes to property rights, and access to data can be automated. If the corporate resolution model is needed, legal requirements regarding the use of signing authorities must be in place. Also, as in the U.S., the mortgage finance industry and the national, regional or local government responsible for property rights tracking must embrace the idea.

MERS works closely to identify and implement the most cost effective use of MERS for its members, but implementing MERS outside the U.S. will require an even higher level of customization and compromise.

CONCLUSION

Scenario 1:

A mortgage closing table in a lawyer's office in any American town. The buyer and seller are attending with their legal representatives. The property in question is shown in the county **recorder's** office as having one mortgagee of record for the past 20 years: **Mortgage Electronic Registration** Systems, Inc. The current servicer is identified via a computer. There are no breaks or irregularities in the chain of title, so the closing takes place uninterrupted.

Scenario 2:

Mortgage Servicer A plans to sell the servicing for 10,000 loans to Servicer B. While conducting the due diligence on the loan files, Servicer A is satisfied that all the loans were registered on the **MERS** System at origination, which means there are no assignments. Servicer B, also a **MERS** member, agrees to pay a premium for the servicing. Servicar B may save up to $220,000 because it doesn't have to record new assignments.

Welcome to the new world of **MERS. MERS** has gone from fledgling concept to thriving reality in the U.S. in eight years. As more mortgage companies and housing agenties mandate **MERS**, the current 4 million **MERS**-registered loans will increase almost exponentially. The hurdles **MERS** has overcome were big and often discouraging. But **MERS** supporters understood its value and how it would eliminate huge mortgage industry inefficiencies and they broke down every wall they came against.

"Our challenge: How deep can we take **MERS** into the mortgage industry. To reach our goal of registering every real-estate loan in the U.S., we must make **MERS** better, simpler, cheaper and faster for everyone involved,"Arnold said.

GRAPHIC: IMAGE GRAPH, Figure 1
IMAGE GRAPH, Figure 2
IMAGE GRAPH, Figure 3

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Exhibit 11

MERS aids electronic mortgage market Mortgage Banking January, 1997

Mortgage Banking

January 1997

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"MORTGAGE SERVICING RIGHTS HAVE BECOME A COMMODITY, notes Dick Hebl, senior vice president, loan administration at Knutson Mortgage Corporation in Minneapolis. "But they are traded in a cumbersome, involved manner." Hebl says that time delays-and the problem of adequately serving borrowers while transferring a loan package-increase the difficulty of buying or selling servicing.

Knutson Mortgage is an active subservicer receiving many "sight unseen" loans that often come with existing problems, adds Hebl. Ownership rights often are not correct on county land records, he explains. For instance, a defunct savings and loan might be named as the servicer. Hebl's staff then must track down a government official who is authorized to sign on behalf of the long-gone financial institution.

New approach

An automated alternative to these problems is the promise of the new **Mortgage Electronic Registration** Systems, Inc. (**MERS**). Knutson Mortgage is one of **MERS**' charter members, and Hebl recalls thinking "this is a big deal" when he first saw how **MERS** would work.

Knutson Mortgage is incorporating **MERS** into its loan origination software. In 1997, the firm will start generating an 18digit mortgage indentification number (MIN) for every origination. A MIN will stay with a loan throughout its life-even as ownership of the loan and its servicing changes hands.

Knutson will record the mortgage or deed of trust in public land records, just as it does today. But an assignment also will be recorded in the county records, naming **MERS** as mortgagee-ofrecord.

MERS then electronically will track ownership and servicing transfers on that loan. When rights are traded, no additional assignments would have to be recorded in the land records. And unrecorded assignments, which currently are prepared for investors or warehouse lenders, also will become unnecessary.

MERS will register each loan according to its MIN and serve as an electronic clearinghouse for recording ownership rights and ongoing transfers. It will seek to cut costs and reduce errors by centralizing certain information now scattered through closing documents, public land records and mortgage assignments.

"MERS addresses a problem that was costing the industry a significant amount of money," says Rick Amatucci, a Fannie Mae vice president and the agency's liaison with MERS. He recalls that the idea grew out of an Interagency Task Force, which brought the secondary marketing agencies and the Mortgage Bankers Association of America (MBA) together "to identify ways to bring efficiencies to the industry," Amatucci says.

A feasibility study and business plan were then developed before incorporating MERS in 1995, says MBA Executive Vice President Warren Lasko. He cites "a very high level of enthusiasm" within the industry for an initiative that is designed to: U Lower costs for servicers, which offers benefits to themselves as well as their borrowers.

U Provide immediate access to information on mortgage ownership rights to both consumers and the industry.

(Table Omitted)

Captioned as: What MERS Costs

* Lessen the potential for fraud by giving lenders the ability to track individual mortgages throughout their life span. MERS President and Chief Executive Officer Paul Mullings cites a "very, very positive response" to the system. "Some say it was overdue for the industry," he adds. Mullings sees MERS as part of a movement toward the use of electronic rather than paper-based processes in mortgage lending.

The genesis of MERS reveals the industrywide cooperation behind the initiative. Fannie Mae and Freddie Mac each invested $ 1 million in MERS as startup capital. Lenders, industry vendors and real estate professional associations combined to bring in another $ 2 million.

MERS is a nonstock corporation owned by its members-similar to the way MasterCard is owned by financial institutions offering the cards. However, MERS has two classes of members. Charter members have a financial interest in the project, in addition to the voting rights that all members enjoy.

A bright idea In January 1997 MERS plans to hire four additional staff members-to bring the total in its McLean, Virginia, offices to just 10. Yet the senior management team of Mullings, General Counsel Roland Arnold III, and Senior Vice President of Operations and Information Management Dan McLaughlin come into the venture with reputations of previously helping to develop financial services innovations.

Mullings formerly was CEO of the residential mortgage division at Los Angeles-based First Interstate BanCorp. Arnold was part of a team at AT&T Universal Card Services which won the 1993 Malcolm Baldridge award. McLaughlin previously helped make the industry more aware of technology as an MBA staff member. MERS is likened to an "industry utility"-a cooperative effort to cut expenses for many lenders and servicers. Servicers, investors, warehouse lenders and consumers all should easily recognize what firm is servicing a given mortgage once it's within MERS. Because it is the mortgagee-of-record, MERS also will receive all legal notices and forward mail to servicers.

Multiple avenues for accessing MERS will be available, ranging from toll-free numbers to dedicated phone lines. MERS officials say they want to allow lenders to use the technology they already have, as much as possible, to avoid forcing companies to make further investments in order to use MERS.

People involved with the development of MERS note that the system's largest potential problem is simply that lenders won't use it enough to build a sizable database of loans. However, four industry vendors have developed strategic marketing alliances with MERS in an attempt to gain early acceptance by servicers and lenders.

Servicing broker Hamilton, Carter, Smith & Co., in Los Angeles, due diligence firm Hanover Capital Partners Ltd., of Chicago, Milwaukee-based mortgage insurer MGIC Investor Services Corp., and Stewart Title in Houston will be encouraging lenders to use the new system. "We want to help increase mortgage lending profitability and efficiency," says Curt Culver, president and chief operating officer at Mortgage Guaranty Insurance Corporation (MGIC).

David Greco, vice president of marketing at MGIC, says larger lenders will be taken through a customized analysis showing the financial benefits they can expect from using MERS, rather than using traditional assignments. Adopting the system "doesn't appear to be a very difficult question" for most servicers, he adds.

Projected savings

An average life-of-loan savings of almost $ 70 is forecast by MERS, by figuring savings of $ 10 each on unrecorded assignments to an investor and warehouse lender, and $ 40 on recorded assignments when servicing is sold. Additionally, MERS expects to save lenders $ 7.50 per loan on lien releases.

"Savings depend on how much a lender transfers servicing," says Stephen Morrison, senior vice president, secretary and general counsel at Norwest Mortgage, Inc., in Des Moines, Iowa. Morrison currently is chairman of the MERS board of directors.

Adding efficiency to servicing trades should increase the intrinsic value of servicing, according to people close to the project. MERS estimates its use will cause loans to trade $ 25 to $ 50 higher, and that servicing liquidity also will be increased.

Herman Churchwell, chairman and CEO of Hamilton, Carter, Smith & Co., predicts a two-tier market will emerge in servicing sales. Packages of loans registered with MERS will trade for more, Churchwell adds.

Although most industry observers expect MERS to bring in savings, "estimates range widely" as to the exact amount, says Mark Fleming, vice president of strategic partnership development at Freddie Mac and the agency's representative to MERS. He adds that industrywide savings are projected at between $ 77 million to $ 200 million annually.

Getting involved

EDS-based in Plano, Texas-is spending millions of dollars to build and maintain the

MERS infrastructure, which is modeled after the book-entry system used by Wall Street firms to record ownership interests in securities. In return, EDS will earn fees from the registry's use.

"Lenders are pleasantly surprised at the ease of adjusting their systems to use MERS," Mullings notes. "We supply turnkey software to help."

Although Mullings won't disclose revenue projections for MERS, he predicts the system will register 10 to 15 percent of all new originations and servicing transfers within a year of its April 1997 rollout. At the end of year two, Mullings foresees 25 percent of assignments moving through MERS.

And in five years he projects that 70 to 75 percent of all new originations and servicing transfers will be performed with the help of MERS. "The faster the database grows, the faster the benefits grow to the mortgage banking industry," Mullings says.

Rollout of MERS is scheduled to begin according to the following schedule: Allied Mortgage Group, Inc., and Norwest Mortgage, Inc., will start registering MIN numbers with MERS in late March. Then 1st Nationwide Mortgage will go on the system in April. GE Capital Mortgage Services, Inc.; Knutson Mortgage Corp.; Merrill Lynch Credit Corp.; and ReliaStar Mortgage Corp. will follow in May.

July will see HomeSide Lending, Inc., and Weyerhaeuser Mortgage Corp. using the system, according to plans. General members will be welcomed once these charter members are on MERS. (See sidebar for more on charter members.) Technology partner

EDS-which also provides electronic commerce facilities for other industries-will assist MERS members as they go online. Service bureaus and software vendors also are being given technical information to align their systems with MERS.

"Building an interface is not difficult" says Lesley Grimes, vice president and mortgage servicing product manager at ALLTEL Information Services, Inc. in Jacksonville, Florida. A lack of lender awareness will slow the use of MERS more than technical matters will, she adds. "Education is the most important issue" for MERS, Grimes says.

Most servicers are taking a wait-and-see attitude toward MERS, adds Dick Bryant, president of Fiserv Mortgage Products in South Bend, Indiana. But he adds that acceptance of the system is a question of "not if, but when."

Grimes agrees that "most servicing managers think MERS is a good idea. But they will let other people do it first." However, Bryant expects Fannie Mae and Freddie Mac will "lean heavily" on lenders to encourage use of MERS.

Grimes notes that one way that could be done is by pricing differently for loans, depending on whether or not they are registered with MERS. She adds that large correspondent lenders also might put higher value on purchased mortgages that have MIN numbers.

Unresolved issues

Industry acceptance of MERS probably will follow a "hockey stick" pattern, says Leilani Allen, Ph.D. Allen is director of mortgage banking at Tenex Consulting in Burlington, Massachusetts, the principal consultant involved in establishing MERS.

She explains that technology innovations often experience a period of relatively light adoption, which is then punctuated by a sharp upward rise in use. "Once reports that efficiencies are being found come out," she says, "lenders will say, 'We must do this-or else!'"

But she notes that initally MERS will have some "kinks to work out," along with a challenge to explain itself to the industry. Companies deciding to move ahead with MERS also will find themselves with business decisions to make, adds Allen. "What do you do with the people in your firm who are doing assignments now?" she asks. Cutting back or reassigning staff are alternatives lenders will consider as they move into MERS.

ALLTEL's Grimes adds that servicers will need to alter their processes once they are part of MERS. For instance, MERS must be notified whenever a loan in its database goes into foreclosure.

Although several of the nation's major mortgage servicers are MERS charter members, some national lenders are unenthusiastic about becoming involved with the project at this time. Some are reluctant because they haven't seen the product working or analyzed its costs. Others don't see MERS saving them anything in the context of how they work.

Yet those already involved with the project are optimistic. Having large servicers as charter members goes a long way toward building the necessary critical mass to make MERS a success, note Amatucci and other observers.

Norwest's Morrison says, "It will take a year or so, and then growth will take off, as lenders see that MERS works." Cost savings and premium servicing values will bring the mortgage industry to MERS, he adds.

Morrison adds that "almost all lenders are thinking of this as a fait accompli." Software vendors tell Morrison that being able to integrate MERS in their systems "is a 'have to have,' not a feature that's 'nice to have: It's almost like a compliance issue," he says.

Norwest Mortgage will first use MERS with retail loans, by making the MIN its loan number. When correspondent or wholesale loans come to Norwest from non-MERS members, the MIN will be added at that point. All MERS members agree to make MERS the mortgagee-of-record or beneficiary of the deed of trust for every new loan they originate or service.

Strong commitments

Allen notes that becoming a MERS member generally has been a CEO-level decision for the charter companies involved. One reason is that a financial commitment was required.

Yet, she adds that another important factor for some charter members was having the opportunity to help fashion MERS from its inception. "Having a seat on the board is more important than return on investment," says Allen.

In addition to the $ 1 million cash infusions from Fannie Mae and Freddie Mac, large charter members put in $ 250,000 each, midsized members added $ 100,000 apiece and small members came up with $ 10,000 to $ 50,000-to invest a total of $ 4 million in the project.

MERS allocates these capital investments as 75 percent debt and 25 percent equity. Loans are projected by MERS to return an annual compounded rate of 20 percent, while equity will earn an estimated 12 percent a year.

Capital plus interest will be repaid by the end of the year 2000, according to MERS. Charter members also have the option of choosing discounted transaction fees for the first three years of MERS' operation, in lieu of a cash investment return.

Original investors came in "on faith," notes Allen, because the details of how MERS would work weren't ironed out until mid-1996 at working group meetings involving different industry players. Lenders and servicers of various sizes, along with the secondary market agencies, "got in a room together, walked through the process, and came to an agreement," says MERS' McLaughlin.

Allen adds: "I was particularly impressed that people from very different organizations could coalesce around what MERS should do, and how it should operate. That's hard to do within a company, much less between fierce competitors."

Single niche But as with any new venture, there are vested interests to encounter and resistance to change. McLaughlin explains: "We're not competing with anyone, or displacing anyone. We've kept focused on a niche-electronically registering and tracking mortgage rights."

Yet, he adds that document custodians and tax service companies have wondered if MERS would change their industry roles. However, "MERS won't change" traditional industry relationships between lenders, service providers and secondary market agencies, says Norwest's Morrison.

In fact, McLaughlin believes MERS will make the working relationship between servicers, investors and warehouse lenders "much more congenial than it is today" He notes that all parties will more easily be able to track loans to ensure that contractual obligations are being met.

Morrison predicts that warehouse lenders will require the use of MERS to help avoid the possibility of funding two loans on the same property. He notes: "Today it's very much up in the air who gets stuck if the wrong party is paid." He adds that under MERS, warehouse lenders are released from liability if they pay according to instructions.

Future enhancements

Freddie Mac's Fleming says the existence of MERS will help build "a movement towards electronic commerce" in the mortgage industry. "It's possible that MERS could move into new functions," he notes.

Fannie Mae's Amatucci agrees that "MERS will be a good model. Maybe there are other areas where we as an industry can work together."

Tenex's Allen says, "It's inevitable that MERS will do more in the future. MERS also will encourage other cooperative efforts in the industry." Sharing information to help servicers with loss mitigation is a possible example, she adds.

"MERS can branch out," adds board chairman Morrison. "But we want to concentrate on doing this right first. There are lots of ideas-but we want to get a few years down the road before starting any new projects." Industry concerns

Allen cites MERS as an example of "industry maturity. We're looking for efficiencies at the industry level, not the department level."

Yet several industry participants are concerned about how MERS will affect their future. "A number of different people felt threatened at the working groups," recalls James R. Maher, executive vice president of the American Land Title Association (ALTA). "There were questions about if it could come off and the cost to implement MERS. Some questioned the cost/benefit analysis," he adds.

Maher notes that some title insurers initially saw MERS as "moving away from local land records, and putting it into the hands of a third party that we had no unique access to and that was not designed to help us do our job." He adds that involvement with MERS since its inception has helped to soothe those concerns, although they are not totally gone from the title industry.

How much title insurers will have to pay to access MERS for information on many loans "is still up in the air," says Maher. He adds that "high-volume title companies may have to belong to MERS, at an undetermined cost." Although the openness of MERS is a comfort to the industry, Maher says large title firms will need access beyond having an 800 number to call.

ALTA General Counsel Edmond R. Browne notes that MERS "is not a substitute for title insurance or the public land records. In fact, the foundation of MERS is in the public records."

Having centralized, accurate information about who is servicing specific loans could save title firms money, note the ALTA executives. But they add that until half of all outstanding loans are on MERS, the cost of examining the database probably will outweigh any benefits.

Maher explains there is "a possible perceived diminution in the value of our product" to be weighed against "the efficiency of having close to absolute assurance that the right party is being paid" at closing.

Title insurers hope that in the future MERS can electronically transmit payoff amounts and other release information, Maher says. Until then, they are hoping that MERS will enforce lienrelease requirements.

Recorders are worried Less optimism is found in county recorder offices. MERS "will take fees out of recorder's offices," says Rebecca Jackson, Jefferson County clerk in Louisville, Kentucky. She also is the land records interest group leader for the National Association of County Recorders and Clerks.

Recording assignments "is one of the more profitable things we do," she adds. Although new deeds will continue to be recorded in county offices, Jackson notes, "reassignments are much easier to process."

She adds that recording fees vary across the country. In fact, Jackson claims that in some places **MERS** fees will actually be higher, which is "a downside for consumers."

Making sure homeowners are protected from fraud and guaranteeing that consumers and county **recorders** will have access to **MERS** data are her main concerns. Jackson notes that "it will be easier for the public to get information, if **MERS** keeps its promises." And she says, "**MERS** has been very responsive" to input from county **recorders**.

"But we haven't seen it yet," Jackson adds. Although "the majority of **recorders** have had information across their desks about **MERS**," she notes "a good deal of education" will be needed before all the nation's **recorders** are aware of the new system.

Jackson says that many county **recorders** will contact **MERS** as a customer service on behalf of people seeking information about assignments. "We will be the ones educating the public at the initial point of contact," she says. "It will add time to our day." To make this easier, Jackson hopes to be able to have an online hookup with **MERS-which MERS** officials say Kenosha County in Wisconsin already has done.

Ongoing implications Tenex's Allen says that an additional issue is that the industry groups involved might disagree about how to run **MERS** in the future. However, she says items agreed on to date already "define 80 percent of the answer" to most issues that could arise.

Board Chairman Morrison adds that the **MERS** *governing structure has worked so far. We'll see how it will work with more general members."

Functionality is another concern any new technology raises. If savings come to lenders as projected, EDS could be poised to gain further business as electronic commerce grows in the industry. EDS currently is working on another project designed to offer electronic document preparation and storage.

Balanced against these challenges is the vision of cost savings, better information, and more valuable servicing assets. Providing better data about the mortgage industry's primary asset-servicing-is an important step in the industry's evolution. M B

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Exhibit 12

MERS: Tracking Loans Electronically.

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MERS passed a milestone late last year by getting past the 1 million loan mark on its electronic registry for mortgages. A key change to standard loan documents ushered in the MERS-registered loan as a more accepted part of the origination process. This step sets the stage for industrywide acceptance of this paperless and cheaper alternative to assignments.

THE TERM "BEST EXECUTION" HAS SPECIAL MEANING FOR THE MORTGAGE INDUSTRY. But, in general, it can be defined as the most desirable and valuable way of doing things with the highest degree of skill. Has MERS (Mortgage Electronic Registration Systems) provided the industry with that kind of value? Let's take a look at a little history and at the various lenders and servicers using MERS today.

December 1999 marked a milestone in the brief history of MERS, as the company passed the 1 million mark in mortgage loan registrations on its national electronic loan registry. McLean, Virginia-based MERSCORP, Inc., is the operating company that owns the MERS(r) System and is the parent of Mortgage Electronic Registration Systems, Inc., McLean, Virginia, which is the company that appears as mortgagee of record in the county land records.

MERSCORP, Inc., was formed by Mortgage Bankers Association of America (MBA) member companies as a central electronic loan registry in an ambitious attempt to help lenders streamline the lending process and eliminate the need to record assignments when selling loans to other mortgage companies.

In 1998, the industry's leadership recapitalized MERS to permit the company to complete what it had begun in its first year of operation. Now is a good time to check the progress of the effort and take a look at the future.

As you read this, nearly 1.5 million loans will have been registered on the MERS System. More than 100 companies use MERS, with registrations occurring every day. Six of the top 10 mortgage originators (according to Inside Mortgage Finance) are originating or purchasing MERS-registered loans. Other major originators and aggregators, representing 20 of the nation's top 30 lenders, are integrating MERS into their operations this spring and summer. The participation in MERS by these lenders, plus its acceptance by Fannie Mae, Freddie Mac, Ginnie Mae, Federal Home Loan Bank, VA, FHA and major Wall Street rating agencies, means that all lenders and investors can accept MERS-registered loans.

A little history

The rising tide of paper that was choking mortgage loan productivity in the early 1990s provided the impetus for an industry task force to recommend the establishment of MERS in an effort to eliminate the need to prepare and record assignments. MERS would allow mortgage lenders and servicers to cooperate to reduce or eliminate their paperwork burdens and bring a higher level of efficiency to secondary market sales and trades between trading partners. Because secondary market transactions involving the sale of both beneficial rights as well as servicing rights generated a flood of paper mortgage loan assignments, MERS took up the task of providing an alternative to using paper for tracking these transfers between trading partners.

The Depository Trust Corporation (DTC), New York City, provided a good model. DTC had long ago enabled the national securities markets to eliminate the need for paper stock certificates to record the purchase and sale of stocks, bonds and other securities. DTC is a participant-owned corporation that records securities transactions electronically, eliminating the need to pass paper stock certificates or other security certificates back and forth. It is difficult to imagine accommodating the current volume of securities trading on the national exchanges if stock traders were required to use paper certificates to pass ownership rights.

The MERS System was designed to perform similar functions for mortgage lenders, but with a difference: MERS would first concentrate on eliminating mortgage loan assignments by providing an electronic registry to track the many transfers that occur in our active markets today. Although many lenders are using assignments to make MERS the mortgagee of record, the maximum cost reductions for lenders occur when MERS appears in the security instrument. This concept is known as MERS as Original Mortgagee (MOM).

MERS received approval from Fannie Mae and Freddie Mac in 1997 to act as mortgagee of record on uniform security instruments. This approval meant that MERS could be named in the mortgage or deed of trust as mortgagee and nominee for the lender at the outset. Then once the security instrument was recorded, transfers of beneficial rights and servicing rights could be tracked on the MERS electronic database, eliminating the need for any recorded assignments between trading partners. Approved Fannie Mae/Freddie Mac security instruments became available in late spring 1998 from document vendors.

Systems, the MIN and value

Mortgage lenders can be reluctant to embrace change, especially to their business processes. While naming MERS as mortgagee on the security instrument seems a fairly straightforward change, loan origination systems and servicing systems needed to be modified. Several large mortgage lenders and servicers that could see the immediate benefits of eliminating assignments from their operations began to make the necessary system changes.

The process was slow, but by the end of 1998, several lenders and wholesalers were ready to originate and/or purchase MERS-registered loans from trading partners. The process continued to gain momentum during 1999, in spite of a lengthy systems freeze imposed on most lenders by Year 2000 computer concerns. As companies lifted their Y2K development freezes, MERS activity accelerated.

"Today, many vendors have completed MERS-related enhancements or are in the process. MERS-ready software is rapidly becoming a feature demanded by mortgage companies," says Dan McLaughlin, executive vice president and product division manager for MERS. "In the last year, we have seen MERS readiness become key criteria in our customers' evaluation of new software products. In exhibition halls and in advertising, the 'MERS-Ready' logo is prominently displayed by those vendors that have completed integration testing with us."

Not to be left in the dust in the race for e-commerce solutions, McLaughlin announced at the MERS user conference in March that MERS will introduce a browser-based interface for registering loans on MERS in May. "Market research indicates that our MERS Lite members should gain substantial benefits from registering loans through our Web-enabled interface to MERS," says McLaughlin. "It's one more way that we are making it easier for customers to use MERS." MERS Lite members are companies that typically originate and sell their production servicing-released.

MERS benefits are available to lenders by using a mortgage identification number (MIN) that can be created by the lender and placed on the mortgage or deed of trust prior to closing. This change affects loan origination and closing document systems. The MIN is used on MERS to track a mortgage loan throughout its life. The MIN must be recognized and tracked by loan origination, secondary market and servicing systems.

The good news for companies embracing system changes was that using MOM, as the practice has come to be known, provides an immediate cost reduction of approximately $22 per loan. The MERS registration fee is $3.50, yielding substantial savings over paper processes. This up-front cost savings has provided a powerful incentive for lenders who deal in secondary market transactions, which is the majority of lenders today.

Mortgage loan servicers also benefit substantially from the elimination of the need to track, account for and correct paper assignments. As servicing rights are traded, transfers are tracked electronically on the MERS database. No assignment is required to effect the transfer between MERS mem bers, nor for sales to Fannie Mae or Freddie Mac, for inclusion in Ginnie Mae securities or for private rated or nonrated securities.

MERS impact on securities

In Februry 1999, Lehman Brothers took the first step in the securities market by including MERS-registered loans in a jumbo mortgage-backed security (MBS). This security gave the rating agencies the chance they had waited for--an opportunity to rate a MERS package. Standard & Poors, Duff & Phelps and Fitch IBCA have rated securities containing loans that name MERS as mortgagee of record without hurting the security's rating.

Moody's Investors Service took the opportunity to issue an independent Structured Finance special report entitled "Mortgage Electronic Registration Systems, Inc. (MERS): Its Impact on the Credit Quality of First-Mortgage Jumbo MBS Transactions" in April 1999. The report states that the "impact on the credit quality of jumbo first-mortgage MBS transactions will be negligible." The report also identified areas that would not be harmed: the legal mechanism to put creditors on notice of a mortgage is valid; the ability to foreclose and take real estate owned (REO) will not be materially affected; and credit enhancement levels for first-mortgage jumbos will not be increased as a result of the use of MERS. (Any nonstandard could add credit enhancement; MERS does not).

However, the most significant finding in the report specified that in transactions where the securitizer used MERS, there would be no need for new assignments of mortgages to the trustee of MBS transactions.

"We are aware of five major companies that have MERS-registered loans in their securitizations: Lehman Brothers, Bank of America, Norwest, Residential Funding Corporation [RFC] and Countrywide," says Bill Hultman, senior vice president of MERS. "These companies have been the pioneers and cleared the path for MERS as the best execution for all types of mortgage loans."

In pursuing acquisition of MERS-registered loans, REC indicated that the cost savings would be approximately $15 to $17 a loan. Norwest estimated its savings would be in the neighborhood of $300,000 to $500,000 this year for its correspondent loans (i.e., savings from back-office improvements such as elimination of the need to track, correct and rerecord missing or incorrect assignments).

Rick Scogg, president of Aurora Loan Services, Aurora, Colorado, says his company saves hundreds of thousands of dollars a year. "We have already benefited and will benefit considerably more in the future," he says. "We buy and sell servicing frequently. When we buy portfolios, there are payoffs and foreclosures the next day and therefore there is a delay in the lien-release process [for non-MERS loans]. With MERS, we don't need to get attorneys to correct these, and that saves us thousands of dollars a year.

"Truly, the foreclosure and release process is the biggest pleasant surprise for us," Scogg says. "It has had a major impact on our efficiency after acquisitions."

Warehouse lenders

As MERS memberships and registrations grow, more sectors of the mortgage industry come in contact with the benefits of MERS. Interim funders can get a security interest in a MERS-registered loan in three ways: they can accept an unrecorded assignment from MERS in recordable form; waive the unrecorded assignment by becoming a MERS member and registering its interest on the MERS System; or waive the unrecorded assignment from MERS and enter into an electronic tracking agreement that establishes a contractual relationship among MERS, the interim funder and the mutual customer.

The electronic tracking agreement has emerged as the best and most comfortable solution for these lenders and for MERS and its members. It gives everyone a contract that all parties agree to, which requires MERS, upon notice, to become the nominee for the interim funder in the public land records. That means the security interest of the interim funder is automatically perfected without any further action if there is a default by the MERS member who is also the interim funder's customer.

"We anticipate this will become the method chosen by most interim funders," says Hultman. "Several entities have approved this method and accepted it as a way of doing business without requiring the traditional unrecorded assignment. As more companies adopt this as a way of doing business, it will quickly establish MERS as the best execution in this arena as well."

The lender advantage

From the outset, MERS was designed to be the central electronic registry that tracked the ownership of mortgage loans for the entire industry. The approval of MOM (where MERS serves as nominee for the lender in the recorded security instrument) by Fannie Mae and Freddie Mac allowed the industry to register loans on the system without a prior assignment. Let's look at how registration and tracking of ownership rights on MERS have worked and examine if MERS delivered the cost savings that was projected.

There is no doubt that approval for MERS to act as original mortgagee provided the catalyst for the success of MERS. In the year and a half since MOM loan documents became available, many more companies have activated their membership (some companies had a latent deactivated membership status, while others became members) in MERS. The first two large companies to encourage their correspondents to deliver MERS loans were Norwest Mortgage (now Wells Fargo), Des Moines, Iowa; and Nations Banc (now Bank of America Mortgage), Charlotte, North Carolina. In fu1lly 1998, Merrill Lynch Credit Corporation became the first lender to originate MOM loans by using MOM securityinstruments. But another national company took its MERS participation one step further.

In 1999, Old Kent Mortgage Company, Grand Rapids, Michigan, became the first nationwide company to implement MERS companywide for correspondent, wholesale and retail origination channels. Old Kent registers loans in two ways: by using MOM and by assigning closed loans- either purchased or in portfolio-to MERS.

After one full year of experience with MERS, Old Kent has realized many benefits. Says Michelle Genrich, vice president of operations for Old Kent, "There is no doubt that the savings identified in the cost benefit [analysis] are now a reality. The registered loans have not gone to final payoff yet, but we expect even greater benefits at that time. The next refi period will be the true test, and we have no doubt the savings will be there also."

Old Kent has benefited from streamlining the origination process through the elimination of the assignments. The $3.50 registration fee is paid by the borrower and is shown on the HUD-I for conventional loans. "MERS is a win-win [situation]," says Genrich. When lenders originate loans using "MERS as Original Mortgagee (MOM), the need for an assignment is eliminated-creating a cost savings of about $22 per loan. Old Kent has listed the $3.50 charge on the HUD-I and the borrower has paid the $3.50 instead of paying the $22 for an assignment.

Alliance Mortgage Company, Jacksonville, Florida, has been registering loans on the MERS System for two years, both using MOM documents and by assignment. "The elimination of the assignment has been tremendous for us," says Betty Ellis, vice president of operations for Alliance. "It is not just confined to the monetary savings of not having to record the assignment, but all of the nitty-gritty [steps involved] in many processes that cost time and money.

"For example," Ellis says, "the accounting department has savings directly related to MERS that were not identified in the cost-benefit analysis. If a recording fee check doesn't clear the bank for an extended period of time, it has to be reissued and other departments notified about the stale check. This multiplies over a period of time when there are thousands of loans. The back office saves a tremendous amount of time. The savings per loan in this case is a minimum of $20."

McLean, Virginia-based NVR Finance, Inc., has adopted MERS registration to streamline deliveries to its correspondent trading partners. "The initial impact within the company has been great," says Charles L. Riecker, executive vice president of NVR. "For example, in our managers meeting when we announced we would be doing MOM docs, our managers expressed tremendous expectations of greater efficiencies as a result.

"One of the title companies that does a lot of business with us said they would like to insure all of their loans in this fashion. They were overjoyed," Riecker says. "The concept is so simple, but people in general don't grasp the ramifications of MERS. Even in a situation where servicing is retained, some loans require more than one assignment. The changing market creates additional assignments. MERS eliminates all that."

Big benefits for servicers

A number of servicers that have serviced MERS-registered loans are already reaping the benefits of MERS. Large and small servicers benefit from the elimination of assignments in a number of ways. From the beginning of the postclosing process, savings occur because companies do not need to track documents and re-record them if errors occurred. Unrecorded assignments to Fannie Mae and Freddie Mac are unnecessary, and Ginnie Mae certification procedures are streamlined.

HomeSide Lending, Jacksonville, has experienced cost and time savings in postclosing areas not often easily identified. For example, HomeSide saves time by using MERS certifying officers for releases in the paid-in-full department, where completion of releases can be done in halt the time, according to Stephan Avery, project manager at HomeSide.

HomeSide is implementing MERS in phases. The company eliminated assignments by using MERS to register bulk loans and co-issue transactions. Eliminating as much as 300,000 agency assignments had a significant economic impact.

Says Avery, "Some trading partners were initially hesitant about registering loans on MERS. But we found that as we walked them through the process, they realized MERS was not a mammoth project requiring tons of resources to implement."

William Glasgow, executive vice president of HomeSide, has been instrumental in incorporating MERS into company operations. "We expect MERS to provide a long-term benefit to HomeSide's servicing and production divisions by simplifying the document tracking and recovery process," he says. "Furthermore, we expect our wholesale production customers to benefit by reducing the expense of originating mortgages. The economic benefit will be derived over the expected life of the book of business currently registered. The immediate savings for HomeSide comes from certain bulk transactions completed."

HomeSide has recommended its sellers utilize MOM security instruments and register loans on MERS.

Anthony P. Meli, senior vice president of Edison, New Jersey-based Chase Manhattan Mortgage, says, "MERS has enabled us to reduce costs for our business partners by eliminating the assignments. These are hard dollar savings for our clients and [that] is another reason for them to do business with Chase."

Chase correspondents have been delivering MERS-registered loans at an increasing rate, according to Meli. "Tracking assignments back and forth with county recorders' offices and just handling the paper is extremely expensive," says Meli. "These costs are embedded in the process, and eliminating assignments cuts these costs for us.

"We recommend MERS to our trading partners," Meli says, "because MERS-registered loans streamline the process, and we don't have to handle the paper either. The future for our industry relies on creating more efficiencies in the process, reducing costs and managing data, not paper. We encourage our business partners to take advantage of this methodology now."

Fleet Mortgage Group, Columbia, South Carolina, offers the perspective of a company preparing to integrate MERS into its business operations this year. "Fleet correspondent lending is and has been a huge proponent of MERS," says Stannye Baringer, senior vice president of correspondent lending operations for Fleet. "We believe that this is where the industry wants to be, as it clearly benefits all parties in the transaction. Many of our customers have approached us about MERS, and as more and more aggregators and servicers come on board with MERS, it will make it easier and less costly for correspondents to do business."

"A number of our customers are already MERS-enabled," Baringer says. "Because of the size of our servicing portfolio, we must have the process automated. At the same time that enhancements are being made to our servicing system to accommodate MERS, we are implementing a new front-end system. So it has taken us just a bit longer to roll out MERS to our customers. But we will be there, too."

In February, Principal Residential Mortgage, Des Moines, Iowa, announced its delivery program to correspondents. "Over the past year, our correspondents have been asking us to get involved with MERS," says Phil Kuhn, vice president of correspondent lending for Principal. "Our correspondents view us as having a full spectrum of products because we are able to accept MERS loans."

Kuhn cites the example of a recent discussion with a prospective correspondent. "This correspondent decided to come aboard with Principal because we are now MERSready. Correspondents view MERS as a future trend," he says. "We're absolutely recommending MERS to all our trading partners."

Service providers assist

One of the ways to measure best execution is to assess the impact of a process in business flows. Says Jim Stewart, vice president of new accounts for Glendale, California-based Nationwide Title Clearing, "Over the past two years or so, and especially last year, we at NTC have seen a marked increase in our clients' desire to record assignments to MERS. And I can't think of a single instance in which a client has wanted to 'deregister' a loan off of MERS."

Mary E. (Bette) Albarran, managing director of Bay View Financial Trading Group, Beltsville, Maryland, has worked with several customers who are MERS members. "As more companies become active on MERS, we will see trading of registered MERS loans really become advantageous for sellers, especially for agency paper," she says. "It all comes down to what the seller will net out of the gross purchase price. Preparation and recording of assignments erode that price. When both parties are on MERS, the costs are considerably reduced.

"All things being equal, if a seller is on MERS, they prefer to sell to a purchaser who is on MERS rather than to a non-MERS purchaser for whom they would have to produce assignments," says Albarran. "MERS-ready sellers can avoid the whole issue of assignments by performing transfers electronically to a MERS purchaser. Not only is cost a factor, but preparing, recording and tracking assignments is extremely time consuming.

"Obviously, purchasers pick and choose the portfolio offerings they will bid on based on a number of criteria," Albarran continues. "A purchaser will consider the size of the offering, the investor, the types of loans, WAC [weighted average coupon], WAM [weighted average maturity] and geographic location. It would certainly be an advantage for a MERS purchaser to find a seller who can provide MERS-registered product. An added advantage is the reduction in time to recertify pools."

Albarran also works with Bayview Portfolio Services, a MERS registrar. She believes that most companies that buy and sell loan servicing as a regular part of their business plan will use MOM. "At some point in time," says Albarran, "we will have to assume that most of these companies will become MERS members. It only makes sense."

R.K. Arnold, president and chief executive officer of MERS, has led the effort to encourage lenders and servicers to adopt MOM loans as their standard business methodology. "It's been gratifying to watch the trend of more and more companies embracing the MERS assignment-free method of doing business," he says. "The year 1999 validated the MERS concept with lenders large and small. It's now our job to accelerate the pace of industry acceptance in the year 2000.

As thousands of new MERS-registered loans are boarded by servicers, the elimination of assignments from the business process has shown collateral benefits, even outside the typical residential mortgage transaction. "Our members have found numerous new ways that using MOM documents adds to efficiencies in their shops," says Arnold.

"We've also been approached by nontraditional lenders and commercial lenders to eliminate assignments from their processes as well," Arnold says. "In fact, in some respects the commercial lending sector is an even richer ground for MERS, because so many commercial deals require multiple assignments. We already have some commercial lenders that have decided to use MERS, and the timeshare sector seems to be particularly interested.

"Several electronic exchanges have approached us to do business as well. They see MERS as the only way to offer a fully electronic mortgage transaction; otherwise, assignments are required to sell the loans," says Arnold.

"Finally, second mortgages and home-equity loans represent some of our best volume--and subprime lenders, with all those multiple assignments, see extra benefits to MERS originations," Arnold says. "These business sectors will add to the overall savings that MERS can bring to the mortgage industry, making a MOM loan the best execution."

Carson Mullen is executive vice president and customer division manager for MERS, McLean, Virginia. He was formerly president and chief executive officer for Wasatch Document Systems, Salt Lake City, and vice president of national accounts for MGIC, Milwaukee.

The MERS Difference

In the Life of a Loan

The following is a brief summation of the pathway taken by a MERS loan:

* Originate and close loan with MOM security instrument and record with county recorder.

* Register the loan data on MERS(R) System.

* Track transfer of beneficial or servicing rights electronically (no assignment).

The following is the path of a non-MERS loan:

* Create security instrument and assignments for closing, both recorded and unrecorded assignments.

* Record security instrument and loan assignment with county recorder.

* Await return of recorded assignment.

* Correct assignment mistakes.

* Rerecord correct assignments.

* Endure constant follow-up from investors.

* Lose productivity chasing paper.

* Watch assignment costs multiply.

LENDERS ON THE MERS SYSTEM SINCE APRIL 1997

Aegis Mortgage Corporation

Alliance Mortgage Banking Corporation

Alliance Mortgage Company

Amaximis Lending, LP

Ameri-National Mortgage Company, Inc.

America Mortgage Express Financial

American Mortgage Funding Corporation

AmeriSouth Mortgage Company

Aurora Loan Services, Inc.

BancMortgage Financial Corporation

Bank of America Mortgage

Bank of New York Mortgage Company, LLC

Cal Coast Mortgage Corporation

Cendant Mortgage

Centennial Bank

Chase Manhattan Mortgage Corporation

Chevy Chase Bank, FSB

CitiMortgage, Inc. (formerly Source One Mortgage)

Citizens Bank of Cortez

Com Unity Lending

Commerce Mortgage Corporation

ComNet Mortgage Services

Continental Savings Bank

Corinthian Mortgage Corporation

Countrywide Home Loans, Inc.

Crescent Mortgage Services, Inc.

Eagle Home Mortgage, Inc.

Federated Lending Corporation

First Nationwide Home Finance

First Nationwide Mortgage Corporation

Fortress Mortgage, Inc.

GN Mortgage Corporation

Guaranty Bank, SSB

Harbor Financial Mortgage Corporation

Home Financing Unlimited, Inc.

HomeSide Lending, Inc.

Horizon National Bank

Household Financial Services

Ivanhoe Financial, Inc.

Ivy Mortgage

Landmark Financial Services

Majestic Mortgage Services, Inc.

Market Street Mortgage Corporation

McAfee Mortgage & Investment Company, Inc.

Merrill Lynch Credit Corporation

Mid America Mortgage, Inc.

Midwest Mortgage Services

Molton, Allen & Williams Corporation

Molton, Allen & Williams, LLC

Mortgage Investment Corporation

Mortgage South, Inc.

Nationwide Home Mortgage Company

Nextstar Financial Corporation

North American Mortgage Company

Norwest Mortgage, Inc. (now Wells Fargo)

Old Kent Mortgage Company

PNC Mortgage Corporation of America

Principal Residential Mortgage, Inc.

ReliaStar Mortgage Corporation

Residential Mortgage Corporation

Select Mortgage

Shea Mortgage

Shore Mortgage

Sound Mortgage, Inc.

Sterling Capital Mortgage

Temple-Inland Mortgage Corporation

Unity Mortgage Corporation

Visalia Mortgage Corporation

Voyager Bank/Voyager Mortgage

W/E Mortgage, Inc.

WestAmerica Mortgage Company

Western States Mortgage Corporation

Exhibit 13

SPECIAL REPORT OF THE WASHINGTON STATE BAR ASSOCIATION LEGAL OPINIONS COMMITTEE

Opinions on Deeds of Trust in Favor of Agents, Trustees and Nominees

July 12, 2011

RCW 61.24.005(2) defines the "beneficiary" of a deed of trust to mean "[t]he holder of the instrument or document evidencing the obligations secured by the deed of trust, excluding persons holding the same as security for a different obligation." The statute does not expressly permit an agent, trustee or nominee for the holder of the obligations to act as beneficiary, nor does the statute expressly prohibit it.

In sophisticated commercial financings, it is common for a deed of trust to name a beneficiary that may not be the holder of the secured obligations. For example, the named beneficiary may be the agent bank for a bank group or an indenture trustee for a group of bondholders. In home lending and some smaller commercial property financings, it is common for Mortgage Electronic Registration Systems, Inc. ("MERS"), as nominee of the lender, to be named as the beneficiary.

There has recently been litigation in which borrowers of home loans have challenged MERS' status as the beneficiary of Washington deeds of trust on the theory that MERS is not the holder of the secured obligations and, therefore, cannot validly act as beneficiary of a Washington deed of trust. The question was certified to the Washington Supreme Court by the King County Superior Court in the case of *Vinluan v. Fidelity National Title and Escrow Company, et al.*, Washington Supreme Court case no. 85637-1. Although the Supreme Court Commissioner declined to accept discretionary review of the question, his Ruling Denying Review filed April 25, 2011 stated that "whether MERS can be a deed of trust beneficiary under Washington law is an important issue that deserves resolution, probably by this court." Thereafter, the United States District Court for the Western District of Washington entered an Order Certifying Question to the Washington Supreme Court in which it certified similar (if not identical) questions to the Supreme Court. *Bain v. Metro. Mortg. Group Inc., et al.*, No. C09-0149-JCC (W.D. Wash. June 27, 2011) (Coughenour, J.). As of the date of this special report, the Supreme Court has not ruled on the certified questions in the *Bain* case.

The Committee believes that, in a properly presented case, a Washington court considering the question should conclude under agency principles that the holder or holders of the obligations secured by a Washington deed of trust can appoint an agent, trustee or nominee to act as beneficiary under that deed of trust. In some situations (*e.g.*, widely held secured bond obligations), there is no practical alternative. However, in the absence of controlling statutory or decisional authority, there is a chance that a court could rule to the contrary or could rule on the MERS situation in a way that unintentionally affects other types of representatives, such as agent banks and indenture trustees.

Given the uncertainty created by the *Vinluan* case, it might be appropriate to include a qualification drawing attention to this issue until the questions certified to the Washington Supreme Court by the *Bain* Court are decided. Such a qualification could be expressed as follows and added to the Washington statutes listed in paragraph D-3 of the Illustrative Opinion Letter form previously published by the Committee:[1]

> RCW 61.24.005(2) defines the "beneficiary" of a deed of trust as "[t]he holder of the instrument or document evidencing the obligations secured by the deed of trust, excluding persons holding the same as security for a different obligation" and does not expressly provide for such holder or holders to appoint an [agent] [indenture trustee] [nominee] to act as beneficiary. We express no opinion whether a deed of trust naming an [agent] [indenture trustee] [nominee] for the holder or holders as the beneficiary can be foreclosed nonjudicially.

As with the other qualifications set forth in paragraph D-3 of the Illustrative Opinion Letter, the Committee intends these qualifications to be advisory and customarily understood to apply, whether or not expressly set forth in the opinion letter.[2]

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[1] Supplemental Report Covering Secured Lending Transactions, a Report of the Ad Hoc Committee on Third-Party Legal Opinions of the Business Law Section of the Washington State Bar Association ("Supplemental Report"), at pp. 6-7 (Oct. 2000).

[2] *See id.*, n. 42

Exhibit 14

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA
SAN DIEGO DIVISION
Case No. 3:08-md-01988-DMS-WMC
Case No. 3:08-md-01972-DMS-WMC
Case No. 3:08-md-01957-DMS-WMC
Case No. 3:08-md-01888-DMS-WMC
- -x
In Re:
COUNTRYWIDE FINANCIAL CORP.
MORTGAGE MARKETING AND SALE
PRACTICES LITIGATION

THIS DEPOSITION RELATES TO ALL ACTIONS:
White v. Countrywide Financial
Corporation, et al., No. 08-CV-1972-
DMS-WMC; Jackson v. Countrywide
Financial Corporation, et al.,
No. 08-CV-1957-DMS-WMC; Leyvas v.
Bank of America Corporation, et al.,
No. 08-CV-1888-DMS-WMC;
- -x

April 29, 2011
9:15 a.m.

Deposition of CHRISTOPHER L. PETERSON, taken by attorneys for Defendants, pursuant to notice, held at the offices of Whatley Drake & Kallas LLC, 1540 Broadway, New York, New York, before Helen Mitchell, a Shorthand Reporter and Notary Public.

Peterson

bono matter where the borrower was the victim of a foreclosure -- fraudulent foreclosure rescue scam. My client has now passed away, and her daughter is her representative of her estate. We're litigating to try and recover the home equity -- the value of the home equity that we believe was inappropriately taken from my client. So that's an individual small case in Salt Lake City, where I live.

I'm also a consultant in a series of cases regarding the Mortgage Electronic Registration System, which I know you're familiar with. And those cases are pending around the country. My involvement in that case is relatively limited; I provided some advice about the legal foundation of those cases, but am not actively involved in litigating those cases.

Q Which cases are you referring to?

A These cases are False Claims Act cases that have been filed in a couple of different states and are being litigated.

Q And who is your work for there?

A The work in that case is for an

Peterson

attorney named Robert Hager. A group of several attorneys from around the country are working on that.

Q I just want to understand a bit more. You talked about advice about the legal foundation.

Can you talk about what that means?

A I was a consultant on some of the underlying legal theories involved in those cases, but my role has not been to brief or appear in court, et cetera.

Q But providing legal consultation; is that correct?

A That's right.

Q Is that work ongoing?

A To a limited degree. My involvement in the case is primarily in shaping -- attempting to help shape the legal theories upon which the case was going to proceed, but those cases are often actively being litigated, and my continuing involvement is minimal.

Q And what are your arrangements for

Peterson

payment in those cases?

A Well, in the pro bono matter, where --

Q I'm actually just asking about the MERS cases.

A Well, in the MERS cases I have a cut of the potential contingent awards that would be available if the cases succeed, but because I'm not contributing to the capitalization of the case, I'm not putting my own funds on the loan, I'm not supporting the -- you know, costs of the litigation, my cut is capped.

Q And what is that?

A My cut -- let's see, it's either 5 or 10 percent, I forget, but it's capped at $5 million in the event that there is a successful recovery.

Q And these are cases that contend that MERS -- the MERS system led to the deprivation of revenue by the county recorder's offices; correct?

A That's correct.

Q And it's your understanding that