Tennessee

Due Process and Notice to MERS

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Tennessee has now joined a list of states whose highest courts have held that the failure to provide MERS with independent notice of sales that might eliminate its interest in real property is not a violation of due process. In the recent case, the context was a tax sale. [*Mortgage Electronic Registration Systems, Inc. v. Ditto,* 2015 Tenn. LEXIS 100 (Tenn. Dec. 11, 2015)].

Background — MERS brought suit to set aside a 2010 tax sale of real property. MERS contended that the county's failure to provide it with notice of the tax sale violated its rights under the Due Process Clause of the U.S. Constitution.

Conflicting Decisions Reviewed — The Supreme Court of Tennessee found that the issue in the case "is better framed as whether MERS has a property interest that is protected under the Due Process Clause. *This is an issue of first impression in this Court.*"

After discussing general principles regarding the Due Process Clause, the court looked to other states for guidance. The majority of cases involving MERS have addressed MERS's appointment as beneficiary "solely as nominee" for the lender. Many cases have upheld such appointment. [See *Thompson v. Bank of America, N.A.,* 773 F.3d 741 (6th Cir. 2014)]. Thus, according to those courts, MERS has the authority *to act on behalf of* a valid note holder, so MERS is able to validly assign a deed of trust or enforce a note on behalf of the lender.

Other courts, however, have held that MERS's designation as beneficiary as nominee for the lender does not give it the power to assign a deed of trust. The typical reasoning is that because the note and security instrument cannot be "split," and MERS never held authority to assign the promissory note that evidences the actual debt, MERS would likewise have no authority to assign the deed of trust. [Citations omitted here due to space.]

The real question for the *Ditto* court, though, was not whether MERS had the authority to act on behalf of the lender, but whether MERS had its own *independent* interest that enjoyed protections under the Due Process Clause. The *Ditto* court found the relevant decisions divided. Some courts held that the appointment of MERS as beneficiary nominee for the lender did not grant MERS a protected interest in the property. *Ditto* relied heavily on *Landmark National Bank v. Kesler,* 216 P.3d 158 (Kan. 2009), to explain those decisions.

In *Landmark,* the Supreme Court of Kansas found that MERS being appointed a "nominee," was "more akin to that of a straw man than to a party possessing all the rights given a buyer ...." The Kansas court ultimately held that "[t]he Due Process Clause does not protect entitlements where the identity of the alleged entitlement is vague. A protected property right must have some ascertainable monetary value." *Landmark* concluded that MERS did not demonstrate "any tangible interest in the mortgage beyond a nominal designation as the mortgag[ee]. It lent no money and received no payments from the borrower. It suffered no direct, ascertainable monetary loss as a consequence of the litigation."

Ditto further looked to *Weingartner v. Chase Home Finance, LLC,* 702 F. Supp. 2d 1276 (D. Nev. 2010), for a discussion of MERS's role and usage of the term "beneficiary." *Weingartner* found that MERS was not a true beneficiary "in any ordinary sense of the word. Calling MERS a beneficiary is what cause[d] much of the confusion. To a large extent, defendants in these actions have brought this mass of litigation upon themselves by this confusing, unorthodox, and usually unnecessary use of the word 'beneficiary'...."

Summarizing *Landmark, Weingartner,* and similar cases, *Ditto* states: "[t]hese courts held that MERS was not the beneficiary under the deed of trust and, as nominee, was simply an agent or 'straw man' for the lender. As a result, these courts held that MERS did not have its own protected interest in the subject property."

Ditto also recognized conflicting decisions. For example, in Mortgage *Electronic Registration Systems, Inc. v. Bellistri,* 2010 WL 2720802 (E.D. Mo. 2010), a county failed to give MERS notice of a tax sale, while the Missouri statute required notice to any person "who holds a publicly recorded deed of trust, mortgage, lease, lien or claim upon that real estate." *Bellistri,* at *10. The court held that a "publicly recorded" claim in the property included MERS's appointment as beneficiary as nominee. Thus, it had a due process right to notice.

Conclusion — The *Ditto* court agreed with those courts holding that MERS is not a true beneficiary, despite such language in the deed of trust. The court noted that MERS "receives nothing from the [deed of trust] itself." As the language in the deed of trust specifically qualified the term "beneficiary" by noting that MERS was a beneficiary "solely as nominee" for the lender, MERS was able to act only as an agent for the lender, not for its own interests.

Ditto did not question MERS's authority to act as agent for the lender or successor lenders. However, *Ditto* held that its appointment as agent gave MERS no independent property interest whatsoever.

Finally, the court observed in *Ditto* that the notice provisions in the deed of trust itself only addressed required notices between the borrower and the lender; the deed of trust did not require any notice to MERS.

It is important to note that the Tennessee legislature has already acted to provide MERS a specific protection without the need to resort to due process arguments. Thus, the practical impact of *Ditto* in Tennessee may be somewhat limited. Nonetheless, the findings of *Ditto* may be far-reaching, as it is likely that other courts struggling to define the role of MERS and its true interest in mortgages or real property will find *Ditto's* logic compelling.

Washington

Two Important Judicial Decisions

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Notice of Default in Washington *(Leahy v. Quality Loan Service Corp. of Washington)*
Nonjudicial foreclosure in Washington is a two-notice process. The first notice, called the Notice of Default (NOD), provides a 30-day window for a borrower to payoff, reinstate, or elect mediation. If none of those three things happens, then the second notice (Notice of Trustee's Sale) is issued to set an actual foreclosure sale. Since the creation of the NOD, beneficiaries foreclosing in Washington have often sought guidance on when, and whether, to issue a new NOD if a sale doesn't occur.

With all of the state and federal loss mitigation programs, more foreclosures go on hold after the NOD issued — which results in this situation arising more often. The Washington Deed of Trust Act and amendments through the Foreclosure Fairness Act do not provide a clear answer to this question. The Division One Court of Appeals addressed this issue in a published opinion titled *Leahy v. Quality Loan Service Corp. of Washington, 2015* Wash. App. LEXIS 1363 (2015).

In *Leahy,* the trustee had issued an NOD in April 2010, and three subsequent notices of trustee's sale were issued: the first in 2010, the second in 2011, and the third in 2012. The Leahy property was finally sold under the third notice of trustee's sale in January 2013, close to three years after the issuance of the original NOD. The court analyzed the statute and concluded that Washington law did not require a new NOD before each new Notice of Trustee's Sale. The court looked at the legislative purpose of the NOD and concluded that it was to notify the debtor of the amount he owes, and that he is in default.

The *Leahy* court examined an earlier appellate ruling, *Watson v. Northwest Trustee Services, Inc.,* 180 Wash. App. 8, 321 P.3d 262, review denied, 181 Wash. 2d 1007 (2014). There, the court held that the trustee was required to reissue an NOD when the Notice of Default was issued before the effective date of the Foreclosure Fairness Act (July 22, 2011) and the Notice of Trustee's Sale had been issued after the Act, on November 8, 2011. The Court of Appeals confirmed that the ruling in *Watson* was only applicable to the facts of that "gap" foreclosure case because the Foreclosure Fairness Act changed the form of the NOD; therefore, a borrower with a foreclosure sale after the effectiveness of the Act should have the benefits of the additional language (including the invitation to mediation) in the new NOD. Furthermore, those additional protections in the NOD only apply for "owner-occupied residential real property." The Leahys claimed that they lived in the property from February 2010 until May 2010 while they were renovating it to become a rental property, which was during the window of time that the Notice of Default was issued. However, the court did not find that the Leahys had provided enough evidence to the trial court to support their claim and, therefore, the *Watson* case was not analogous.

Actual Possession – What does it really mean? *(Selkowitz v. Litton Loan Servicing)*
Washington's Nonjudicial Foreclosure statute requires the trustee to have proof that the beneficiary is the owner before it can foreclose a deed of trust. One way in which the trustee satisfies this burden is by having a declaration from the beneficiary that it is the "actual holder" of the note. The foreclosure statute does not define the phrase "actual holder," nor does it define "owner." The state Supreme Court, in *Brown v. Dept. of Commerce,* 2015 Wash. LEXIS 1191 (Oct. 22, 2015), held that the statute is superfluous, inharmonious, and ambiguous, but that the legislature intended to track Article 3 of the UCC in finding that the beneficiary is the holder. [See USFN e-Update Nov./Dec. 2015 Edition, Washington article, "Note Holder can Modify and Enforce the Note," for a summary of the *Brown* opinion. That article may be viewed in USFN's online Article Library at www.usfn.org.]

Taking it a step further, the Division One Court of Appeals in *Selkowitz v. Litton Loan Servicing,* 2015 Wash. App. LEXIS 2882 (Nov. 23, 2015), analyzed a situation where beneficiary Litton had constructive possession of the note at the time of the execution of the beneficiary declaration. The note was being held by a document custodian and despite the plaintiff-borrower's claim that constructive possession is not sufficient, the *Selkowitz* court cites to the *Bain* and *Brown* opinions and finds that nothing in these prior cases suggests "that the insertion of the word 'actual' was intended to create a departure from the UCC's definition of 'holder.'" This ruling is pending a motion to publish. ■