COA Opinion: Mortgage Electronic Registration System may not foreclose by advertisement

22. April 2011 By Sarah Lindsey

In *Residential Funding Co v. Saurman*, the Michigan Court of Appeals held, in an opinion authored by Judge Shapiro, that Mortgage Electronic Registration System (MERS) did not have authority under MCL 600.3204(1)(d) to foreclose by advertisement because it did not own an interest in the indebtedness secured by the mortgage. Judge Wilder dissented, concluding that under the mortgage security instruments, MERS had a contractual interest in the indebtedness.

In these consolidated actions, lender Homecoming Financial LLC and defendants executed promissory notes and mortgages for home purchases. The mortgages named MERS as mortgagee and gave it the right to foreclose on the property in the event of default. Defendants defaulted on their respective notes. MERS began non-judicial foreclosures by advertisement as permitted under MCL 600.3201, et seq., purchased the property at the subsequent sheriff's sales and then quit-claimed the property to plaintiffs as respective successor lenders. When plaintiffs subsequently began eviction actions, defendants challenged the respective foreclosures as invalid, asserting, inter alia, that MERS did not have authority under MCL 600.3204(1)(d) to foreclose by advertisement because it did not fall within any of the three categories of mortgagees permitted to do so under that statute. The district courts concluded that MERS did have authority to foreclose by advertisement and their conclusions were affirmed by the respective circuit courts. In a split decision, the Court of Appeals reversed.

MERS was developed as a mechanism to provide for faster and lower cost buying and selling of mortgage debt. MERS allowed financial entities to buy and sell loans without having to record a mortgage transfer for each transaction because the named mortgagee, which was MERS, would not change. MERS was responsible for keeping track of which entity held a mortgage at any given time and, if MERS foreclosed on the property, MERS would quit claim the property to the lender that owned the loan at the time of the foreclosure.

The Court considered whether MERS as mortgagee, but not noteholder, could exercise its contractual right to foreclose by advertisement. Foreclosure by advertisement is governed by MCL 600.3204(1)(d), which provides, in pertinent part:

[A] party may foreclose a mortgage by advertisement if all of the following circumstances exist:

* * *

(d) The party foreclosing the mortgage is either the owner of the indebtedness or of an interest in the indebtedness secured by the mortgage or the servicing agent of the mortgage.

The sole issue addressed by both the majority and dissent was whether MERS was "the owner . . . of an interest in the indebtedness secured by the mortgage." MCL 600.3204(1)(d). The majority concluded that MERS was not an owner of an interest in the indebtedness. It reasoned that the note and the mortgage are two different legal transactions providing two different sets of rights. MERS, as mortgagee, only held an interest in the property as security for the note, not an interest in the note itself. In support of its interpretation of the phrase "the owner . . . of an interest in the indebtedness secured by the mortgage," the court opined that if MERS were permitted to foreclose on the properties, the borrowers obligated under the note could potentially be subject to double exposure for the debt. If MERS foreclosed on the property, that would not necessarily operate to extinguish the debt evidenced by the note. The Court pointed out that judicial foreclosure would ensure that the mortgagor would not be at risk for double exposure for the debt.

The majority also noted that the statute does not provide for foreclosure in the name of an agent or a nominee. It stated that "[i]f the Legislature intended to permit such actions, it could have easily included "agents or nominees of the noteholder" as parties that could foreclose by advertisement. The majority rejected plaintiffs' argument that the Legislature did not create three discrete categories of entities that could foreclose by advertisement but rather envisioned a continuum of entities. The majority stated that it could not rewrite the plain language of the statute, which does not provide for a "continuum."

In dissent, Judge Wilder read the statute more broadly and would have held that MERS was an owner of an interest in the indebtedness. He reasoned that MERS owned a contractual interest in the indebtedness because the lender Homecoming conveyed to MERS the right to act for the benefit of Homecoming, which is a greater interest than just an interest in the property as security for the note.