The Mortgage Crisis: It's Complicated!
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Mortgage rates, which rose precipitously during December, have fallen during January and while still above the record low during the week of November 11, 2010, thirty year rates and fifteen year rates continue to be remarkably favorable. Despite low interest rates and home prices which have fallen dramatically in the past four years, home buying activity has fallen substantially when compared to early 2010 when the First-Time Homebuyer Tax Credit remained in effect. Since the expiration of this stimulant, real estate activity has fallen markedly.

Not a single day goes by in which some article does not appear in our newspapers, on the internet or in other media regarding the foreclosure crisis. Foreclosure filings in the last quarter of 2010, according to RealtyTrac, were down 8% from the same period one year prior. That is no comfort when a reported 799,064 homes supposedly were the subject of foreclosure related filings, including default notices, foreclosure suits, auction notices and lender repossessions.

Are Foreclosure Filings Really Going Down?

Many individuals question whether the drop in the number of foreclosure filings in the fourth quarter of 2010 indicates that the economy is strengthening. Rather, many believe that the fall-off in activity has been a result of the following:

1. Legislation in various states making foreclosures more difficult;
2. Lawsuits by homeowners who have lost homes to banks which have been less than careful in the foreclosure process; and,
3. The moratorium in the Fall of 2010 by major lenders which went into effect while the lenders evaluated their internal procedures.

How Did We Get Here?

Anyone can provide a glib answer to the question of how these circumstances came about. They can simply say, "Follow the money." While greed and profit may be a component, the truth is that the real estate economy virtually sustained the overall economy during a major portion of the George W. Bush Presidency. In truth, the vast majority of Americans saw this period in real estate as positive because:

1. Real estate brokers flourished;
2. Title companies and all the ancillary services (home inspections, surveying, appraisals) flourished;
3. Mortgage lenders and mortgage brokers flourished;
4. Ancillary services expanded, new opportunities were created and new business models became possible; and,

5. The financial services industry found a new niche.

The result was a rapid increase in the price of homes, the ability to use the equity in one's home to buy luxuries that were not previously available, the bolstering of the home construction industry, furniture sales, home improvement supplies and numerous related activities creating economic expansion.

"Let's Point a Finger!"

Our culture has become one in which fingers are pointed and particular segments of the real estate industry are targeted for blame for the current collapse. Frankly, it is this author's opinion that finding someone to blame is certain to produce a repetition of these circumstances in the future. It is preferable to view it as a confluence of factors: everyone's innate desire for success, our love for seeing things "go up", along with the good feelings that go with partaking in a prosperous economy.

If we take a benign approach and not attack banks, brokers, mortgage originators, appraisers, title companies or investment bankers, it is far easier to analyze what aspects of the system are in need of improvement. What clearly has emerged over the past three years are the following:

1. Banks and consumers are better served when lenders maintain strict underwriting guidelines so that homebuyers are realistic about their ability to fund the purchase of a home whether or not good times are ahead.

2. Securitization of home loans is a vehicle for the creative generation of funds. It may also create a false sense of security for the purchasers of securitized mortgages. It also makes a simple process so complex that the lenders, the after-market buyers and the homebuyers are open to losses.

3. Real estate brokers, appraisers and title companies are all in need of establishing strict standards for their industries to ensure that consumers, lenders, after-market purchasers and others are not misled into engaging in transactions that are fundamentally flawed.

U.S. Bank National Association v. Ibanez

The January 7, 2011 decision rendered by the highest court in the State of Massachusetts (the Supreme Judicial Court) in the matter of *U.S. Bank National Association, trustee v. Antonio Ibanez (Oct. 7, 2010 – Jan. 7, 2011 No. SJC-10694)* recently made headlines when the court found that U.S. Bank, acting as a trustee, had improperly foreclosed on the property of Antonio Ibanez.

What is "Securitization"?

The court explained the concept of securitization in relation to the Ibanez mortgage. Ibanez borrowed $103,500.00 on December 1, 2005 to purchase property in Springfield, Massachusetts. He used a lender, Rose Mortgage, Inc., which duly recorded the mortgage following the closing. Rose Mortgage, Inc. then executed an assignment of the mortgage in "blank" (not specifying the name of the assignee). Many months later, the name of Option One Mortgage Corporation was inserted into the Assignment. Option One Mortgage Corporation then assigned the Ibanez mortgage to Lehman Brothers Bank, FSB which in turn assigned the mortgage to Lehman Brothers Holdings, Inc. Lehman Brothers Holdings, Inc. then assigned the mortgage to Structured Assets Securities Corporation. Structured Assets Securities Corporation then assembled a group of 1,220 mortgage loans and assigned them as a group to U.S. Bank, as trustee for the Structured Assets Securities Corporation, to create "Mortgage Pass-Through Certificates". Thus, the Ibanez mortgage was pulled into a trust and converted into a mortgage-backed security that could be bought and sold by investors. This total process is known as "securitization". The Mortgage Pass-Through Certificates created by Lehman Brothers Holdings, Inc. then became the subject of a private placement memorandum (a 273 page document) and the 1,220 mortgages were sold to a group of investors.

"Let's Find a Shortcut"

As a result of the pressures of the marketplace, the documentation regarding the assignments of the mortgages and their securitization were not handled carefully. Massachusetts is known as a "title theory" state. This is contrasted with New York State which is a "lien theory" state. In New York, because it is a lien theory state, a buyer holds the deed to property even though there is a mortgage on the property. The mortgage becomes a lien on the property but title remains with the purchaser. The lender's lien is removed only when all of the loan payments have been completed. In a lien theory state such as New York, although there are minor exceptions, lenders go through what is known as "judicial foreclosure", which is time consuming and must be handled methodically.

In Massachusetts, which is a title theory state, the lender becomes the actual owner of the property. Even though the buyer receives a deed to the property, when the buyer signs a mortgage, the borrower gives title back to the mortgage holder which holds the title as security until all of the payments are made. If the lender has actual title to the property, the lender can go through what is known as a "non-judicial foreclosure", which speeds up the foreclosure process. The lender need only show that it has good title to the property via a loan made to the owner or a valid assignment of a mortgage instrument and that proper publication was made regarding the foreclosure sale.

Court Finds Flaws

In this recent decision by the Massachusetts Supreme Judicial Court, the court indicated that the myriad assignments had not been adequately documented, that the foreclosing party, U.S. Bank, could not show that it had been given a valid assignment of the mortgage and when U.S. Bank sought to confirm that its foreclosure proceeding had been handled properly, the court found against the plaintiff, U.S. Bank, and concluded that U.S. Bank had failed to demonstrate that it was the holder of the mortgage at the time that the properties had been foreclosed and that the bank failed to demonstrate that it acquired fee simple title to these properties by "purchasing them at the foreclosure sale."

The court's decision involved not only U.S. Bank Corp., it also included Wells Fargo & Co. which was similarly seeking approval of a different foreclosure sale. The circumstances applicable to the Wells Fargo mortgage were essentially the same. Judge Gants writing for the Supreme Judicial Court stated:

> **"The legal principles and requirements we set forth are well established in our case law and our statutes. All that has changed is the plaintiffs' apparent failure to abide by those principles and requirements in the rush to sell mortgage-backed securities."**

Impact of the Massachusetts Decision

Consumer groups hailed this recent decision as one which is likely to make lenders cautious about proceeding to foreclosure. Rather, hope has been expressed in many quarters that banks will help homeowners who are struggling to keep their homes. The Realtor magazine - Daily News reported that:

> **"Experts say the court ruling was a positive for homeowners who are in the middle of the foreclosure process, those trying to work out modifications, refinance or do a short sale. They say that reaching a deal with lenders may become easier."**

Whether or not this is true will be determined in time. What is clear is that the complexities of the current environment weigh heavily on the market. Adding to these complications, the Obama administration has boosted funding to housing counseling agencies in order to help borrowers review loan documentation and avoid potential mortgage scams. On December 28, 2010, the Department of Housing and Urban Development Secretary Shaun Donovan announced that $73 million dollars in grants were provided to more than 500 national, regional and local organizations. The grants are aimed at helping people "become or remain homeowners or find rental housing."

Impact on the Real Estate Market

Distressed properties are now a major component of the real estate sales market. It is estimated that 25-33% of all sales involve a distressed property. Many believe that the current circumstances will prevail for many years to come. Short sales have become a major factor in the marketplace and involve complexities and the need for expertise. It is clear that until the marketplace turns upward and prices begin to rise above the levels of outstanding mortgages, short sales will continue to be a significant factor in the marketplace. Short sales should not be undertaken by anyone not trained in this segment of the market. It can be a long and frustrating process for buyers, sellers, brokers and everyone else involved. Many of these frustrations can be avoided by securing the necessary skills through education and certifications.

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