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FORECLOSURES AND THE FAILURE OF THE AMERICAN LAND TITLE RECORDING SYSTEM

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As the residential foreclosure crisis has developed, it has revealed a succession of systemic failures in the public and private sectors. Many scholars and policymakers have criticized the lack of transparency in the residential mortgage market and argued that the opacity of the system, along with the increasing complexity of transactions, contributed to the present financial crisis.¹ The recent announcement that major lenders were suspending pending foreclosure actions in the wake of questions about their documentation practices has focused attention on another opaque system that has failed to keep pace with the increasing complexity of the modern real estate industry: the American land title system. When the antiquated local title recording system failed to meet the needs of national lenders, they created a separate, private, limited access system to record and track residential mortgage assignments. The failures of that private, parallel system are playing an important role in millions of foreclosure cases. This Essay argues that the current foreclosure crisis should serve as a regrettable wake-up call for a long-overdue modernization of the American land title recording system.

In a number of recently reported cases, the foreclosing lender has had difficulty demonstrating to the court that it actually owns the mortgage that it is attempting to foreclose.² As any lawyer surely remembers from her 1L Property course, conveyances in real estate are normally recorded with a county recorder or register of deeds. To locate a mortgage and identify the

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1. See generally Christopher Peterson, Two Faces: Demystifying the Mortgage Electronic Registration System's Land Title Theory, 46 Real Prop. Tr. & Est. L.J. (forthcoming 2011), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1684729 (on file with the *Columbia Law Review*) (criticizing Mortgage Electronic Recording System's lack of transparency and describing its role in the financial crisis).

2. See, e.g., *U.S. Bank Nat'l Ass'n v. Ibanez*, No. SJ-10694, 2011 WL 38071, at *9 (Mass. Jan. 7, 2011) (affirming lower court ruling that securitization documents submitted by lender failed to demonstrate lender was mortgage holder); Emily Peck, Billion-Dollar Foreclosure Mess Took Root at \$75k House, Wall St. J. Real Est. Blog, Oct. 15, 2010, at <http://blogs.wsj.com/developments/2010/10/15/billion-dollar-foreclosure-mess-took-root-at-75k-house/> (on file with the *Columbia Law Review*) (describing lender who often cannot truthfully certify he possesses "true and accurate copy of the note or mortgage").

lender, one must simply look in the chain of title to the real property in question and find the name. Reality is not as straightforward.

In 1993, frustrated by the cost and time involved in complying with state laws regarding the recording of mortgage assignments, the residential mortgage industry created the Mortgage Electronic Recording System (MERS), a private, parallel recording system.³ The shortcomings in MERS that have emerged during the residential foreclosure crisis require us to address the underlying public land title recording system. This Essay describes how the public land title recording system is lacking and suggests how it can be improved to lessen the chance of such problems in the future.

Proposing modernization of the American system of land title recording is not a new idea. Professors Dale Whitman and Gerald Korngold, among other prominent property scholars, have made similar arguments in recent years. This Essay goes beyond those proposals and suggests a radical solution for three reasons: (1) computer technology, particularly with respect to organizing and searching data, has dramatically improved since Professors Whitman and Korngold respectively addressed the problem; (2) this Essay reimagines the indexing function through technology, rather than focusing on the digital submission of recorded documents; and (3) this Essay proposes the gradual federalization of land title records. Previous proposals to modernize the land title system recommended uniform acts to standardize local processes, but did not advocate for a national system because title recording is generally perceived as an essential function of local government.

I. GOALS AND OBJECTIVES OF THE RECORDING ACTS

The American land title system has straightforward goals. In conjunction with related state statutes, it is designed to establish a clear priority in title. To this end, the system is highly transparent. Everyone is on constructive notice of every recorded document, and has open access to those records. Additionally, to ease access, many urban and populous counties have placed recent records online to permit easier access.⁴ All land title offices allow searching on-site. The combination of transparency and clear priority in title creates security in land interests and strengthens the confidence of investors to purchase real estate or lend money secured by real estate. Owners and lenders would have far less incentive to invest in real estate if their respective priorities of title were murky.

II. HOW THE RECORDING ACTS WORK

Little has changed since colonial days in the process by which title is recorded.⁵ There are over 3,000 local recording systems where holders of an

3. Gerald Korngold, *Legal and Policy Choices in the Aftermath of the Subprime and Mortgage Financing Crisis*, 60 *S.C. L. Rev.* 727, 741–42 (2009).

4. See, e.g., Automated City Register Information System for New York City, NYC.gov, at <http://www.nyc.gov/html/dof/html/jump/acris.shtml> (last visited Mar. 6, 2011) (providing online, searchable property records for Manhattan, Queens, Bronx, and Brooklyn).

5. See Dale A. Whitman, *Digital Recording of Real Estate Conveyances*, 32 *J. Marshall L.*

interest in real estate can register that interest.⁶ For centuries, deeds, mortgages, easements, and leases were hand-transcribed into books. Indexes were created as finding guides to locate the transcriptions. Some counties used multiple index books—one for deeds, one for mortgages, and one for miscellaneous records. In most American recording offices, computers are now used to digitize new records and maintain the indexes, although some smaller and more rural counties continue to use physical books for indexing.⁷ Still, many counties that digitize their records and index on a computer maintain the fiction of a paper-based system by referring to the location of a document by “book” and “page” numbers.

There are two methods of indexing land title records: the tract index and the grantor/grantee index. The tract index uses a legal description of the relevant land as its organizing principal. The grantor/grantee index uses the names of the parties to a conveyance as its organizing principal. Indexes normally include the following fields of information: names of the parties, type of conveyance, recording date, short legal description, and reference to the location of the document.

III. SHORTCOMINGS OF THE PROCESS

The most significant problem in the recording process is the manner in which documents are indexed. America is wedded to crude grantor/grantee and tract indexes because they were the height of technological innovation when first implemented in the Massachusetts Bay Colony in 1640. Even progressive jurisdictions utilizing electronic recording have simply transferred this paper-based indexing system into a simple database akin to a Microsoft Excel spreadsheet.⁸

Grantor/grantee indexes are difficult to use and prone to problems.⁹ For instance, a chain of title may only be fully reconstructed if the index is accurate. Even a small inaccuracy such as a misspelled name or variation on a name in an index can make the instrument impossible to locate. For example the surname “de la Hoya” may be indexed as de la Hoya, Hoya, or la Hoya.¹⁰ Even more problems exist if an errant recorder copies the name as delahoya. If a woman acquires property in her maiden name, then sells the property in her

Rev. 227, 227 (1999) (“During the past 350 years, little has changed in the way real estate conveyances are recorded in America.”).

6. George Lefcoe, *Real Estate Transactions, Finance, and Development* 248 (6th ed. 2009).

7. Tanya D. Marsh, *The Limits of Constructive Notice: A Call to Reform Indiana’s Recording Statutes*, *Res Gestae*, Oct. 2002 at 20.

8. For example, the Iowa Electronic Recording System, which is appropriately lauded for its progressive approach in several respects, simply transfers the paper-based indexing regime to electronic media with the addition of a parcel identifier number. See Iowa Land Records, at <https://iowalandrecords.org> (last visited Mar. 6, 2011); see also Press Release, Simplifile & Iowa Land Records, Simplifile and Iowa County Recorders Integrate Systems to Enable Electronic Recording (June 1, 2007), available at <http://www.simplifile.com/eRecording/pdfs/Iowa%20CLRIS%20PR%20v053007.pdf> (on file with the *Columbia Law Review*).

9. Lefcoe, *supra* note 6, at 250 (citing Whitman, *supra* note 5, at 230).

10. *Id.* at 248.

married name, the index will only connect the two deeds if both names are listed on the second deed and appropriately recorded in the index. Inevitably, many mistakes have occurred and continue to occur because of the human role in translating documents into an index.

These mistakes have consequences. Courts have held that a mis-indexed conveyance is not binding on third parties.¹¹ For the beneficiary of the mis-indexed interest, a single mistake can have catastrophic consequences. The current indexing system has an unacceptably high possibility of such errors for two reasons. First, local recorders are immune from damages caused by mis-indexing.¹² Second, the indexing systems in place are arranged around a few key pieces of data: the names of grantor and grantee or the tract description. A typo or unexpected variance in a single data field can put the conveyance outside of the chain of title for a parcel.¹³

Further, this static indexing system cannot account for changing legal descriptions of property parcels. Older systems use traditional metes and bounds descriptions to identify parcels of land. Newer systems assign a parcel identification number. Both of these approaches assume that land therein described will remain static. But land changes; it is split and combined. Roads are vacated. Rivers move. Condominiums are established and buildings are demolished. By assigning a single identifier to a parcel of land, we assume a false stability and make it more difficult to track the chain of title on a parcel that undergoes change.

Beyond the archaic nature of the system, the dispersion of the recording function into thousands of local offices means that there is no standard system for recording and indexing. Recording laws differ from state to state, and indexing practices can differ over time in the same county.

These obvious problems with the current system, particularly the cost of understanding and complying with the rules of over 3,000 separate offices, led major players in the residential housing lending process to form a private, parallel recording process.

The Mortgage Electronic Registration Systems, Inc. (MERS) was created by the Mortgage Bankers Association, Fannie Mae, Freddie Mac, the Government National Mortgage Association, the Federal Housing Administration, and the Department of Veterans Affairs in 1993 to provide “electronic processing and tracking of [mortgage] ownership and transfers.”¹⁴ MERS was established in part to facilitate the bundling of debt and sale of

11. See, e.g., *Chem. Bank v. Title Servs., Inc.*, 708 F. Supp. 245, 249 (D. Minn. 1989) (“[T]he burden is properly on the creditor to make a proper filing and the creditor bears the risk of misfiling. . . . Accordingly, this court declines to impose a duty on searchers to search under possible misspellings of a debtor’s name.”).

12. See, e.g., *In re R.A. Beck Builders, Inc.*, 66 B.R. 666, 668 (Bankr. W.D. Pa. 1986) (noting that a county clerk cannot be liable for mis-indexing under Pennsylvania law).

13. Emily Bayer-Pacht, *The Computerization of Land Records: How Advances in Recording Systems Affect the Rationale Behind Some Existing Chain of Title Doctrine*, 32 *Cardozo L. Rev.* 337, 346–57 (2010) (discussing electronic indexing systems and impact on chain of title doctrine).

14. Korngold, *supra* note 3, at 741–42 (citing *MERSCORP, Inc. v. Romaine*, 861 N.E.2d 81, 83 n.2 (N.Y. 2006)).

mortgage portfolios. When a loan registered with MERS is made, the mortgage names MERS in conflicting terms. The Fannie Mae/Freddie Mac approved mortgage form contains the following provision: “‘MERS’ is Mortgage Electronic Registration Systems, Inc. MERS is a separate corporation that is acting solely as a nominee for Lender and Lender’s successors and assigns. MERS is the beneficiary under this Security Instrument.”¹⁵

When the mortgage or portfolio is subsequently sold, the conveyance information is registered in MERS, but no assignment is recorded. For example, my own residential mortgage names MERS as the lender’s nominee. I write my monthly mortgage check to a particular financial services company, but I do not know if that company actually owns my mortgage, or is servicing it on behalf of another lender, or a trust of investors. If I were ever so unlucky as to receive a foreclosure notice, I could not consult the county records to verify if the entity threatening foreclosure actually owns the debt on my home. That information is held only in MERS. Initially, only paid customers of MERS were able to access the information it stores. Perhaps in response to criticism of this lack of transparency, MERS has recently created a system, called MERS Servicer Identification System,¹⁶ which is designed to permit homeowners to discover the identity of their servicer and the investor that owns their loan. Although the new service is a step forward in promoting transparency, it remains problematic. When I searched the system by the address of my home, the system was unable to find a record of my mortgage.

MERS has been a controversial innovation. Some observers have lauded its national scale and electronic indexing functions. Although many local recorders have viewed MERS with suspicion,¹⁷ a number of state courts have expressly permitted the recording of mortgages with MERS.¹⁸ Some courts and other observers, however, are concerned that the legal fiction of MERS’s status as the “mortgagee of record,” when it holds no beneficial interest in the property, is irreconcilable with mortgage law.¹⁹

15. Freddie Mac, Federal Home Loan Mortgage Corporation Authorized Changes for MERS 3 (2010), available at <http://www.freddiemac.com/uniform/unifchanges.html> (on file with the *Columbia Law Review*).

16. MERS Servicer Identification System, at <https://www.mers-servicerid.org/sis/> (last visited Mar. 6, 2011).

17. See, e.g., *MERSCORP*, 861 N.E.2d at 83–85 (holding that the Suffolk County Clerk could not refuse to record and index mortgages naming MERS as the lender’s nominee or mortgagee of record).

18. See, e.g., *id.* at 84–85 (“[T]he County Clerk is required to accept the MERS assignments and discharges of mortgages for recording.”).

19. See, e.g., *Landmark Nat’l Bank v. Kesler*, 216 P.3d 158, 166–67 (Kan. 2009) (describing relationship between MERS and financial institution that putatively purchased the mortgage as “more akin to that of a straw man than to a party possessing all the rights given a buyer”); *Mortg. Elec. Registration Sys., Inc. v. Saunders*, 2 A.3d 289, 295 (Me. 2010) (“As discussed above, MERS’s only right is the right to record the mortgage. Its designation as the ‘mortgagee of record’ in the document does not change or expand that right; and having only that right, MERS does not qualify as a mortgagee pursuant to our foreclosure statute”); Beyond the scope of this article is a discussion of whether MERS has standing, as the “mortgagee of record,” to file a foreclosure action on behalf of the beneficial owner of the debt. For a thorough discussion of these issues, see Christopher L. Peterson, *Foreclosure, Subprime Mortgage*

The residential foreclosure crisis has brought MERS's flaws into clearer view. The inherent opaqueness of MERS has apparently hidden from public view some rather shoddy recordkeeping practices on the part of the lenders. In the fall of 2010, several major residential lenders implemented self-imposed foreclosure moratoriums due to systemic problems in proving ownership of the relevant mortgages.²⁰ If lenders had complied with the public land title system, a string of mortgage assignments would have easily allowed them to establish standing to file a foreclosure action.²¹

IV. A BETTER SOLUTION

The banks invented MERS because the land title system, developed in a far different time and place, failed to meet the needs of the modern real estate industry. But a private, opaque MERS-like system is not the answer. Instead, the federal government should implement a solution that replaces both the existing local land title system and MERS.

An ideal system should be organized around some clear principles. It should be transparent. It should be easy to search, through dynamic, robust indexing, and easy to access, preferably through the Internet. Documents in PDF form should be downloadable. Electronic filing, which has been proposed by several scholars and implemented in limited ways, should be facilitated. There should be uniformity and consistency in the rules governing the form and substance of documents eligible for recording. The system should be public. Establishing and protecting a clear registry of property interests is and should continue to be an essential function of government.

An ideal system will deal with the fundamental problem with the American land title system: It is a paper-based system that has been awkwardly translated to computers. Rather than continue to try to force a square peg to fit into a round hole, we should start from scratch. In many larger jurisdictions, land title records are digitized for archiving purposes. It is one small step to apply optical character recognition (OCR) software and make each recorded document completely searchable.²²

Indexes should not be limited to the names of the parties, the type of conveyance, a legal description, and the date of recording. Conveyance documents could be identified with limitless data, including cross-referencing to prior conveyances. Imagine integrating property tax records, subdivision plats, and recorded documents with a dynamic map.²³ With a click, a person

Lending, and the Mortgage Electronic Registration System, 78 U. Cin. L. Rev. 1359, 1380–86 (2010).

20. J. Taylor Rushing, Foreclosure Moratorium Takes Center Stage in Battleground States, *The Hill*, Oct. 16, 2010, at <http://thehill.com/homenews/campaign/124533-foreclosure-moratorium-takes-center-stage-in-senate-battleground-states> (on file with the *Columbia Law Review*).

21. Lenders have also had difficulty locating original promissory notes. Since notes are not recorded, improvements to the land title system would not address that aspect of the problem.

22. See, e.g., Automated City Register Information System for New York City, *supra* note 4 (providing online, searchable property records for Manhattan, Queens, Bronx, and Brooklyn).

23. Many urban jurisdictions already have maps available online utilizing Geographical Information Systems (GIS) technology. Integrating that information with land title records would

could bring up all of the data in the records pertaining to a particular parcel. In such a system, it would be easier for a lawyer or title insurer to sort through the documents and determine which are properly in the chain of title and thus binding on the property.

Technologically, this type of system would be easy to implement within the existing structure of local offices.²⁴ However, if recorded documents were digitized and indexed online, the rationale for a local system would significantly diminish. Although precedent strongly dictates that land title records be kept at the local level,²⁵ the original rationale for a local system has disappeared. It is no longer important that the recording office be located within one day's horse ride of the county limits.

A single, national system is the most appropriate solution for the modern real estate industry. Politically, however, it would be extremely difficult to dismantle the local system. The American recording system is in the hands of thousands of elected officials, many of whom hold offices established in their state's constitution. Eliminating them, particularly in one fell swoop, would be nearly impossible.

Given these difficulties, I propose that we simply make the local recorders obsolete. I propose that the federal government create an alternative recording system that includes the features that I outline above. A uniform state law would allow a parcel of real property to permanently migrate out of the local recording system and into the new federal system. A memorandum of the switch would be recorded at the local office, giving notice to all to use the federal database for updated title information. At the time of transfer, I propose that an attorney or title company prepare an abstract of title that includes all conveyances and encumbrances in the chain of title during the relevant marketable title period. That abstract of title, along with certified copies of all documents named therein, would be added to the federal system. Searchers interested in historical documents could still find them at the local level, but new conveyances would need to be added to the federal system.

A compromise approach may seem more feasible, but would be a clear second-best solution. Such a compromise might be to centralize the land title system at the state level, much like the registration system used for Article 9 filings under the Uniform Commercial Code.²⁶ Iowa has taken a step towards such a state system. Although county recorders continue their traditional functions in Iowa, an electronic statewide index has been established and is

be a powerful improvement. See Jeremy Speich, *The Legal Implications of Geographical Information Systems (GIS)*, 11 *Alb. L.J. Sci. & Tech.* 359, 370 (2001) ("GIS is a key component to the improvement of the public recording system.").

24. See Dean Arthur Gaudio, *Electronic Real Estate Records: A Model for Action*, 24 *W. New Eng. L. Rev.* 271, 273–75 (2002) (describing success of the Uniform Electronic Transaction Act and proposing broader uniform real estate electronic recording act).

25. See Korngold, *supra* note 3, at 736 (describing failure of any state to adopt Uniform Land Transactions Act (ULTA), proposed by the National Conference of Commissioners on Uniform State Laws (NCCUSL) in 1975; or Uniform Land Security Interest Act (ULSIA), proposed by NCCUSL in 1985).

26. See, e.g., U.C.C. § 9-402 (2005) (outlining formal requisites of filing statement for secured transaction).

available on the Internet.²⁷ Combining the Iowa model with my prescription would be an improvement, but a costly and ultimately inefficient one. There are great economies of scale to be realized with consolidation of the recording and indexing functions. In addition, as the current economic situation reminds us, the modern real estate industry is no longer a local activity. Most Americans did not obtain a home loan from George Bailey, but from Bank of America. Recommending the federalization of what has long been regarded as a core function of local government will doubtless be controversial. But the recording of land title records is essentially a ministerial task that conveys little political power. I contend that the balance between local and federal governments would not be shaken by the national consolidation of the land title system.

Given the fundamental problems inherent in MERS, particularly its private, nontransparent nature, I propose that registering mortgages and permitting assignments through MERS be prohibited. If they were deprived of their private system, I suspect that lenders would prefer the new federal approach to the status quo. Lenders would likely eventually require the transfer of residential parcels into the new federal system as a condition of lending. Many property owners, particularly the owners of commercial real estate, would likely also prefer a single national system. Allowing a gradual transition to a national system would encompass the best aspects of the local recording system and MERS, while making a radical and absolutely necessary shift from a paper-based indexing paradigm to a robust and dynamic searching system.

I do not lightly suggest that we abandon 370 years of precedent. But the residential foreclosure crisis, and the role of MERS, demonstrates that the American land title system is broken. The time has come for a radical reinvention that meets the needs of the modern real estate industry.

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27. Iowa Land Records, *supra* note 8.