



MBA Fact Sheet

The Role of Electronic Mortgage Registrations

The Need for Electronic Registration

Recent events in the mortgage loan servicing industry have prompted questions about how mortgages are recorded and their ownership tracked. These questions are important for a number of reasons. In today's mortgage finance system, a loan is often sold one or more times after origination and then securitized as part of a pool of similar mortgages. Additionally, the overwhelming majority of mortgage loans are paid off through refinancing or sale of a property long before their terms (such as 15, 30 or 40 years) expire. These facts make tracking the servicer and ownership of every mortgage challenging and, at the same time, absolutely critical to the efficient operation of the mortgage market.

To understand the purpose of a registry of mortgage rights, it is important to understand the nature of mortgage loans. Mortgage loans are complex financial products that come with piles of paperwork (actual and electronic) at every step of the process – from borrower application to the ultimate marketing of a security backed by that loan. Two instruments are fundamental to virtually every mortgage loan today and rise above the rest in terms of legal importance – the promissory note and the security instrument, which is generally a mortgage or deed of trust. The security instrument establishes the note holder's right to the property, securing repayment of the borrower's promissory note upon the borrower's default.

The legal principle governing the right to receive payment under a mortgage note is that "possession" of the note determines ownership and the security instrument follows the note. The security instrument is recorded in the local (usually county) land records office to provide "public notice" of the mortgage lien.

The American process for allowing a borrower to possess real estate while paying the debt, and requiring the lender to record a notice of lien so that subsequent creditors and other interested parties can be aware of the lender's security interest in the real property, has been in place since the early 17th century. For hundreds of years, it worked pretty much the same way in counties across the country.

In more recent history, it also has been common practice to divide up the rights in a mortgage into "legal" rights and "equitable" or "beneficial" rights. Going back to the launch of FHA-insured mortgages in the 1930's, when a loan was made, the mortgage originator was identified in the public records as "mortgagee of record" on behalf of a life insurance company that would purchase the mortgage obligation. All rights to receive payment were sold to the insurance company which would become the equitable owner of the promissory note. To the world, the mortgage originator/servicer would be the mortgagee of record, but the entity would hold only "bare legal title" in order to service the mortgage on behalf of its investor. "Servicing" includes

collecting mortgage payments, remitting them to investors, and handling mortgage delinquencies and defaults on behalf of an investor. As the secondary mortgage market evolved, this model was adopted by Fannie Mae and Freddie Mac, Ginnie Mae, and private label securitizers.

Under this model, every time servicing obligations changed hands as the mortgage moved through the mortgage business chain, the new servicer was generally required by the investor to record the assignment of its bare legal title in the local land records office. The records also had to be updated and liens released, as they do still today, any time a mortgage was paid off through a refinance or sale of the property.

By the early 1990s, with homeownership continuing to grow and interest rates falling to new lows, it was apparent that the mortgage recordation system that had been in use for nearly 400 years could not keep up with the modern volume of residential real property finance transactions. In fact, the 1993 mortgage refinance boom, still one of the largest in American history, was hampered by a severe backlog of paperwork (which included the assignments between servicers) at land records offices in many areas of the country, often delaying lien releases and related home purchase and mortgage refinance transactions to the detriment of consumers trying to benefit from falling interest rates and compromising the chain of record title. Borrowers, lenders and government officials all became frustrated by this situation which was exacerbated by the growing volume of investor-required mortgage assignments.

The mortgage recordation backlog of the early 1990s was somewhat analogous to Wall Street's "paperwork crisis" of the late 1960s, where clerks were buried in so many paper stock certificates that they could not process them fast enough. To solve this crisis, Wall Street turned to technology and a system of book-entry accounting to track stock ownership. Mortgage companies, banks, investors and government officials saw the positive results of this evolution in the stock market and began to discuss how to apply a similar concept to tracking mortgage ownership rights, servicing rights and warehouse loans (short-term security interests in mortgage obligations prior to their sale into the secondary mortgage market). Out of these discussions was born an industry utility that came to be called MERS, or Mortgage Electronic Registration Systems, Inc.

MERS Today

Today, MERS is an integral part of modern mortgage finance. MERS has dramatically improved the quality and availability of information in the residential mortgage process since its operations began in 1997.

The MERS[®] System is a database of information provided by mortgage lenders, servicers and investors. It is owned and operated by MERSCORP, Inc., the parent company of Mortgage Electronic Registration Systems, Inc. Using a standard Mortgage Identification Number (MIN), the MERS[®] System tracks changes in holders of loan servicing rights, owners of the mortgage note and holders of warehouse loans.

On the majority of mortgage loans today, borrowers agree at settlement to allow Mortgage Electronic Registration Systems, Inc. to be the mortgagee of record – as "nominee" for the promissory note holder – as the note is sold, aggregated and securitized. The mortgage lien and its priority position are properly established in the county recorder's office, while the ownership of the note and other mortgage rights move through the modern system of banking and capital markets, all the time being tracked closely by the MERS[®] System.

Allowing Mortgage Electronic Registration Systems, Inc. to serve as the mortgagee of record has relieved the pressures on the public land records caused by repeated transfers of mortgage rights (such as servicing and ownership rights), and thereby helps protect the accuracy and integrity of the chain of title. MERS also maintains a centralized “mailroom” on behalf of its members to receive and disseminate legal notices it receives as mortgagee of record.

The MERS® System supports the mortgage securitization process by giving banks, brokers, loan originators, servicers, investors and regulators the ability to track key information on every mortgage loan registered on the MERS® System. Since its inception, over 3,000 such market participants have registered more than 65 million loans with on the MERS® System. Today, over half of all outstanding mortgages are registered on the MERS® System.

MERS is also useful to borrowers, both directly and indirectly. MERS, for the first time, created a way for borrowers to track the servicer (and sometimes the investor) for their loan. This service is free online at <http://www.mersinc.org/homeowners/> or by calling (888) 679-6377. Through the reduction of paperwork and other efficiencies, MERS has helped significantly reduce the costs of a mortgage which helps keep the mortgage market liquid and ultimately reduces costs to borrowers. In addition, MERS has decreased the time it takes to refinance a loan which can be a significant benefit to borrowers attempting to lower their interest rate or move from a variable interest rate loan to one with a fixed rate.

As the mortgagee of record, it is common for MERS to play a role in foreclosures. If Mortgage Electronic Registration Systems, Inc. is the mortgagee of record with the county land records, and the borrower is in default on the mortgage, foreclosure can be legally commenced either by Mortgage Electronic Registration Systems, Inc. on behalf of the note owner, or by servicer or other entity if the note owner instructs MERS to assign the mortgage to the servicer or other entity. The process varies in these two ways due to state laws and/or the preference of the servicer or investor. It is important to note that Mortgage Electronic Registration Systems, Inc. only initiates foreclosure when it has been instructed to do so by the owner of the mortgage and possesses the mortgage note.

For more information on MERS, go to www.mersinc.org.

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