Foreclosure Fraud in a Nutshell

and How Newt Gingrich Abetted the Theft of Average Joe's Home

by Bill Butler

Previously by Bill Butler: Attempted Murder of Capitalism

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The untold story in the foreclosure crisis unfolding across America is that, following a foreclosure perpetrated by one of the October 2008 Bailout Banks (e.g. Bank of America, Citibank, JPMorgan, Wells Fargo) Fannie Mae or Freddie Mac suddenly appear as the record owner of Average Joe's home. These federal government sponsored entities then go into local housing court and get a court order authorizing them to evict Joe. If Joe resists, these supposedly charitable institutions obtain a writ ordering the local sheriff to forcibly remove Joe from his home.

Newt Gingrich recently admitted to accepting $1.8 million from Freddie Mac ($25,0000 to $30,000 a month during one span of time) for advising this proto-fascist entity. Gingrich claims that he supports Fannie and Freddie because he believes the federal government "should have programs to help low income people acquire the ability to buy homes." But Fannie and Freddie don't do this and never have. When government "helps" someone by subsidizing the purchase of something (through easy credit or lower-than-market rates), it makes that something more expensive. Helping someone buy something that is overpriced because of your help is not help. Fannie/Freddie subsidies not only hurt the low income people they intend to help, they hurt everyone by subsidizing, and therefore distorting, the entire housing market. Fannie/Freddie's charity has now taken a dark turn. Like their Depression-era New Deal predecessor the Regional Agricultural Credit Corp., Fannie/Freddie are now repossessing homes at an increasing and alarming rate.

Mr. Gingrich either does not understand economics – government subsidies make things more expensive, not less expensive, and therefore hurt their intended beneficiaries – or he is a vain, selfish, and cynical man with no interest in actually helping his neighbor.

You decide.

THE OCTOBER 2008 BAILOUT PAID OFF THE HOLDERS OF MORTGAGE BACKED SECURITES AND DERIVATIVE INSUREDS

The facts indicate that the Federal Reserve "printed" at least 16 trillion dollars as part of the 2008 bailouts. The bigger questions, however, who got it, why and what did the Fed get in return? The Fed doesn't just print money. It prints money to buy stuff. Most often this is U.S. Treasuries. That changed in October of 2008. In and after October 2008 the Fed printed new money to buy mortgage-backed securities (MBS) that were defaulting at a rapid rate. Want proof? Here is a link to the Federal Reserve balance sheet which shows that the Fed is holding over a trillion dollars in mortgage backed securities that it began acquiring in 2008.

Why is the Federal Reserve holding all these MBS? Because when "the market" collapsed in September of 2008, what really collapsed is the Fannie/Freddie/Wall Street mortgage "daisy chain" securitization scheme. As increasing numbers of MBS went into default, the purchasers of derivatives (naked insurance contracts betting on MBS default) began filing claims against the insurance writers (e.g. AIG) demanding payment. This started in February 2007 when HSBC Bank announced billions in MBS losses, gained momentum in June of 2007 when Bear Stearns announced $3.8 billion in MBS exposure in just one Bear Stearns fund, and further momentum with the actual collapse of Bear Stears in July and August of 2007. By September of 2008, the Bear Stearns collapse proved to be the canary in the coal mine as the claims on off-balance sheet derivatives became the cascading cross defaults that Alan Greenspan warned could collapse the entire Western financial system.

Part of what happened in October 2008 is that the Federal Reserve paid AIG's and others' derivative obligations to the insureds (pension funds, hedge funds, major banks, foreign banks) who held the naked insurance contracts guaranteeing Average Joe's payments. To understand this, imagine that a cataclysmic event occurred in the U.S. that destroyed nearly every car in the U.S. and further that Allstate insured all of these cars. That is what happened to AIG. When the housing market collapsed and borrowers began defaulting on their securitized loans, AIG's derivative obligations exceeded its ability (or willingness) to pay. So the Fed stepped in as the insurer of last resort and bailed out AIG (and probably others). When an insurer pays on a personal property claim, it has "subrogation" rights. This means when it pays it has the right to demand possession of the personal property it insured or seek recovery from those responsible for the loss. In Allstate's case this is wrecked cars. In the case of AIG and the Fed, it is MBS. That is what the trillions of MBS on the Fed's balance sheet represent: wrecked cars that Fannie and Freddie are now liquidating for scrap value.

Thank you Mr. Gingrich. Great advice.

BUT FANNIE/FREDDIE WASN'T MY LENDER AND WASN'T MY MORTGAGEE, SO HOW CAN THEY TAKE MY HOUSE?

To understand how it came to be that the Fed has paid Average Joe's original actual lender (the MBS purchaser) and now Fannie and Freddie are trying to take Joe's home, you first have to understand some mortgage law and securitization basics.

The Difference Between Notes and Mortgages

When you close on the purchase of your home, you sign two important documents. You sign a promissory note that represents your legal obligation to pay. You sign ONE promissory note. You sign ONE promissory note because it is a negotiable instrument, payable "to the order of" the "lender" identified in the promissory note. If you signed two promissory notes on a $300,000 loan from Countrywide, you could end up paying Countrywide (or one of its successors) $600,000.

At closing you also sign a Mortgage (or a Deed of Trust in Deed of Trust States). You may sign more than one Mortgage. You may sign more than one Mortgage because it **does not represent a legal obligation to pay anything.** You could sign 50 Mortgages relating to your $300,000 Countrywide loan and it would not change your obligation. A Mortgage is a security instrument. It is security and security only. Without a promissory note, a mortgage is nothing. Nothing.

You "give" or "grant" a mortgage to your original lender as security for the promise to pay as represented by the promissory note. In real estate law parlance, you "give/grant" the "mortgage" to the "holder" of your "promissory note."

If you question my bona fides in commenting on the important distinction between notes and mortgages, I know what I am talking about. I tried and won perhaps the first securitized mortgage lawsuit ever in the country in *First National Bank of Elk River v. Independent Mortgage Services*, 1996 WL 229236 (Minn. Ct. App. No. DX-95-1919).

In FNBER v. IMS a mortgage assignee (IMS) claimed the ownership of two mortgages relating to loans (promissory notes) held by my client, the First National Bank of Elk River (FNBER). After a three-day trial where IMS was capably represented by a former partner of the international law firm Dorsey & Whitney, my client prevailed and the Court voided the recorded mortgage assignments to IMS. My client prevailed not because of my great skill but because it had actual, physical custody of the original promissory notes (payable to the order of my client) and had been "servicing" (receiving payments on) the loans for years notwithstanding the recorded assignment of mortgage. The facts at trial showed that IMS rejected the loans because they did not conform to their securitization parameters. In short, IMS, as the "record owner" of the mortgages without any provable connection to the underlying notes, had nothing. FNBER, on the other hand, had promissory notes payable to the order of FNBER but did not have "record title" to the mortgages. FNBER was the winner because its possession of and entitlement to enforce the notes made it the "legal owner" of the mortgages.

The lesson: if you have record title to a mortgage but cannot show that you have possession of and/or entitlement to enforce the promissory notes that the mortgage secures, you lose.

This is true for 62 million securitized loans.

Securitization – The Car That Doesn’t Go In Reverse

There is nothing per se illegitimate about securitization. The law has for a long time recognized the rights of a noteholder to sell off pro-rata interests in the note. So long as the noteholder remains the noteholder he has the right to exercise rights in a mortgage (take the house) when there is a default on the note. Securitization does not run afoul of traditional real estate and foreclosure law when the mortgage holder can prove his connection to the noteholder.

But modern securitization doesn’t work this way.

The "securitization" of a "mortgage loan" today involves multiple parties but the most important parties and documents necessary for evaluating whether a bank has a right to foreclose on a mortgage are:

(1) the Borrower (Average Joe);

(2) the Original Lender (Mike's Baitshop and Mortgages or Bailey Savings & Loan – whoever is across the closing table from Joe);

(3) the Original Mortgagee (could be Mike's B&M, but could be anyone, including Fannie's Creature From the Black Lagoon, the mortgagee "nominee" MERS);

(4) the "Servicer" of the loan as identified in the PSA (usually a Bank or anyone with "servicer" in its name, the entity to whom Joe makes his payments);

(5) the mortgage loan "pooling and servicing agreement" (PSA) and the PSA Trust created by the PSA;

(6) the "PSA Trust" is the "special purpose entity" created by the PSA. The PSA Trust is the heart of the PSA. It holds all securitized notes and mortgages and also sells MBS securities to investors; and

(7) the "Trustee" of the PSA Trust is the entity responsible for safekeeping of Joe's promissory note and mortgage and the issuer of MBS.

The PSA Servicer is essentially the Chief Operating Officer and driver of the PSA. Without the Servicer, the securitization car does not go. The Servicer is the entity to which Joe pays his "mortgage" (really his note, but you get it) every month. When Joe's loan gets "sold" multiple times, the loan is not actually being sold, the servicing rights are. The Servicer has no right, title or interest in either the promissory note or the mortgage. Any right that the Servicer has to receive money is derived from the PSA. The PSA, not Joe's Note or Joe's Mortgage, gives the Servicer the right to take droplets of cash out of Joe's monthly payments before distributing the remainder to MBS purchasers.

The PSA Trustee and the sanctity of the PSA Trust are vitally important to the validity of the PSA. The PSA promoters (the usual suspects, Goldman Sachs, Lehman Bros., Merrill, Deutchebank, Barclays, etc.) persuaded MBS purchasers to part with trillions of dollars based on the idea that they would ensure that Joe's Note would be properly endorsed by every person or entity that touched it after Joe signed it, that they would place Joe's Note and Joe's Mortgage in the vault-like PSA Trust and the note and mortgage would remain in the PSA Trust with a green-eyeshade, PSA Trustee diligently safekeeping them for 30 years. Further, the PSA promoters hired law firms to persuade the MBS purchasers that the PSA Trust, which is more than100 percent funded (that is, oversold) by the MBS purchasers, was the real owner of Joe's Note and Joe's Mortgage and that the PSA Trust, using other people's money, had purchased or soon would purchase thousands of similar notes and mortgages in a "true sale" in accordance with FASB 140.

The PSA does not distribute pool proceeds that can be tracked pro rata to identifiable loans. In this respect, in the wrong hands (e.g. Countrywide's Angelo Mozilo) PSAs have the potential to operate like a modern "daisy chain" fraud whereby the PSA oversells the loans in the PSA Trust, thus defrauding the MBS investors. The PSA organizers also do not inform Joe at the other end of the chain that they have sold his $300,000 loan for $600,000 and that the payout to the MBS purchasers (and other derivative side-bettors) when Joe defaults is potentially multiples of $300,000.

The PSA organizers can cover the PSA's obligations to MBS purchasers through derivatives. Derivatives are like homeowners' fire insurance that anyone can buy. If everyone in the world can bet that Joe's home is going to burn down and has no interest in preventing it, odds are that Joe's home will burn down. This is part of the reason Warren Buffet called derivatives a "financial weapon of mass destruction." They are an off-balance sheet fiat money multiplier (the Fed stopped reporting the explosive expansion of M3 in 2006 most likely because of derivatives and mortgage loan securitization fraud), and create incentive for fraud. On the other end of the chain, Joe has no idea that the "Lender" across the table from him has no skin in the game and is more than likely receiving a commission for dragging Joe to the table.

A serious problem with modern securitization is that it destroys "privity." Privity of contract is the traditional notion that there are two parties to a contract and that only a party to the contract can enforce or renegotiate that contract. Put simply, if A and B have a contract, C cannot enforce B's rights against A (unless A expressly agrees or C otherwise shows a lawful agency relationship with B). The frustration for Joe is that he cannot find the other party to his transaction. When Joe talks to his "bank" (really his Servicer) and tries to renegotiate his loan, his bank tells him that a mysterious "investor" will not approve. He can't do this because they don't exist, have been paid or don't have the authority to negotiate Joe's loan.

Joe's ultimate "investor" is the Fed, as evidenced by the trillion of MBSs on its balance sheet. Although Fannie/Freddie purportedly now "own" 80 percent of all U.S. "mortgage loans," Fannie/Freddie are really just the Fed's repo agents. Joe has no privity relationship with Fannie/Freddie. Fannie, Freddie and the Fed know this. So they are using the Bailout Banks to frontrun the process – the Bailout Bank (who also have no cognizable connection to the note and therefore no privity relationship with Joe) conducts a fraudulent foreclosure by creating a "record title" right to foreclose and, when the fraudulent process is over, hands the bag of stolen loot (Joe's home) to Fannie and Freddie.

Record Title and Legal Title

Virtually all 62 million securitized notes define the "Noteholder" as "anyone who takes this Note by transfer **<u>and</u> who is entitled to receive payment under this Note…**" Very few of the holders of securitized mortgages can establish that they both hold (have physical possession of) the note AND are entitled to receive payments on the notes. For whatever reason, if a Bailout Bank has possession of an original note, it is usually endorsed payable to the order of some other (often bankrupt) entity.

If you are a Bailout Bank and you have physical possession of an original securitized note, proving that you are "entitled to receive payment" on the note is nearly impossible. First, you have to explain how you obtained the note when it should be in the hands of a PSA Trustee and it is not endorsed by the PSA Trustee. Second, even if you can show how you obtained the note, explaining why you are entitled to receive payments when you paid nothing for it and when the Fed may have satisfied your original creditors is a very difficult proposition. Third, because a mortgage is security for payments due to the noteholder **and only the noteholder**, if you cannot establish legal right to receive payments on the note but have a recorded mortgage all you have is "record" title to the mortgage. You have the "power" to foreclose (because courts trust recorded documents) but not necessarily the legal "right" to foreclose. Think FNBER v. IMS.

The "robosigner" controversy, reported by 60 Minutes months ago, is a symptom of the banks' problem with "legal title" versus "record title." The 60 Minutes reports shows that Bailout Banks are hiring 16 year old, independent contractors from Backwater, Georgia to pose as vice presidents and sign mortgage assignments which they "record" with local county recorders. This is effective in establishing the Bailout Banks' "record title" to the "mortgage." Unlike real bank vice presidents subject to Sarbanes-Oxley, Backwater 16-year olds have no reason to ask: "Where is the note?"; "Is my bank the noteholder?"; or "Is my Bank entitled to receive payments on the note?"

The Federal Office of the Comptroller of the Currency and the Office of Thrift Supervision agree with this analysis. In April of 2011 the OCC and OTS reprimanded the Bailout Banks for fraudulently foreclosing on millions of Average Joe's:

…without always ensuring that the either the promissory note or the mortgage document were properly endorsed or assigned and, if necessary, in the possession of the appropriate party at the appropriate time…

The OCC and OTS further found that the Bailout Banks "failed to sufficiently oversee outside counsel and other third-party providers handling foreclosure-related services."

Finally, Bailout Banks consented to the OCC and OTS spanking by admitting that they have engaged in "unsafe and unsound banking practices."

In these "Order and Consent Decrees," the OCC and the OTS reprimanded all of the usual suspects: Bank of America, Citibank, HSBC, JPMorgan Chase, MetLife, MERSCorp, PNC Bank, US Bank, Wells Fargo, Aurora Bank, Everbank, OneWest Bank, IMB HoldCo LLC, and Sovereign Bank.

Although the OCC and OTS Orders are essentially wrist slaps for what is a massive fraud, these orders at least expose some truth. In response to the OCC Order, the Fannie/Freddie-created Mortgage Electronic Registration Systems (MERS), changed its rules (see Rule 8) to demand that foreclosing lawyers identify the "noteowner" prior to initiating foreclosure proceedings.

NEWT'S FANNIE/FREDDIE ENDGAME: PLANTATION USA

Those of us fighting the banks began to see a disturbing trend starting about a year ago. Fannie and Freddie began showing up claiming title and seeking to evict homeowners from their homes.

The process works like this, using Bank of America as an example. Average Joe had a securitized loan with Countrywide. Countrywide, which might as well have been run by the Gambino family with expertise in "daisy chain" fraud, never followed the PSA, did not care for the original notes and almost never deposited the original notes in the PSA Trust. Countrywide goes belly up. Bank of America (BOA) takes over Countrywide in perhaps the worst deal in the history of corporate America, acquiring more liabilities than assets. Bank of America realizes that it has acquired a big bag of dung (no notes = no mortgages = big problem) and so sets up an entity called "BAC Home Loans LLP" whose general partner is another BOA entity.

The purpose of these BOA entities is to execute the liquidation the Countrywide portfolio as quickly as possible and, at the same time, isolate the liability to two small BOA subsidiaries. BOA uses BAC Home Loans LLP to conduct the foreclosure on Joe’s home. BAC Home Loans LLP feeds local foreclosure lawyers phony, robosigned documents that establish an "of record" transfer of the Countrywide mortgage to BAC Home Loans LLP. BAC Home Loans LLP, "purchases" Joe’s home at a Sheriff’s sale by bidding Joe’s debt owed to Countrywide. BAC Home Loans LLP does not have and cannot prove any connection to Joe’s note so BAC Home Loans LLP quickly deeds Joe’s property to Fannie and Freddie.

When it is time to kick Joe out of his home, Fannie Mae shows up in the eviction action. When compelled to show its cards, Fannie will claim title to Joe’s house via a "quit claim deed" or an assignment of the Sheriff’s Certificate of sale. Adding insult to injury, while Joe may have spent years trying to get BOA to "modify" his loan, and may have begged BOA for the right to pay BOA $1000 a month if only BOA will stop the foreclosure, Fannie now claims that BOA deeded Joe’s property to Fannie for nothing. That right, nothing. All county recorders require that a real estate purchaser claim how much they paid for the property to determine the tax value. Fannie claims on these recorded documents that it paid nothing for Joe’s home and, further, falsely claims that it is exempt because it is a US government agency. It isn’t. It is a government sponsored entity that is currently in conservatorship and run by the US government.

Great advice Newt.

CONCLUSION

It is apparent that the US government is so broke that it will do anything to pay its bills, including stealing Average Joe’s home.

That’s change that both Barack Obama and Newt Gingrich can believe in.

APPENDIX

More and more courts are agreeing that the banks "inside" the PSA do not have legal standing (they have no skin in the game and so cannot show the necessary "injury in fact"), are not "real parties in interest" (they cannot show that they followed the terms of the PSA or are otherwise "entitled to enforce" the note) and that there are real questions of whether any securitized mortgage can ever be properly perfected.

The banks' weakness is exposed most often in bankruptcy courts because it is there that they have to show their cards and explain how they claim a legal right, rather than the "of record" right, to foreclose the mortgage. More and more courts are recognizing that, without proof of ownership of the underlying note, holding a mortgage means nothing.

The most recent crack in the Banks's position is evidenced by the federal Eight Circuit Court of Appeals' decision in *In Re Banks*, No. 11-6025 (8th Cir., Sept. 13, 2011). In *Banks*, a bank attempted to execute a foreclosure within a bankruptcy case. The bank had a note payable to the order of another entity; that is, the foreclosing bank was "Bank C" but had a note payable to the order of "Bank B" and endorsed in blank by Bank B. The bank, Bank C, alleged that, because the note was endorsed in blank and "without recourse," that it had the right to foreclose. The Court held that this was insufficient to show a sufficient chain of title to the note, reversed the lower court's decision and remanded for findings regarding when and how Bank C acquired the note.

See also, *In Re Aagard*, No. 810-77338-reg (Bankr. E.D.N.Y., Feb. 10, 2011) (Judge Grossman slams MERS as lacking standing, working as both principal and agent in same transaction, and exposes MERS' alleged principal US Bank as unable to produce or provide evidence that it is in fact the holder of the note); *In Re Vargas*, No. 08-17036SB (Bankr. C.D. Cal., Sept. 30, 2008) (Judge Bufford correctly applied rules of evidence and held that MERS could not establish right to possession of the 83-year old Mr. Vargas' home through the testimony of a low-level employee who had no foundation to testify about the legal title to the original note); *In Re Walker*, Bankr. E.D. Cal. No. 10-21656-E-11 (May 20, 2010) (holding that neither MERS nor its alleged principal could show that they were "real parties in interest" because neither could provide any evidence of the whereabouts of, much less legal title to, the original note); *Landmark v.Kesler*, 216 P.2d 158 (Kan. 2009) (in this case the Kansas Supreme Court provides the most cogent state court analysis of the problem created by securitization – the "splitting" of the note and the mortgage and the real party in interest and standing problems that the holder of the mortgage has when it cannot also show that it has clean and clear legal title to the note); *U.S. Bank Nat'l Ass'n v. Ibanez*, 941 NE 40 (Mass. 2011), (the Massachusetts Supreme Court denied two banks' attempts to "quiet title" following foreclosure because the banks' proffered evidence did not show ownership of the mortgages – or for that matter, the notes – prior to the Sheriff's sale); and *Jackson v. MERS*, 770 N.W.2d 489 (Minn. 2009) (this federal-gun-to-the-head – certified question from federal court asking for state court blessing of its already decided ruling – to the Minnesota Supreme Court is most notable for the courageous dissent of NFL Hall of Fame player and only popularly elected Justice Alan Page who opined that MERS should pound sand and obey state recording standards).