ABI 18TH ANNUAL SOUTHWEST BANKRUPTCY CONFERENCE
Four Seasons Resort
Las Vegas, NV
September 23-25, 2010

RESOLVED: SERVICERS LACK STANDING TO PROSECUTE MOTIONS FOR RELIEF FROM STAY ON BEHALF OF UNNAMED BENEFICIARIES

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These materials summarize several prominent decisions by bankruptcy courts faced with deciding whether to grant automatic stay relief for purported lenders, servicers and/or their agents to foreclose on property. These cases address the constitutional standing and real party in interest status of parties to foreclose where they cannot show they hold the past due note or that they are entitled to enforce it.

INTRODUCTION

In the past decade, electronic information and data transmission have increased the speed at which we do business. These seemingly efficient tools have made it easier for banks to transfer funds and buy and sell notes without leaving a paper trail. However, now that the real estate bubble has burst, courts are demanding to see the paper trail for promissory notes before allowing lenders to foreclose on real property. As required by the Constitution, courts must confirm that a lender actually has standing and will benefit from the court granting relief from an automatic stay before the court can do so. Below is a brief description of the concepts related to standing and real parties in interest, followed by a summary of several different cases addressing these issues.

DISCUSSION

In the cases below, the courts discuss whether the party seeking relief from the automatic stay has standing to bring the motion and/or is the real party in interest. Many courts use the terms of standing and real party in interest interchangeably because the two concepts are closely related, but they do have distinct requirements. Standing has both constitutional and prudential (*i.e.* self-imposed) requirements. The real party in interest question is really the prudential component of the overall standing analysis, while injury-in-fact is a constitutional requirement. Both requirements must be met before a court can grant

relief from the automatic stay. In addition, a party also has standing to seek relief if it has the authority to act on behalf of an entity that has standing. Therefore, a nominee or agent will have to prove both (1) that it is an agent with the authority to act on behalf of the principal and (2) that the principal has both constitutional standing and prudential standing. However, even if a party has standing, the agent must prosecute the action in the name of the real party in interest and not in its own name.

The standing requirement is "an essential and unchanging part of the case-or-controversy requirement of Article III." *Lujan v. Defenders of Wildlife*, 504 US 555, 560 (1992). This constitutional doctrine requires that a claimant must present an actual or imminent injury that is fairly traceable to the defendant's conduct and redressable by a favorable ruling. *Davis v. Fed. Election Comm'n*, 128 S.Ct. 2759 (2008). The standing question is a threshold issue, required before a court may entertain a suit. *Warth v. Seldin*, 422 U.S. 490, 495 (1975). Thus, if a lender cannot prove standing, the court has no authority to hear its motion for relief from stay and it must dismiss the motion.

Prudential requirements also require that a party bringing a motion be the real party in interest. Rule 17 of the Federal Rules of Civil Procedure ("FRCP") requires "[a]n action must be prosecuted in the name of the real party in interest." Fed. R. Civ. P. 17. The purpose is to ensure the party bringing forth the action is the party who "possesses the substantive right being asserted under the applicable law." 6A Wright, Miller & Kane, *Federal Practice and Procedure* § 1541 (Westlaw current through 2009 update). This reflects the fact that the federal judiciary also adheres to certain prudential principles concerning standing. *Bennett v. Spear*, 520 U.S. 154, 162 (1997). The real party in interest inquiry is one of the prudential considerations the judiciary self-imposes to limit the role of courts in democratic society. *See,*

e.g., In re Village Rathskeller, 147 B.R. 665, 668 (Bankr. S.D.N.Y. 1992). Because Rule 17 applies in adversarial bankruptcy proceedings, parties must adhere to Rule 17 in order to seek relief from automatic stay. Rules 9014 and 7017, Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"); *In re Hwang*, 396 B.R. 757, 766 (Bankr. C.D. Cal. 2008).

The cases in this discussion illustrate potential standing and real party in interest issues arising in bankruptcy proceedings. While the Mortgage Electronic Registration Systems ("MERS") promised to streamline mortgage transactions and cut costs, this service often results in a series of unrecorded transfers or transfers to parties outside the servicer's system that can complicate knowing how a note traveled through the system and whether a party really has standing to seek foreclosure. The cases below demonstrate how some creditors and servicers failed to show they had standing or were, or were acting on behalf of, the real party in interest.

In re Hwang

The Bankruptcy Court for the Central District of California reconsidered its denial of IndyMac Federal Bank's ("IndyMac Bank") motion for relief from automatic stay. *Hwang*, 396 B.R. at 760. In this case, IndyMac transferred ownership of the note to an unknown party, but never transferred possession of the note. *Id.* The court found that, despite IndyMac Bank being entitled to enforce the note against the debtors, it was not the real party in interest because it was not ultimately entitled to the payments made on the note, so the court affirmed its denial of IndyMac Bank's motion for relief from automatic stay. *Id.* at 766-67.

The original payee and beneficiary of the deed was Mortgageit, Inc. ("Mortgageit"). *Id.* However, Mortgageit later transferred it to IndyMac Bank. *Id.* at 761. Mortgageit was a MERS member, but MERS lost its rights when the deed passed to IndyMac Bank. *Id.*

IndyMac Bank later sold the note to "unidentified 'investors' through Freddie Mac" while retaining physical possession of the note. *Id.* IndyMac Bank argued it was the authorized servicing agent for the new owner. *Id.* at 761-62. However, the court rejected this argument since IndyMac Bank admitted it did not know who the owner was and submitted no evidence of any such agreement. *Id.* However, the court found that IndyMac Bank was entitled to enforce the promissory note since it is a negotiable instrument, and under California law, the holder of a negotiable instrument has the right to enforce it. *Id.* at 762-63. For any instrument payable to a particular person, the holder is required to prove both (1) that it is in possession of the instrument and (2) that the instrument is payable to that person. *Id.* Here, IndyMac Bank can enforce the note because it has possession of the note which is payable to IndyMac Bank. *Id.* Since IndyMac Bank never delivered the note to the new owner, the right to enforce the note never passed and IndyMac Bank remains the holder of the note, retaining the right to enforce it. *Id.* at 763-65.

However, to prosecute the action in its own name, IndyMac Bank also must be the real party in interest. *Id.* at 766. The court found that a party may have constitutional standing, but still not be the real party in interest (*i.e.,* have prudential standing) if the substantive right belongs to someone else. *Id.* at 767-68. In this case, even though IndyMac Bank was entitled to demand and receive payment from debtors, the payments actually belonged to the new owner, not IndyMac Bank. *Id.* at 764-65.

Even if IndyMac Bank proved it was the servicing agent for the owner of the note, it must bring the action in the real party in interest's name rather than its own name, or join that party to the action to satisfy FRCP 19. *Id.* at 770-71. The purpose of FRCP 19 is to join "all persons whose joinder would be desirable for a just adjudication of the matter." *Id.* In this

case, joinder is required because "as a practical matter [failure to join will] impair . . . the person's ability to protect the interest." *Id.* at 771. Here, adjudicating the motion without joining the owner jeopardizes the owner's ability to protect its interest. *Id.* Since the court gave IndyMac Bank more than two months to join the new owner, but IndyMac failed to do so, the court denied the motion for relief from automatic stay. *Id.* at 772.

In re Hayes

In *Hayes,* the court noted that "mortgage servicers are parties in interest with standing by virtue of their pecuniary interest in collecting payments under the terms of the notes and mortgages they service." *In re Hayes,* 393 B.R. 259, 267 (Bankr. D. Mass. 2008) (*citing In re Woodberry,* 383 B.R. 373, 379 (Bankr. D.S.C. 2008); and *In re Conde-Dedonato,* 391 B.R. 247 (Bankr. E.D.N.Y. 2008)). However, Deutsche Bank National Trust Company, in its capacity as Trustee under a securitization Pooling and Servicing Agreement (a "PSA"), the moving party under the stay relief motion, did not prove that the mortgage at issue ever was assigned to the Depositor under the PSA. *Id.* at 268. The court noted that both it and the debtor "are entitled to insist that the moving party establish its standing in a motion from a relief from stay through the submission of an accurate history of the claim of ownership of the mortgage. Absent such proof, relief from the stay is unwarranted and a proof of claim filed by the moving party, to which an objection is filed, must be disallowed." *Id.* at 269.

Consequently, the court denied Deutsche Bank's stay relief motion and sustained the debtor's claim objection without prejudice to reconsideration upon the filing of an amended proof of claim by the proper party. *Id.* at 270 (*citing* Bankruptcy Code § 502(j) and Bankruptcy Rule 3008); *see also In re Wells,* 407 B.R. 873, 881-83 (Bankr. N.D. Ohio 2009) (disallowing proof of claim in a chapter 13 case because the Trustee under a PSA and its

servicer failed to prove that the Trustee had standing to file the proof of claim). Ominously for counsel for the mover, the court noted that inaccurate representations about the moving party's status as a holder may constitute a violation of Bankruptcy Rule 9011 and may warrant sanctions under 28 U.S.C. § 1927. *Hayes,* 393 B.R. at 269; s*ee also In re Fitch,* 2009 WL 1514501 (Bankr. N.D. Ohio, May 28, 2009) (the court ordered an audit of any cases in its district in which MERS filed affidavit of default and, if any incorrect affidavits were filed, ordered counsel to appear at an adjoined hearing).

In re Jacobson

In this case, the Bankruptcy Court for the Western District of Washington denied the motion for relief from automatic stay because the moving party, UBS AG, could not show it had standing, nor that it had authority to act for anyone that did have standing. *In re Jacobson*, 402 B.R. 359, 369 (Bankr. W.D. Wash. 2009). UBS AG purported to represent ACT as servicer of the note. *Id.* The court cited Hwang, noting that even if the moving party is the noteholder's agent, it does not make the agent a real party in interest. *Id.* at 366. To have standing to prosecute the motion in the name of the real party in interest, the court required UBS AG to show it had authority to act on the noteholder's behalf. *Id.* at 367. Since UBS AG made no such showing, and it was not the real party in interest, the court denied the motion. *Id.* at 770.

Execution of the original note was on behalf of Castle Point Mortgage ("Castle Point") and listed MERS as a beneficiary "solely as nominee for lender and lender's successors and assigns." *Id.* at 362. Castle Point later sold the note to ACT Properties, LLC ("ACT") in an unrecorded transaction. *Id.* However, UBS AG admitted that Wells Fargo held the note. *Id.* at 363. The court questioned, as did the court in *Hwang*, whether ACT itself would even qualify

as the holder given that someone endorsed it in blank and another had possession of the note. *Id.* at 369.

As both an admonition and suggestion to MERS, the court instructed that it is possible to prove the identity of the various holders and servicers by putting forth evidence and stated that some courts require such evidence to be admissible before considering it. *Id.* at 367. The evidence put forth by UBS AG did not meet any standards of admissibility, and the court further commented on its ineffectiveness. *Id.* UBS AG submitted a conclusory declaration by a "bankruptcy specialist" stating he was a custodian of the records, knew them to be a true copy of the originals made at the time of the events in the ordinary course of business. *Id.* at 368. Although no business records were submitted, the court opined that the "bare assertion that one works for the company and is familiar with its recordkeeping procedures is not sufficient . . . to establish the person is sufficiently knowledgeable about the subject of the testimony." *Id.* The testimony needs to express information warranting the conclusion that the records presented are what they purport to be. *Id.*

Unlike *Hwang*, the movant here asserted that it was the servicer of the note and acting on behalf of the holder. In addition, neither UBS AG nor ACT had actual possession of the note and thus neither appeared to have any right to enforce it. *Id.* at 370. While establishing that UBS AG is the agent rather than the noteholder seems like it might be an easier standard to meet, it must still show it is the agent of ACT. *Id.* Even if it could, it must also show ACT is the real party in interest and join ACT as a party or litigate in its name instead of its own name. *Id.* Because UBS AG was not the real party in interest nor could it show it was acting on behalf of the real party in interest, the court denied the motion for relief from stay. *Id.*

In re Sheridan

In this case, the Bankruptcy Court for the District of Idaho considered a stay relief motion brought by MERS as nominee for HSBC Bank USA ("HSBC"). *In re Sheridan*, 2009 WL 631355 (Bankr. D. Idaho, Mar. 12, 2009). MERS not only asserted it was nominee, but also characterized itself as a "secured creditor and Claimant." *Id.* at *1. MERS was designated a beneficiary on the Deed of Trust and as nominee for the noteholder at the time of execution. *Id.* at *6 The court still found this insufficient, as there was no showing made as to who the current noteholder was. The court also held MERS was not an actual beneficiary, despite the Deed naming it one, since no actual economic benefit accrued to it. *Id.* at * 4.

The Promissory Note and Deed of Trust identified the lender as Fieldstone Mortgage Company ("Fieldstone"), and the Deed also identified MERS as nominee and beneficiary for the noteholder and all its successors and assigns. *Id.* at * 4. The Promissory Note also stated that "anyone who takes this Note by transfer and who is entitled to receive payments . . . is called the Note Holder." *Id.* at *1. MERS argued that it had authority to act for the current noteholder, whoever that was, since it was named as a beneficiary and nominee for all successors and assigns. *Id.* at *4. Even if the court agreed, there is still the issue of the Note not indicating any transfer to other parties. *Id.* at *5. Therefore, Fieldstone appeared to be the current noteholder, and MERS did not purport to represent Fieldstone at any time. *Id.* at *4. The court denied the motion for relief from stay for two reasons: (1) It found the "titular designation" of MERS as "beneficiary" on the Deed insufficient to establish it as such; and (2) there was no evidence or explanation presented showing whether HSBC had any current interest in the note. *Id.*

Merely naming a party as a beneficiary of an instrument is not sufficient to make it one. *Id.* The court looked to Idaho Code § 45-1502(1) which defines a beneficiary for purposes of the trust deed statute as "the person for whose benefit a trust deed is given." *Id.* Therefore, MERS was not a beneficiary under Idaho Code because the trust deed benefits the noteholder, which appeared to be Fieldstone in this case. *Id.* In addition, the language used in the Deed of Trust was confusing as it also stated that MERS will act "solely as nominee for Lender and Lender's successors and assigns." *Id.* Because MERS was not a beneficiary under Idaho Code and the language of the Deed was ambiguous, the court held that MERS was not a real party in interest and could not bring the motion in its own name. *Id.*

Even if MERS was properly acting as the agent of the real party in interest there was no showing that HSBC, or even Fieldstone, had any current interest in the note. *Id.* If there had been, the action must still be brought in the real party in interest's own name, not its agent's. *Id.* Later MERS submitted a "supplemental affidavit" stating that it had obtained an original copy of the Note, which now indicated an endorsement. *Id.* at *5. The court found the affidavit improper for several reasons. But, even had the court been able to consider it, the affidavit would not have assisted MERS since there was neither a date nor any indication of who the transferor or the transferee was. *Id.* at *6. Even if Fieldstone had endorsed the note in blank it would not have established HSBC or Fieldstone as the noteholder since Idaho Code provides it "may be negotiated by transfer of possession alone until specially indorsed." *Id.* The court held, "the only entity that MERS could conceivably represent as agent/nominee would be [Fieldstone]. But MERS does not represent [Fieldstone] . . . and, in fact, . . . conten[ds] that [Fieldstone] is no longer a party in interest." *Id.* at *6.

Because MERS was unable to establish that it was a real party in interest with standing, or even that it represented such, the court denied the motion for relief from stay. *Id.; accord, In re Vargas,* 396 B.R. 511 (Bankr. C.D.Cal. 2008) (because MERS was not the holder of the note, and because only the holder of a negotiable promissory note is entitled to enforce same, the stay relief was denied).

In re Mitchell

Mitchell is the lead case for a number of motions to lift stay filed in MERS' own name or filed in the name of MERS as nominee for another. *In re Mitchell*, 2009 WL 1044368 (Bankr. D. Nev., Mar. 31, 2009). The Bankruptcy Court for the District of Nevada handled the motions in a joint hearing because each of the cases had substantially similar issues regarding MERS' standing. *Id.* at *1. MERS withdrew the motions to lift stay in all but four of the cases and, in this opinion, the court issued orders in two of the cases. *Id.* Like *Sheridan*, this court denied the motions in both cases because MERS was not the noteholder nor did it show the authority to act on behalf of one who was the noteholder. *Id.* at *4.

Similar to *Sheridan*, MERS argued it had standing because the deeds of trust either named it as a beneficiary or as the nominee of the beneficiary. *Id.* The court noted that merely naming MERS a beneficiary does not give it any rights to enforce the note. *Id.* at 3. The court found that, since MERS had no rights to any payments, servicing rights or any rights to secured properties, it was not a beneficiary. *Id.* The court also found similar ambiguities in the language of the deeds of trust and in MERS' brief regarding whether MERS argued it had standing in its own right, or as the nominee, or both. *Id.* Even if MERS was a beneficiary of the note, that alone would be insufficient to confer standing. *Id.* For MERS to foreclose, it must show that it had possession of the note and the deed of trust or it had authority to act as

agent for the entity that did. *Id.* at *4. Because MERS was not the beneficiary or the holder of the deed of trust, nor was there evidence that the principal it purported to act on behalf of were either of these, the court denied the motions for relief from stay. *Id.* at *6.

In re Wilhelm

In a recent decision, the Bankruptcy Court for the District of Idaho further expounded on the requirements for lenders to show standing when seeking relief from the automatic stay. *In re Wilhelm,* 407 B.R. 392 (Bankr. D.Idaho 2009). In his decision, Judge Myers held that the movants in five different actions for relief from stay lacked standing to bring such motions because: (1) they were not named on the notes at issue; (2) the notes were not indorsed in blank or to any specific person or entity (such as the movants); (3) the movants failed to prove that they held the notes; and (4) the movants were not proper assignees of the notes even though they argued that MERS assigned the notes to them because the notes named MERS as beneficiary acting solely as nominee with no right to assign the notes.

The court found that "there are two threshold questions in each of these motions: (1) Have Movants established an interest in the notes? (2) Are Movants entitled to enforce the notes?" *Id.* at 398. The court held that the Movants failed to provide any admissible proof to answer either question in their favor and, in fact, the notes attached to several declarations contradicted the information contained in the declarations. In reaching its decision, the court did add one important admonition to counsel: "In general, counsel should gather the appropriate documents and factual data *before* filing the motions (as required by Rule 9011 in any event), rather than attempting to cure patently defective motions with serial supplemental filings." *Id.* at 403 (emphasis in original).

In re Foreclosure Cases

Standing and real party in interest problems occur outside of bankruptcy courts in foreclosure actions themselves. In *In re Foreclosure Cases,* 2007 WL 3232430, *2 (N.D. Ohio, Oct. 31, 2007), the United States District Court for the Northern District of Ohio dismissed fourteen (14) foreclosure actions filed by Deutsche Bank National Trust Company ("DB"), as Trustee under a PSA for certain asset-backed pooled mortgage facilities because the DB failed to establish diversity jurisdiction and standing. In the foreclosure actions, Judge Christopher Boykin issued an Order requiring DB to prove that it was the holder and owner of the underlying notes and mortgages that were the basis for each of the foreclosure actions. DB was required to file a copy of the executed Assignment demonstrating that DB was the holder and owner of the Note and Mortgage as of the date the Complaint was filed. The original lender was reflected as the mortgagee and no assignment to DB was reflected in the chain of title. Under Ohio law, assignments of mortgages are subject to recording requirements. Therefore, in addition to execution of a mortgage assignment, recording may also be required to establish standing.

DB produced Mortgage Assignments dated after the date of the original foreclosure complaint. These Mortgage Assignments were attached to pleadings in support of DB's position that the Mortgage Assignments were sufficient to establish standing to prosecute the foreclosure actions, even though such Mortgage Assignments were entered into after the commencement of the foreclosure actions. The Court disagreed. It found that DB was not the holder of the notes when the complains were filed and dismissed all 14 foreclosure actions. The dismissals were without prejudice to re-file at a later date.

Other recent, notable cases dealing with standing issues in state law foreclosure proceedings are: *Mortgage Electronic Registration System, Inc. v. Southwest Homes of Ark.,* 302 S.W. 3d 1 (Ark. 2009) (MERS is not a necessary party in a deed of trust foreclosure because it is neither the trustee nor the beneficiary under the deed of trust); *Landmark Nat'l Bank v. Kesler,* 216 P.3d 158 (because MERS is not a lender, it is not a necessary party in a mortgage foreclosure action and has no due process right to intervene; the court describes MERS, variously, as a "straw man" and a "front man" for its financial institution members); *Goodyke v. BNC Mortgage, Inc.,* 2009 WL 2971086 (D.Ariz., Sept. 11, 2009) (because a nonjudicial foreclosure in Arizona does not require presentation of the original note before commencing the foreclosure proceedings, debtors' "show me the note" argument in support of an action to enjoin the foreclosure lacks merit).

CONCLUSION

The cases discussed above highlight the failure of several lenders to keep adequate records of transfers of underlying notes. Without a proper paper trail, lenders cannot show that they have standing or are the real parties in interest entitled to bring a motion for relief from the automatic stay or a subsequent foreclosure action. In addition, attorneys should take note of how courts will regard conclusory affidavits in support of these motions as well as the potential for Rule 11 land mines when taking a client's averments regarding the ownership of a note or deed at face value without making a reasonable and independent inquiry before submitting such statements to a court.

DISCLAIMER

This presentation summarizes certain cases, arguments and developments, and is for educational purposes only. It should not be attributed as the views either of the authors or the presenters or of their clients.

TABLE OF RECENT ADDITIONAL AUTHORITIES REGARDING STANDING ISSUES

1. Stay Relief Cases:

In re Emrich, 2009 WL 3816174 (Bankr. N.D. Cal., Nov. 12, 2009)

In re Gramajo, 2009 WL 2824786 (Bankr. N.D. Cal., Apr. 24, 2008)

In re Hayes, 393 B.R. 259 (Bankr. D. Mass. 2008)

In re Jacobson, 402 B.R. 359 (Bankr. W.D. Wash. 2009)

In re Lopez, 2010 WL 1636040 (Bankr. D. Ariz., Apr. 19, 2010)

In re Sheridan, 2009 WL 631355 (Bankr. D. Id., Mar. 12, 2009)

In re Weisband, 427 B.R. 13 (Bankr. D. Ariz. 2010)

2. Claims Objections Cases

Brown v. Ameriquest Funding II, LLC, 2010 WL 1571160 (Bankr. D. Mass. Apr. 19, 2010)

In re Hayes, 393 B.R. 259 (Bankr. D. Mass. 2008)

In re Minbatiwalla, 424 B.R. 104 (Bankr. S.D. N.Y. 2010)

In re Samuels, 415 B.R. 8 (Bankr. D. Mass. 2009)

In re Williams, 395 B.R. 33 (Bankr. S.D. Ohio 2008)

3. Adversary Proceedings/Foreclosure Cases

Brown v. Ameriquest Funding II, LLC, 2010 WL 1571160 (Bankr. D. Mass. Apr. 19, 2010)

Dumesnil v. Bank of America, N.A., 2010 WL 1408889 (D. Ariz., Apr. 7, 2010)

Newbeck v. Washington Mutual Bank, 2010 WL 291821 (N.D. Cal., Jan. 19, 2010)

Rhoads v. Washington Mutual Bank, F.A., 2010 WL 1408888 (D. Ariz., Apr. 7, 2010)

In re Williams, 395 B.R. 33 (Bankr. S.D. Ohio 2008)

4. Sanctions Cases

In re Lee, 408 B.R. 893 (Bankr. C.D. Calif. 2009)