COMMENTARY

Ibanez: A 19th-century decision for the 21st century

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The Massachusetts Supreme Judicial Court issued its opinion in *U.S. Bank National Association v. Ibanez* Jan. 7, effectively turning back the clock on modern mortgage finance to the 1800s.[1] Rather than acknowledge the clear intention of its own Legislature and join the vast majority of states where "the mortgage follows the note," the court erred by following case law from the 19th century — cases that even then were slipping out of the mainstream law of secured transactions.

In *Ibanez*, a residential mortgage and note passed from the original mortgagee through several entities and eventually was securitized. Antonio Ibanez stopped paying his mortgage, and his property was indisputably subject to foreclosure. The securitization trustee, as holder of the original note (indorsed in blank),[2] and an assignment of mortgage (executed in blank),[3] foreclosed on the mortgage and published a notice of a sale. The trustee purchased the property at the foreclosure sale. After the sale, the record holder of the mortgage assigned it to the trustee, and the assignment was recorded. A similar fact pattern occurred in connection with foreclosure on the Massachusetts property of Mark and Tammy LaRace by another securitization trustee, which occurred around the time of the Ibanez foreclosure.

When the trustees brought separate actions in the Massachusetts Land Court to quiet title to the Ibanez and LaRace properties, the court consolidated the cases and held that the foreclosure sales were void because the foreclosing party must be the holder of the mortgage *before* the foreclosure commences. When the trustees offered up assignments in blank and other documents in an attempt to show valid pre-foreclosure assignments, the court found that the pre-foreclosure assignments of mortgage in blank and the other proffered documents did not effectively transfer the mortgages. As a result, because the mortgage does not automatically follow the note in Massachusetts, the holders of the notes could not foreclose. The Massachusetts Supreme Judicial Court affirmed.

For well over a century, it has been settled law throughout the United States that the "mortgage follows the note."[4] In his 1826 "Treatise on the Law of Mortgages," British barrister John Joseph Powell said, "[t]he real transaction in the transfer of a mortgage, amounts merely to an assignment of a debt, collaterally secured by a charge on the real estate."[5]

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In 1847 the Virginia Supreme Court held that "the mortgage follows the debt."[6] In the most notable case on point, the U.S. Supreme Court clearly stated in 1873 that "the transfer of the note carries with it the security, without any formal assignment or delivery or even mention of the latter."[7]

In an effort to make "the mortgage follows the note" a national standard, the Restatement (Third) of Property states: "A transfer of an obligation secured by a mortgage also transfers the mortgage unless the parties to the transfer agree otherwise."[8]

Additionally, the Uniform Commercial Code explicitly "codifies the common-law rule" that the mortgage follows the note.[9] The reason that the mortgage follows the note is straightforward: If the mortgage and the note were separated, the underlying purpose of the transaction would be defeated. The holder of the mortgage would have the possessory interest to foreclose on the property, but without the promissory note, would never have the right to foreclose.

Conversely, the holder of the note without the mortgage would have an unsecured debt, which would defeat the entire purpose of creating the mortgage. As the Restatement notes, "This result is economically wasteful and confers an unwarranted windfall on the mortgagor."[10]

Massachusetts, however, is in a true minority of states where the law remains, in the words of the Restatement, "economically wasteful."[11] Transferring the note does not transfer the mortgage; Rather, the mortgage stays with the transferor of the note, and the transferee only obtains an "equitable right" to the mortgage. For its rule, the Massachusetts Supreme Judicial Court cited two cases from the 1800s: *Barnes v. Boardman* (1889)[12] and *Young v. Miller* (1856).[13] As precedent, however, *Barnes* and *Young* are weak. *Barnes* was most recently cited in 1942, and *Young* was last mentioned by a Massachusetts court in 1934.[14]

Moreover, the *Ibanez* court ignored legislative efforts to modernize Massachusetts commercial law. For example, Mass. Gen. Laws Ch. 106, § 9-203(g), incorporates the relevant U.C.C. provision word for word: "The attachment of a security interest in a right to payment or performance secured by a security interest or other lien on personal or real property is also attachment of a security interest in the security instrument, mortgage or other lien."

This provision protects those, such as warehouse lenders, who take a security interest in a note (or a bundle of notes) by allowing them to enforce the mortgage in the event of default on the warehouse line. In other words, the mortgage follows the security interest in the note.

It makes no sense to treat the enforceability of the mortgage differently simply because the collateral was transferred as a result of a sale of the note as opposed to the collateralization of a note.

It is settled law in Massachusetts that "[w]here a U.C.C. provision specifically defines parties' rights and remedies, it displaces analogous common-law theories."[15]

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By adopting the U.C.C., it was the explicit intention of the Massachusetts Legislature to "simplify, clarify and modernize" mortgage finance law.[16] Accordingly, it was error for the court to ignore the clear intent of the Legislature in favor of case law that was out of the mainstream even in 1856, generations before modern securitization existed.[17]

CONCLUSION

The Massachusetts Supreme Judicial Court's decision in *Ibanez* was based on antiquated case law and will generate confusion for lower courts facing complex foreclosure questions in the future. The *Ibanez* court should have followed the Legislature's express implementation of the U.C.C. and moved Massachusetts into the 21st century with the rest of the country.

Instead, the *Ibanez* court relied on outdated precedent and left Massachusetts an outlier in the world of property law. The fact remains that Ibanez had stopped paying his mortgage. Concurring in the court's decision, Justice Robert Cordy freely admitted that "[t]here is no dispute that the mortgagors of the properties in question had defaulted on their obligations and that the mortgaged properties were subject to foreclosure."[18]

Some may believe that the court's short-sighted decision to provide an "unwarranted windfall on the mortgagor"[19] is justified considering the current economic climate, but ultimately, the result is both unjust and economically wasteful. WJ

NOTES

1 *U.S. Bank Nat'l Ass'n v. Ibanez*, 2011 WL 38071, Slip Op. SJC-10694 (Mass. Jan. 7, 2011).

2 An endorsement in blank does not name the payee (endorsee) of the note; Rather, the name is filled in later by the party that ultimately owns the note.

3 An assignment in blank has all the formalities necessary for recording, except the identity of the assignee is not filled in.

4 *See, e.g., In re Bird*, 2007 WL 2684265, at ¶¶ 2-4 (Bnkr. D. Md. 2007) ("The note and mortgage are inseparable — the former as essential, the latter as an incident. An assignment of the note carries the mortgage with it, while an assignment of the latter alone is a nullity.").

5 John Joseph Powell, Treatise on the Law of Mortgages 907-08 (1826).

6 *Yerby v. Lynch*, 3 Gratt. 460; *See, also Fisher v. Otis*, 3 Chandler (Wis.) 83, 3 Pin. 78 (Wis. 1850); *Jackson ex dem. Norton v. Willard*, 4 Johns. 41 (N.Y. Sup. Ct. 1809); *Breckenridge's Heirs v. Ormsby*, 1 J.J. Marsh. 236, 1829 WL 1187 ("The mortgage was only a collateral security. Anything that assigns or extinguishes the debt, transfers or discharges the mortgage deed; 2 Marsh. 109; 2 Burrow, 978; 11 Johnson's Repts. 534; 15 Ib. 319.").

7 *Carpenter v. Longan*, 83 U.S. 271 (1872) ("All the authorities agree that the debt is the principal thing, and the mortgage an accessory.").

8 Restatement (Third) of Property, Mortgages § 5.4(a) (1997). The Restatement does allow for the severing of the note and mortgage, but it is only in the rare instance when it is the explicit intention of the two parties, and such intent is expressly documented in the assignment. *See id.* illustration 4.

9 U.C.C. 9-203 cmt. 9 (citing Restatement (Third) of Property, Mortgages § 5.4(a) (1997)). U.C.C. § 9-203(g), codified in Mass. Gen. Laws ch. 106, § 9-203(g), provides that "[t]he attachment of a security interest in a right to payment or performance secured by a security interest or other lien on personal or real property is also attachment of a security interest in the security interest, mortgage or other lien."

10 Restatement (Third) of Property, Mortgages § 5.4 cmt. a (1997).

11 Minnesota appears to be the only other state that uses the "equitable right" or "equitable trust" theory. *Jackson v. Mortgage Elec. Registration Sys.*, 770 N.W.2d 487, 497 (Minn. 2009) ("We have held that, absent an agreement to the contrary, an assignment of the promissory note operates as an equitable assignment of the underlying security instrument.") (citing *First Nat'l Bank of Mankato v. Pope*, 85 Minn. 433, 434-35, 89 N.W. 318, 318-19 (1902)). However, the Maine Supreme Judicial Court recently indicated in dicta that it might be open to this view. *See JPMorgan Chase Bank v. Harp*, 10 A.3d 718 (Me. Jan. 6, 2011) ("At the commencement of the litigation, JPMorgan owned the note, but not the mortgage. JPMorgan would have been vulnerable to a motion by Harp challenging JPMorgan's ability to foreclose at that time.").

12 149 Mass. 106 (1889).

13 6 Gray 152 (1856).

14 This information was obtained through a recent search using Westlaw's KeyCite Online search for 149 Mass. 106 and 6 Gray 152 (Jan. 14, 2010).

15 *Gossels v. Fleet Nat'l Bank*, 453 Mass. 366, 370 (2009) (citing *Nat'l Shawmut Bank v. Vera*, 352 Mass. 11 (1967); *Stone & Webster Eng'g Corp. v. First Nat'l Bank & Trust Co.*, 345 Mass. 1 (1962)).

16 *See* Mass. Gen. Laws. Ann. ch. 106, § 1-102(1, 2) ("This chapter shall be liberally construed and applied to promote its underlying purposes and policies. Underlying purposes and policies of this chapter are to simplify, clarify and modernize the law governing commercial transactions."). Additionally, Chapter 106 was enacted "to make uniform the law among the various jurisdictions." By adhering to dated, outlier law, the court is frustrating the Legislature's clear goals. *Id.* at Section 1-102(2)(c).

17 Courts routinely abandon antiquated practices that lack logical application to modern systems. *See, e.g., Kalinoski v. Kalin*, 829 S.W.2d 24 (Mo. Ct. App. 1992) ("The rule stating that a grantor will not be able to sell property to himself goes back to the days of enfeoffment by livery of seisin. Property law in those days also required a wax seal on a deed and prohibited married women from selling or renting property [citation omitted]. These legal antiquities have since been abandoned for far more reasonable rules. Although the rule before this court, that a grantor will not be able to convey to himself, has not been abandoned by any of our sister states at this time, we see no reason to prolong the life of a rule which was written to apply to days of livery of seisin and which has no logical application or importance today.").

18 *Ibanez*, Slip Op. SJC-10694 at 12.

19 Restatement (Third) of Property, Mortgages § 5.4 cmt. a (1997).

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