

# Mortgages

- Mix of property and contract
  - Promissory Note
  - Mortgage
- *Mortgagor* – grantor of security interest in the land (house buyer)
- *Mortgagee* – this is the one lending the money (bank)
- *Equity* – difference between value of land and security interest granted
  - also called *equity of redemption*

# Mortgages

- Model mortgage:
  - buyer (Mortgagor) contributes 20% equity
  - fixed interest rate
- Does selling the mortgaged property get rid of the mortgage?
  - runs with the land
- Purchaser takes **subject to the mortgage**
- Purchaser takes **assuming the mortgage**
  - Original mortgage may have a no assumption clause
- **Due on sale** clause

# Mortgages

Suppose Joan Watson wants to sell her house to Sherlock Holmes. She still owes \$400,000 on her house; Holmes will be buying it for \$500,000. But she doesn't have \$400,000 in the bank to pay off her mortgage, which has a due on sale clause. How can she accomplish the sale?

- Before sell, what is Joan Watson's equity?
- What happens to the mortgage upon sell?
- Likely a new mortgage?
  - How much money "out of pocket" will Holmes likely pay at purchase?
  - This creates how much equity for Holmes?

## Foreclosure

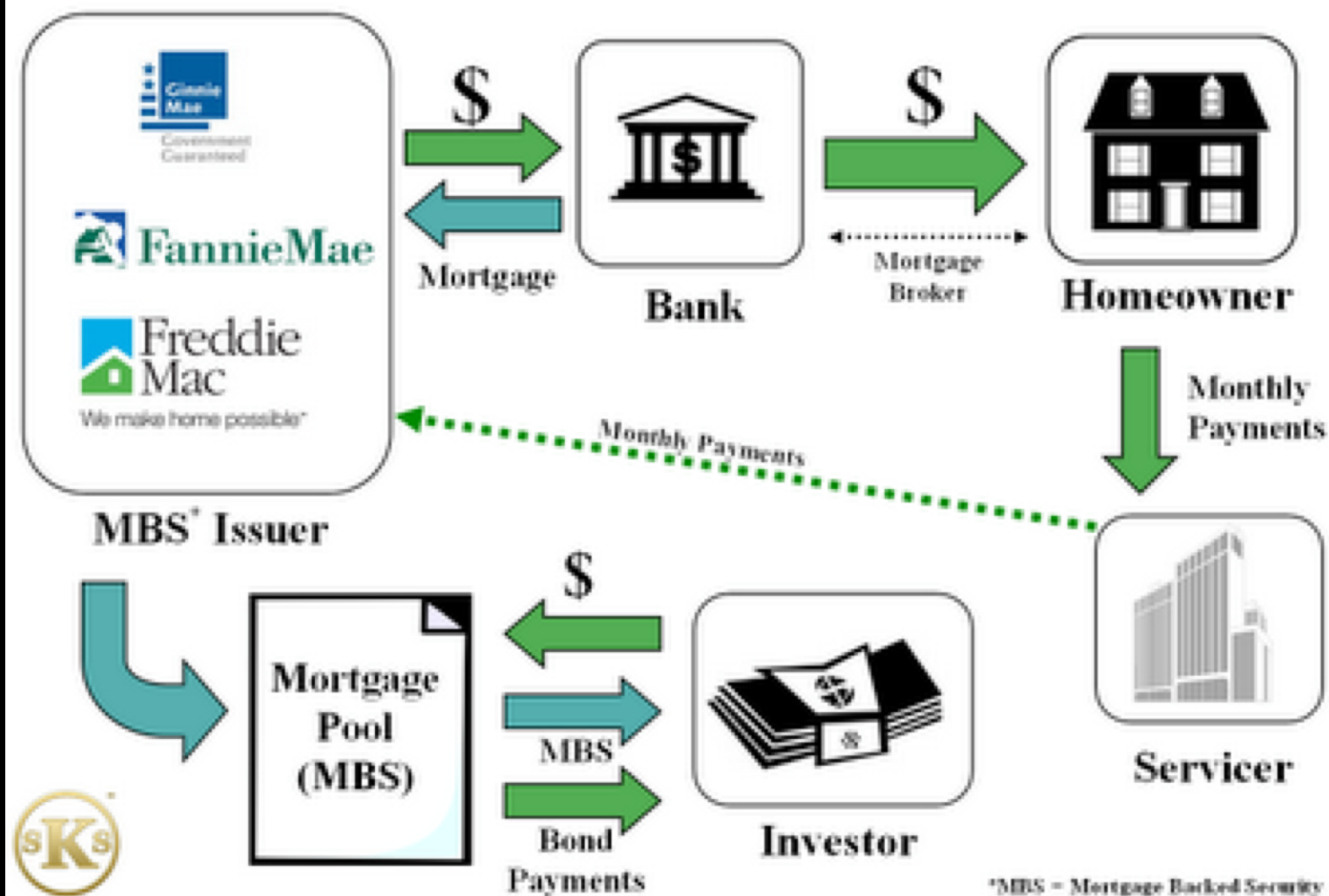
- Initially – must pay on “law day” or lose property
  - What if M’or had some equity?
- Created equity of redemption
  - But how is it extinguished?
- *Strict Foreclosure* – notice, hearing, and court decree – title goes to Mortgagee (not used much)
- *Foreclosure Sale* – notice and hearing and then judicially ordered sale (auction)
- *Deed of Trust* – notice and wait time and then Mortgagee conducts sale (a little faster)
- All of this to cut off *equity of redemption*

## Foreclosure

- Foreclosure sale likely to get market value?
- What happens if foreclosure sale not enough to cover mortgage?
  - Upside down
  - Due process safeguards
- Recourse loan
- Nonrecourse loan

Betty Finn buys a house for \$450,000. She puts down \$90,000 and takes out a mortgage for \$250,000 from Heather Chandler, and a second mortgage for \$110,000 from Veronica Sawyer. When Betty defaults, the house is sold for \$500,000 at foreclosure. Assuming the amounts due on the mortgages haven't changed at all, how should the proceeds be distributed? What would the answer be if the house brought \$350,000 at foreclosure?

# Mortgage Lending with Securitization



## ***McGlawn v. Pennsylvania Human Relations Comm'n***

- McGlawn mortgage broker
- Brokers mortgages to Taylor and Poindexter
- Relevant attributes of these brokered mortgages:
  - Interest rate
    - Compare to prime rate
    - Compare to previous mortgage interest rate
  - Settlement fees
  - Yield spread premium
  - Other fees
  - Fraud
  - Essentially all to African-Americans

## ***McGlawn v. Pennsylvania Human Relations Comm'n***

- What is the claim?
- Reverse Redlining
- Predatory Lending
  - Why did the M'ors accept these?
  - Why would M'ee accept mortgages with high likelihood of default?
  - What if we just had a high interest rate?
- International Discrimination
  - What if no mortgages available for better terms?
- Remedy?
- Moral hazard problem?



# “Nontraditional” Mortgages in General

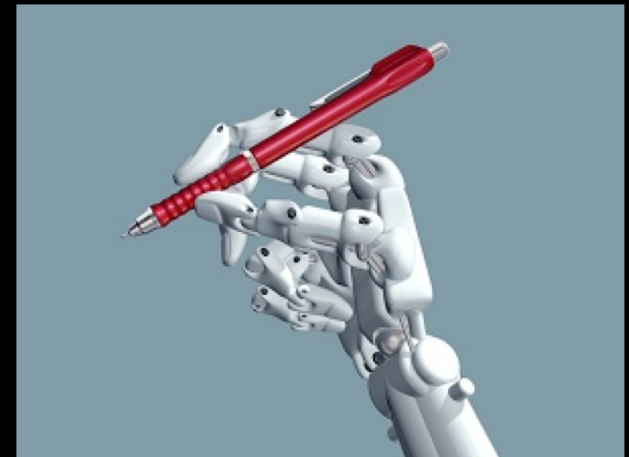
- Adjustable Rate Mortgage (ARM)
  - typical is a 30-year fixed rate
  - ARM has fixed rate for 2-3 years
    - then adjust to higher, variable rate for rest of term
- Debt-to-Income Ratio
  - typically 28-36% gross income
  - these approached 50%
    - and calculate on fixed rate portion of ARM
- Loan-to-Value Ratio
  - typically 80-20
  - approached 100 (no downpayment, equity)
- Predatory?
- What happens with these when economy/housing ↓

## ***Klem v. Washington Mutual Bank***

- Halstein owns home – worth ~235K to 320K
  - Outstanding mortgage – 75K
- Defaults – and Quality forecloses
  - Why not sell before hand?
  - Quality forecloses on behalf of who?
  - Sells for more than \$1 than owes
    - What happens shortly after the sale?
  - False notary -- earlier date of sale
  - Halstein's guardian had found 235K buyer

# *Klem v. Washington Mutual Bank*

- What is the claim?
  - Consumer Protection Act
- (1) Unfair or deceptive act or practice
  - Discretion to postpone sale
    - What about directions from WaMu?
    - Whose interest representing?
    - Lack of proper discretion enough by itself?
  - Predating notarizations
    - Robo signing
    - What is harm?
      - Benefit to consumer?
  - Can foreclosure price be enough?



## ***Klem v. Washington Mutual Bank***

- (2) occurring in trade or commerce
- (3) public interest impact
- (4) injury to plaintiff in his or her business or property
  - What awarded?
- (5) causation

## ***U.S. Bank v. Ibanez***

- Dec. '05 -- Ibanez Mortgage (*M*) – 103K with Rose Mortgage (M'ee)
- June '06 -- Rose Assigns *M* to Option One
- Allegedly assigned from Option One to Lehman, then Lehman Holdings, then Structured Asset, then U.S. Bank
  - All in '06
  - “will be” assigned
  - part of mortgage-backed security

# ***U.S. Bank v. Ibanez***

Rose Mortgage, Inc. (originator)



Option One Mortgage Corporation (record holder)



Lehman Brothers Bank, FSB



Lehman Brothers Holdings Inc. (seller)



Structured Asset Securities Corporation (depositor)



U.S. Bank National Association, as trustee for the Structured Asset Securities Corporation Mortgage Pass-Through Certificates, Series 2006-Z

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  - All in '06
  - “will be” assigned
  - part of mortgage-backed security
- July '07 – U.S. Bank forecloses on Ibanez
- Sept. '08 – Am. Home Mortgage (successor to Option One) assigns *M* to U.S. Bank

## ***U.S. Bank v. Ibanez***

- May '05 -- LaRace Mortgage (*M*) – 103K with Option One (*M'ee*)
- Same month – Option One executes blank assignment
- July '05 – Option One transfers to B of A
  - No document to reflect this assignment
- Oct. '05 – B of A assigns to ABFC
- ABFC pools mortgages and transfers to Wells Fargo
  - Unexecuted
  - No referenced schedule
  - Unsigned document that links Option One, BofA, and Wells Fargo



# *U.S. Bank v. Ibanez*

Option One Mortgage Corporation (originator and record holder)



Bank of America



Asset Backed Funding Corporation (depositor)



Wells Fargo, as trustee for the ABFC 2005-OPT 1, ABFC Asset-Backed  
Certificates, Series 2005-OPT 1

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  - No referenced schedule
  - Unsigned document that links Option One, BofA, and Wells Fargo
- April '07 – Wells Fargo moves to forecloses on LaRace
- May '07 – Option One assigns *M* to Wells Fargo

## ***U.S. Bank v. Ibanez***

- M'ee statutory power of sale
- M'or must have notice of M'ee foreclosing
- Is U.S. Bank or Wells Fargo the M'ee at time of foreclosure?
  - Title Theory state
  - U.S. Bank “will be” assigned
  - Wells Fargo schedule not specifically identify
- Is mortgage note enough?
- Do postsale assigns cure?
- Is this form over substance?
- Is this ruling good for the real estate market?



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