



# The Institutional Risk Analyst

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## Is the US a "BBB" credit? David Woolley on the MERS land title chain fiasco

August 2, 2011

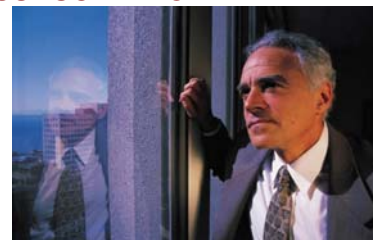
"If ye love wealth better than liberty, the tranquility of servitude than the animating contest of freedom, - go from us in peace. We ask not your counsels or arms. Crouch down and lick the hands which feed you. May your chains sit lightly upon you, and may posterity forget that ye were our countrymen!"

Samuel Adams (1722-1803)

From the cover of "Children of Liberty: The Need for a New Political Party"

Xlibris (2010)

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The Institutional Risk Analyst

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In this issue of *The Institutional Risk Analyst*, we feature a summary of a paper by **David E. Woolley**, a California Licensed Land Surveyor and Certified Fraud Examiner, who is a principal of Harbinger Analytics Group in Tustin, CA. Thanks to David and **Lisa Herzog**, who edited the study and performed research, for summarizing the paper ([click here to see full copy](#)). But first a rant on the furious inaction of the past week.



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The announcement of a "compromise" deal by Congress that will allow the US to continue growing the public debt pile represents little or no real progress on fiscal issues. Politicians are once again seen to be spineless weasels, confirming the view of **Mark Twain** and his followers that the inhabitants of Washington constitute a permanent criminal class. But there is the question of whether the average American politician even understands the current economic circumstance well enough to judge right from wrong. We see **Elizabeth Drew**, for example, whining in the *New York Review of Books* about ["Debt Limit Crazyiness."](#) She writes:

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"**Lawrence Summers**, Obama's recently resigned chief economic adviser, said on *The Charlie Rose Show* in July that he found it "dispiriting" that "all of the energy is on the projected deficits... when the problem right now is that the economy is in danger of stagnating from lack of demand." The Republicans had made it clear for months that they would use the need to raise the debt ceiling as an instrument for extracting concessions from the Democratic President in the form of more cuts in federal programs. And the President assented to their premise, but only if there should also be some additional revenues. Were they all insane? That's not a far-fetched question."

Thank you for being a continuing reader of IRA's Analyst newsletters.

But far more disconcerting is the entirely Marxist economic analysis of Drew, Summers and their fellow travelers such as *New York Times* pundit **Paul Krugman**. Private investment seemingly is evil in the world of Elizabeth Drew. It never occurs to Drew and her colleagues in the Big Media that the point of the deficit debate is to cause a contraction in short-term demand as we find the real level of economic activity *ex-government deficit spending*. Drew and her ilk really believe that economic demand funded with public debt is as valuable as actual private economic activity, an entirely socialist world view. Is not the notion that we simply borrow and spend money we do not have far more insane than the conservative demands for fiscal balance?

## IRA Tweets

- IRA Analyst "MF Global: Where's the Cash? David Woolley on the Risk of Defective Commercial Land Titles" Feb 14, 2012 <http://t.co/zWjTiU8L> 2 days ago
- Santiago on HuffPo "Banking 2012: Maneuvering to Survive the Desert Landscape of Zero Interest Rates " Feb 6, 2012 <http://t.co/31mDcwEE> 10 days ago
- IRA Analyst Newsletter "Facebook "Jumps the Shark", an Interview with Michael Whalen", February 6, 2012 <http://t.co/zWjTiU8L> 10 days ago
- IRA Analyst Newsletter "John Mouseau: Munis Cruise Through a Scorching January", January 31, 2012 <http://t.co/zWjTiU8L> 16 days ago
- Failed Bank Forensics "First Guaranty Bank and Trust Company of Jacksonville" January

For six decades since the end of WW II and especially since the 1980s, Washington has used a combination of debt and inflation to manufacture the illusion of demand, mostly by pulling future sales into the present and later by fueling wanton real estate speculation. These methods to stimulate demand were aided by favorable demographics, a situation now reversed as the baby boomers grow old. Neither Krugman, not Summers nor Elizabeth Drew will ever have the courage and honesty to

tell their fellow citizens that the cost of make-believe economic policy funded with debt-fueled federal spending is double-digit consumer price inflation.

Even as liberal democrats fret about the horrors of a federal debt default, they in fact default on Social Security participants by effectively eliminating the COLA while fueling future inflation. The cost of the affordable housing boom of the last decade was to diminish the value of private money and savings, while rewarding leverage and avarice -- activities encouraged by public/private corruption. The key components of the neo-Keynesian model are (1) inflation fueled by federal debt and (2) the destruction of private financial assets via low interest rate policies by the Fed to protect the TBTF banks. What could be more European -- and anti-American?

You will never hear Larry Summers or Paul Krugman admit that the most recent stimulus spending had little or no effect on the US economy. Summers and Krugman seem to like the idea of impoverished Americans becoming more and more dependent upon government. This is why a growing number of observers believe that *less federal spending* and more private investment is the answer to the US economic malaise. Did you notice that New York State just passed a land bank law to encourage *private* rationalization of excess housing and land? This is the type of restructuring we need to see to help the *private economy* rebound, not more deficit spending.

Thus the "kick the can down the road" debt deal reached between the two institutional parties gets a thumbs down from us in terms of the forward probability of default for the US. The supposed debt deal reached in Washington deserves an immediate credit downgrade for the US, in our humble opinion. IRA co-founder Chris Whalen argues on *Reuters.com* this week, "[Basel III in the age of sovereign default.](#)" that if credit default swaps for the US are trading over 50bp per year, then sure looks like the marketplace is voting for a "BBB" bond ratings equivalent for Uncle Sam. A bond equivalent "AAA" rating equals 1bp of default probability. Will "AAA" sovereigns and corporates trade through Treasuries and agencies? Yep.

So now what do we do with sovereign risk weightings for Basel III in the brave new world of no risk free returns? If S&P drops the US to "A," banks would need to put aside capital against their portfolio of Treasury bonds and agency paper as well. This is one reason that we are giving banks that use The IRA Bank Monitor for stress test modeling the freedom to toggle the risk weight sensitivities for all asset and liability classes. Of note, IRA filed comments on the "[Proposed Guidance on Stress Testing for Banking Organizations With More Than \\$10 Billion in Total Consolidated Assets.](#)" The comments reflect our view that the process needs to have a public and private component to create comparability among banks. Comparability will, in turn, create industry benchmarks for all institutions to use in their ongoing stress testing and forward loss estimations.

We think that a survey approach for understanding the stresses in the entire industry will help regulators understand and mitigate systemic risk as required by Congress. Think classical analysis here, not quantum speculations, in the words of **Richard Feynman** ("[Steady state or dream state?](#)"). IRA CEO **Dennis Santiago** [writes in our comments:](#)

"We observe that the Guidance -- as presently drafted -- lacks specifics as to how regulators will architect a stress regime capable of observing the industry as a whole. Even within the subset of over \$10 Billion asset institutions covered by the guidance, the regime as described is too open in allowing banks to self-assess the stresses they face. There is a place for self assessment, make no mistake, but the first step to meet the direction of Congress with respect to systemic risk mitigation is a consistent approach to understanding the entire industry."

Just imagine taking an approach that first looks at the particular, then the general, to develop national policy regarding banks. That is basic scientific method, after all. But don't hold your breath waiting for any economists in the bank supervisory world to let go of their quantum tools and statistical regressions in favor of an explicit public census of bank performance and risk metrics. That revolution has yet to come, but it is in motion and it is driven by the data.

27, 2012 <http://t.co/JxCmu26t> 20 days ago

- Failed Bank Forensics "Patriot Bank Minnesota" 19810 HEADWATERS BOULEVARD FOREST LAKE, MN, 55025 January 27, 2012 <http://t.co/GVAPng0h> 20 days ago
- Failed Bank Forensics "Tennessee Commerce Bank" 381 MALLORY STATION ROAD FRANKLIN, TN, 37067 January 27, 2012 <http://t.co/KfpOl8H> 20 days ago
- Failed Bank Forensics "BankEast" 607 MARKET STREET KNOXVILLE, TN, 37902 January 27, 2012 <http://t.co/q1Ke3Sww> 20 days ago
- IRA Analyst Newsletter "Fred Feldkamp: Agenda Items for Lame Duck Congress to Fix the US Economy" January 23, 2012 <http://t.co/zWjTiU8L> 23 days ago
- Failed Bank Forensics "Central Florida State Bank" January 20, 2012 <http://t.co/y3EmgSl5> 26 days ago

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## **MERS - THE UNREPORTED EFFECTS OF LOST CHAIN OF TITLE ON REAL PROPERTY OWNERS AND THEIR NEIGHBORS**

By David E. Woolley

Many problems with MERS, the private mortgage title registry system created by the banking industry, have been reported in print media, in movies, on television and in academic journals. Courts have ruled against MERS' standing to foreclose, states Attorneys' General and Federal Bank Regulators are investigating MERS practices including fraudulently robo-signing and back dating missing documents and county recorders are suing to recover lost filing fees.

What none of the experts are analyzing (in specific terms) is the destructive effect that the MERS system will have on 400 years of recorded property rights in the United States. Most articles mention lost chain of title but stop short of explaining what this means, or how these problems will affect homeowners with or without mortgages in the MERS system. These problems deal with determining (1) property boundaries (senior and junior property rights) and (2) proof of ownership in order to obtain title insurance and financing. Because MERS is utilized for transferring title and these transfers are not publically recorded (thereby imparting constructive notice), MERS does not comply with race (first in time) or (constructive or actual) notice statutes and therefore, senior/junior property rights cannot be determined when a discrepancy arises in property boundary lines. Consider the following:

What happens if the chain of title cannot be determined because there are no accurate and publicly recorded deeds/title documents showing chain of title to determine senior and junior rights designations for boundary determinations between neighbors?

What happens when you destroy the property rights and records of homeowners who never defaulted on their mortgages and are now forced to litigate boundary disputes and property rights?

Why, if land title was actually stable, did the title insurance companies repeatedly refuse to underwrite foreclosures?

Historically, when land was subdivided in America, states enacted laws that required a land surveyor to file a public record. These laws made property line determinations available to the public, thus avoiding the need for litigation to resolve boundary disputes. In the Western U.S., subdivided 640 acre parcels were sold/homesteaded based on a government plat showing perfect rows of sections; however, in reality, each 640 acre sections varied from a few inches to a few hundred feet. Because of historically inaccurate surveying technology, there are many inaccurate boundaries that continue to be discovered today. Historically and today, the only practical way for a surveyor to resolve boundary discrepancies, absent litigation, is by examining chain of title records (history of conveyances from one owner to another) to determine senior and junior property rights.

To prove ownership of a particular parcel, a property owner must show a continuous title record back to the first conveyance. When boundary discrepancies arise, the following principles are followed:

As between private parties in a land dispute, a senior right is superior to a junior right.

As between private parties, a junior grant, in conflict with a senior grant, yields to the senior grant.

A grantor cannot convey what he does not own.

Between equal equities, the first in order of time shall prevail.

See [Diagram A](#) for an explanation of these principles in a normal (non-MERS) sequential conveyance when a shortage of land is discovered in a boundary dispute

between neighbors. When the principles listed above are followed, the boundary dispute is settled without the need for litigation between neighbors. The neighbor who obtained their land first in time keeps the entire amount conveyed. The neighbor who obtained their land second in time, keeps the remainder of the land that the original owner had left to convey.

### **MERS Has Broken/Diluted Chain of Title**

MERS was set up to electronically move paper at a high rate of speed to accommodate the securitization of mortgages and to avoid the time and cost associated with the local county recording process. When a MERS member transfers an interest in the mortgage loan to another MERS member, MERS may privately track the assignment within its system but MERS remains the mortgagee of record in publicly recorded documents. Today MERS is sometimes the only company listed in local government records and subsequent changes of ownership are shown in the MERS system only. Unfortunately, the MERS system is entirely inaccurate. A spokeswoman for Fannie Mae told the *New York Times* that the company could never rely on MERS to find ownership of a loan. In 2010, Professor **Alan M. White** of Valparaiso University Law School matched MERS ownership records to public domain records and found that fewer than 30% of mortgages had an accurate record in MERS. Currently, it is estimated that MERS holds over half of all mortgages in the United States - approximately 60 million mortgages and, in the event the chain of title is lost, MERS has a negative effect on the mortgaged homes, and each adjoining property (even those homes with no mortgage).

In many cases today, homeowners cannot search public records to find out who held their mortgage because records show MERS as the mortgage holder and/or the purchaser of the foreclosed property. Chain of title is lost because it cannot be traced amongst the hundreds of thousands of MERS transactions and any property (even without a mortgage) that shares a common property boundary line with the foreclosed property may have also lost its senior rights in a boundary dispute. Boundary disputes between neighbors are very common, however, they were historically not well publicized. This is simply because these boundary disputes were previously resolved by searching chain of title records and dividing property according to the basic principles listed above. Now that chain of title is destroyed or severely diluted, these same boundary disputes will require court intervention to settle boundary lines. Additionally, because of clouded titles, both foreclosed properties and their neighbors may not be able to sell their properties because buyers will not be able to obtain title insurance (without indemnification that banks may provide but subsequent individual sellers will not be able to provide) and consequently, they will not be able to obtain financing.

See [Diagram B](#) for a graphic explanation of these problems created by MERS.

We have already started to see this MERS problem in the context of title insurance become a reality. According to *Bloomberg*, October 20, 2010 "Fidelity National To Require Banks To Sign Foreclosure Warranty," because of the problems with MERS, in order for an individual buyer to obtain title insurance on a foreclosed home purchased from a bank, banks were required to provide a written indemnity to the title insurer and buyer stating that the bank actually owns the property and would defend against any subsequent claims on title. At one point in October 2010, Old Republic was reportedly refusing to write title policies for some foreclosures all together (although this policy was subsequently changed). Subsequently, the title insurance companies relaxed the indemnification requirement. Why? Because if one of the four major title companies required indemnity or refused to insure foreclosures altogether, this would be the demise of the title industry. The problems with boundary disputes will soon follow.

The only known alternative to the chain of title system is the Torrens system registering the owner rather than the land. To institute a Torrens system, you must have a court finding that eliminates the necessity for a chain of title and a declaration of the property location. Conceivably, if done properly, a Torrens system would take hundreds of years to create - not exactly a feasible solution.

MERS, a shell company with approximately 45 employees and 20,000 Vice Presidents (paying \$25.00 each for the right to use the MERS name), may destroy our land title

records affecting all American homeowners (not just those unfortunate enough to face foreclosure) if appropriate actions are not taken. Chain of title destruction boils down to the destruction of a basic American right - land ownership with a verifiable clear title.

Questions? Comments? [info@institutionalriskanalytics.com](mailto:info@institutionalriskanalytics.com)

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