PLUNKETT COONEY

Supreme Court finds Foreclosure Sale Voidable Where Foreclosing Mortgagee, Prior to Foreclosure Sale, Failed to Record Evidence of Assignment of Mortgage Obtained From FDIC

January 4, 2013

Marc P. Jerabek, CIPP/US
(248) 901-4016
mjerabek@plunkettcooney.com

The Michigan Supreme Court recently held that a foreclosing mortgagee is required to record evidence of assignment of the mortgage prior to the non-judicial foreclosure sale, even in instances where the mortgage loan is acquired through a Federal Deposit Insurance Corporation (FDIC) receivership.

The practical effects of this rule are that numerous completed foreclosures may be voidable, likely resulting in an increase in the number of lawsuits against mortgagees during the foreclosure process, and the necessity for the use of judicial foreclosures in cases where the acquiring mortgagee can no longer obtain the necessary assignments.

In *Kim v. JP Morgan Chase Bank*, ___ Mich. ___ (2012); Mich. S. Ct. Docket 144690 (Dec. 21, 2012), JP Morgan Chase Bank (JPM) foreclosed a mortgage that it acquired from now-closed Washington Mutual Bank (WAMU) pursuant to a purchase and assumption agreement between the FDIC, as receiver, and JPM, by advertisement. Following notice and publication, JPM purchased the property at the sheriff's sale.

The mortgagors filed suit to, among other things, set aside the foreclosure sale, and argued that JPM failed to satisfy the statutory requirements to foreclose by advertisement because it failed to record evidence of its mortgage interest prior to the sale. The trial court disagreed and, relying on a Michigan attorney general opinion, determined that JPM was not required to record its interest before the sale because JPM acquired its interest by operation of law through the FDIC receivership.

The Michigan Court of Appeals reversed and held that there is no exception for a mortgage interest which is acquired by operation of law to the requirements of M.C.L. 600.3204, which states in part:

If the party foreclosing a mortgage by advertisement is not the original mortgagee, a record chain of title shall exist prior to the date of sale under section 3216 evidencing the assignment of the mortgage to the party foreclosing the mortgage.

While the court found that the FDIC succeeded the interests of the failed institution and acquired WAMU's mortgage loans *by operation of law*, JPM simply purchased these mortgage loans after they were transferred to the FDIC. Because JPM failed to record evidence of the assignment of the mortgage and simply relied upon WAMU's place in the chain of title, the appellate court found that JPM failed to comply with the statute's requirements and that the foreclosure sale was void.

In a 4-3 opinion, the Michigan Supreme Court affirmed in part and reversed in part the court of appeals' decision. The Supreme Court agreed that, while the FDIC acquired WAMU's mortgage loans by operation of law, JPM's acquisition was akin to a simple purchase agreement, and that there was no exception to M.C.L. 600.3204 that would allow JPM to avoid recording an assignment or mortgage prior to the foreclosure sale. However, the Supreme Court reversed the court of appeals' decision that found the foreclosure sale void, ruled that the sale was *voidable*, that in order to set aside the sale the mortgagors must demonstrate that they were prejudiced by JPM's failure to record an assignment, and remanded the case to the trial court to determine whether the sale should be set aside.

In his concurring opinion, Justice Stephen J. Markman offered guidance to the trial court on the issue of voidability, indicating that the following non-exhaustive factors may be relevant in determining potential prejudice to the mortgagors: 1) whether the mortgagors were misled into believing that no sale had occurred, 2) whether the mortgagors acted promptly after they became aware of the defect, 3) whether the mortgagors made an effort to redeem the property, 4) whether the mortgagors were represented by counsel throughout the foreclosure process, and 5) whether JPM relied on the apparent validity of the sale by taking steps to protect its interest in the property.

The majority determined that JPM acquired WAMU's mortgage loans pursuant to 12 U.S.C. §1821(d)(2)(G)(i)(II), as explicitly evidenced by an FDIC affidavit, which allows the FDIC to *transfer* the assets and liabilities of a failed institution. The Supreme Court ruled that a transfer pursuant to this section was voluntary, unlike a merger pursuant to §1821(d)(2)(G)(i)(I), and JPM, therefore, did not "step into the shoes" of WAMU; thus, JPM did not take WAMU's place in the record chain of title for foreclosure purposes. While the Supreme Court did not equivocally state so, it strongly suggested, that a mortgagee's acquisition of a mortgage loan from the FDIC via merger under §1821(d)(2)(G)(i)(I) would be an involuntary acquisition which occurred by operation of law, thereby permitting a mortgagee to foreclose without first recording an assignment of mortgage.

While finding that JPM's foreclosure sale violated the statute, the Supreme Court upheld long-standing precedent that a mortgagor must first show prejudice before the sale can be set aside. Taken together, the practical effect of *Kim* still places the onus upon the mortgagor to promptly challenge a foreclosure sale similarly situated. However, it is likely that there are hundreds, if not thousands, of completed Michigan foreclosures with similar facts.

For pending or future foreclosures, where the sale has not yet occurred, the execution and recording of the necessary assignments of mortgage should not be problematic because the acquiring mortgagee should have complete authority to draft and execute all necessary documents to effectuate the transfer of the mortgage loans acquired – as was the case for JPM pursuant to the purchase and assumption agreement. However, in the event that this authority does not exist, the foreclosing mortgagee may likely be required to foreclose judicially, which will result in increased time and expense for the mortgagee.

Rapid Reports are distributed by the firm of Plunkett Cooney. Any questions or comments concerning the matters reported may be addressed to Douglas C. Bernstein or any other members of the practice group. The brevity of this update prevents comprehensive treatment of all legal issues, and the information contained herein should not be taken as legal advice. Advice for specific matters should be sought directly from legal counsel.