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Nationalization of the mortgage lending process: What is being done to fix and prevent the problem?

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In my article last year I discussed the nationalization of the mortgage lending process and its effect on the discharge and cancellation procedures of the paid-off mortgage. The industry's nationalization of loan servicing fueled the tolerance of sloppiness in mortgage discharges.

How does this affect the mortgage discharge in the loan closing process? What is being done to fix and prevent this problem?

Historically, consumers relied on their attorneys and settlement agents to follow-up on the payoff and discharge of a mortgage after settlement. Since the application and issuance of the title policy (insuring the lender or the land owner or both) satisfies the lien satisfaction requirements of most lenders' closing instructions, consumers have had little recourse to obtain the discharge of their prior mortgage lien. If they are insured by an owner's title policy, they have indemnity coverage for the discharge of the covered lien. There is no obligation of the Title Company to affirmatively track the discharge and obtain same in the event the discharge is not of record. There is typically a "requirement" under the binder or commitment for the title insurance policy that the superior (paid-off) lien be discharged before the application of the insurance policy is made. Most title insurance companies issue the policies when the title agent confirms that the payoff lender's cashier's department has accepted payment for the payoff without objection. Many times this is accomplished by review of the bank statements for cashing of the check or acceptance of the payoff wire transfer.

The lack of payoff lenders' statutory compliance and the inconsistencies in mortgage discharge-reconveyance methods among states and courthouses has created an ongoing and costly title problem for consumers, attorneys and settlement agents in tracking and reporting the discharge of property liens. As high as 36% of all real estate transactions have some type of mortgage discharge clean up prior to closing, and as high as 17% of all paid off mortgages remain undischarged of record.

Many times the consumer conveyed his or her property via a general warranty deed - warranting that the property is conveyed free of liens. In circumstances where the prior lender fails to discharge the lien, the consumers are left to turn to the settlement company or settlement attorney for help. The title insurance company under its contract of insurance will not affirmatively obtain the discharge unless there is a claim filed. Even then, the title insurance company many times issues an indemnity agreement to the consumer or the claimant in lieu of affirmatively seeking a discharge instrument.

This practice has created an epidemic problem for consumers and title companies - all at the failure of lenders or servicers in complying with the state statute to discharge the lien. As a result, consumers are left with delayed closings, loss loan locks, lost sales and other direct damages that result from the failure of the discharge to appear of record. Ultimately, title companies are burdened

with the task of lien clean-up many years after a transaction has been closed. Typically the payoff lender or servicer is either out of business or has merged or sold its servicing rights to other lenders creating title defects and clouds.

So, what is being done to fix this problem? Historically, indemnification of any prior undischarged lien was the practice in the title industry. Indemnification sends shivers up the spine of most underwriting counsel I know. Now we are seeing new legislation and private discharge tracking services coming to the rescue.

Almost every year a new set of laws is being proposed and in some cases passed to create uniformity in the mortgage discharge process. Legislators are turning to the URMSA (the Uniform Residential Mortgage Satisfaction Act) to pattern their State's laws. This act is similar to the UCC (Uniform Commercial Code) that has provided uniformity in laws involving commercial transactions. The Act follows this flow:

1. Pre-closing: Request payoff (same method as always, but in writing);
2. At closing: Lender's written payoff (max 10 days), mortgage/deed of trust specific;
3. At least 30 days post closing: Follow up notice to lender that, if cancellation or discharge is not filed within the next 30 days, the proposed statute provides for (a) penalties, actual loss, costs or (b) self-help satisfaction or (c) both;
4. More than 30 days following follow-up notice: If no objection by lender (i.e. not paid in full or other cause) to self-help notice above, self-help satisfaction allowed by satisfaction agent. If lender objects erroneously or has not yet cancelled the mortgage/deed of trust, lender is liable for actual loss, costs, damages due to detrimental reliance, and penalties attach if paid in reliance on written payoff statement. This pattern has set at least a benchmark for legislators to formulate their mortgage discharge laws.

Private companies have also provided post-closing discharge tracking services that operate as a complementary post-closing service, separately contracted by the owner of the property and performed after the closing, recording and disbursement of the transaction. The service is designed to police and enforce the paid-off lender's duty to discharge trust deeds or mortgages when fully paid. Typically, the procedures and services associated with the fee charged to the obligor are not a requirement to satisfy the conditions in a title insurance commitment, nor are they duplicative of services provided by the policy of title insurance issued.

It is also important to remember that the duty to discharge the lien from the property is statutory in nature and not a part of the settlement (escrow) contract between the obligor (Seller or Owner of the subject property) and the settlement attorney/agent acting either in a settlement and disbursement capacity or as agent of the underwriter and issuer of the title policy.

It is nice to see that private companies and State legislators are addressing this often ignored problem. There is a great deal left to be done, but we are on our way toward a real estate closing process void of mortgage discharge defects.

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