

ENABLED BY LENDERS, EMBRACED BY BORROWERS, ENFORCED BY THE COURTS: WHAT YOU NEED TO KNOW ABOUT ENOTES

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I. PURPOSE OF THE WHITE PAPER²

Over the past 30 years, the residential mortgage lending industry has largely transitioned to electronic systems for managing documents related to the origination and servicing of residential mortgage loans. These digitization efforts have, however, been primarily focused on using scanned images of paper documents. The mortgage industry now is poised to truly move towards the digital transformation of the full mortgage loan, including all segments of the mortgage lifecycle including application and initial disclosure delivery, closing, notarization, recording and securitization.

As part of this evolution, paper-based negotiable promissory notes are being replaced with the electronic equivalent of a promissory note—otherwise known as an “eNote.” As discussed more fully herein, “eNotes” are what would otherwise be a negotiable promissory note under UCC Article 3, but in the form of an electronic record.

eNotes confer clear and demonstrated benefits on both the mortgage industry and consumers through improved convenience, quality control and transaction speed. Among other benefits, an eNote:

- May be transferred from one holder to another nearly instantaneously;
- Is less expensive to create and transmit than a paper promissory note;
- May be effectively protected against undetected alteration; and
- If managed in a properly designed information processing system, eliminates uncertainty concerning the identity of the current person entitled to enforce the eNote, and when that person first became entitled to enforce.

Despite these clear benefits, eNote adoption by the mortgage industry has been hampered by uncertainty and misunderstanding of the legal rules applicable to the creation, enforceability and transferability of eNotes. The purpose of this White Paper is to review the legal foundation for eNotes and the industry infrastructure supporting eNotes that is now in place, with the goal of dispelling doubts and misleading views about the value and legal standing of eNotes.

II. BACKGROUND

The legality of eNotes was established with the enactment of the federal Electronic Signatures in Global and National Commerce Act (“ESIGN”)³ and the Uniform Electronic Transactions Act (“UETA”)⁴ over 17 years ago (collectively, “eCommerce Laws”). The eCommerce Laws create legal validity on a nationwide basis for the use of eNotes.⁵ The eCommerce Laws also establish a structure for transferring the right to enforce an eNote from the original lender to subsequent purchasers, free of intervening claims to an interest in the eNote.

The eCommerce Laws accomplish this by replacing the requirements for “possession” and “indorsement” of a written or paper promissory note with the concepts of “control” and “transfer of control” for an eNote.⁶ At a high level, the combination of the legal framework and the mortgage industry-standard for establishing and maintaining “control” requires that the eNote be electronically created, signed and secured, and then registered with a registry owned and operated by MERSCORP Holdings, Inc. (the “MERS[®] eRegistry”) showing the original lender named in the eNote as the party with initial “control” of the eNote (the “Controller”) and the location of the eNote (that is where the eNote is being stored). After registration, all subsequent transfers of “control” from one party to another must be properly recorded on the MERS[®] eRegistry, so that the MERS[®] eRegistry identifies the current party in “control” – i.e., the current transferee. With respect to location of the eNote, the eNote is stored and maintained by the lender in what is typically referred to as an “eVault.” The lender must be prepared to demonstrate that the eNote, while in the lender’s “control,” has not been impermissibly altered since it was signed, thus the eVault must have the proper controls in place⁷ to maintain a definitive copy of the eNote, otherwise referred to as the “authoritative copy”. Thus, the eVault is an important component to enforceability.

While the eCommerce laws establish the legal framework and the courts have upheld the enforceability of eNotes (see Part IX below), some practitioners and industry participants continue to express concern over (1) whether, or with what difficulty, the party in control of an eNote will be able to enforce the eNote against the borrower in the event of a dispute; and (2) the priority of the claim held by a transferee receiving control of an eNote as against other potential claimants to an interest in the eNote, and the extent to which that priority exists even though the transferee does not receive physical possession of an “original” promissory note.

This White Paper addresses these two areas of concern by examining the following topics:

- The legal framework for paper negotiable promissory notes;
- The revised legal framework that establishes the validity of an eNote;
- The mortgage industry infrastructure established to support eNotes;
- The process for creating and transferring ownership of eNotes;
- Post-closing; the role of the document custodian for eNotes;
- Introduction of eNotes into evidence;
- The existing reported judicial decisions concerning eNotes; and
- The legal foundations for converting eNotes into original paper promissory notes.

III. PRE-EXISTING LEGAL FRAMEWORK FOR PAPER NEGOTIABLE PROMISSORY NOTES

In the United States, the obligation to repay a purchase-money loan for a residence has traditionally been evidenced by a paper negotiable promissory note. This promissory note is a written document signed by the borrower and delivered to the lender. It is a common practice in the residential mortgage lending industry for the original lender to sell the debt obligation evidenced by the note to an investor. The use of negotiable promissory notes simplifies and streamlines the purchase-and-sale transaction because delivery of the original written note, together with a signed statement of transfer written or stamped on the note itself (called an

“indorsement”), to a good-faith purchaser for value has been sufficient to establish the transferee’s right to both:

- Enforce the note against the borrower free of most defenses arising because of the actions of prior owners of the note, and
- Take ownership of the note free of the claims of other persons to an ownership interest in the Note for one reason or another.

As the industry moved to substitute eNotes for paper promissory notes, a new process to replace the physical delivery of possession and indorsement of an “original” paper promissory note needed to be created. Article 3 alone would not support a promissory note executed as an electronic record.

To address this issue, the provisions of UETA and subsequently ESIGN were intentionally drafted to enable the electronic equivalent of a negotiable promissory note, substituting a process for establishing, and recording transfers of, “control” as the equivalent of possession and indorsement.⁸ How the eCommerce Laws accomplish this is discussed below.

IV. REVISED LEGAL FRAMEWORK THAT PERMITS ENOTES TO REPLACE PAPER NEGOTIABLE PROMISSORY NOTES

As noted above, ESIGN and UETA both define and provide for the creation and existence of an eNote. The eCommerce laws technical term for the eNote is a “transferable record” (“Transferable Record”).⁹ The eCommerce Laws provide that a Transferable Record created in conformity with their requirements is the functional equivalent of a paper negotiable promissory note and is just as enforceable against the borrower as its written counterpart.

The sections of the eCommerce Laws governing Transferable Records establish the conditions that must be met for an eNote to serve as the equivalent of a negotiable paper promissory note. In order to qualify as a Transferable Record at the time of creation and issuance, an eNote must be electronically created, presented to the borrower and executed entirely on information processing systems.¹⁰ Further:

- The eNote must otherwise qualify as a negotiable promissory note under Article 3 if it were in writing.
- The issuer (the borrower) must expressly agree that the instrument is a Transferable Record.¹¹
- In order to obtain equivalent treatment as a negotiable promissory note:
 - The eNote must be signed; and
 - The method used to record, register, or evidence a transfer of interests in the eNote must reliably establish the identity of the person entitled to “control” the eNote (“Control” or “Controller”).¹²

Once these criteria are met, the person identified as the Controller obtains rights equivalent to those granted a holder of a paper promissory note, which includes the right to enforce the eNote.¹³ The Controller can either be the owner of the eNote, a person entitled to ownership (i.e., a beneficial owner), or a person entitled to enforce the eNote. Being the Controller therefore

means having the right to enforce the eNote against the borrower and transfer the eNote to a third party, with the third party transferee becoming the new Controller.

The eCommerce Laws provide a safe harbor for satisfying the rules establishing Control (“Safe Harbor”).¹⁴ Under the Safe Harbor provisions, the Transferable Record must be created, stored, and assigned so that the following conditions are met:

- A single authoritative copy of the record exists that is unique, identifiable,¹⁵ and (except for permitted revisions under UETA), unalterable;¹⁶
- The authoritative copy identifies the person asserting control as either the person to whom the Transferable Record was issued or the person to whom the Transferable Record was most recently transferred;¹⁷
- The authoritative copy is communicated to and maintained by the person asserting control or his designated custodian;¹⁸
- Copies or revisions that add or change an identified assignee of the authoritative copy can be made only with the consent of the person asserting control;¹⁹
- Each copy of the authoritative copy and any copy of a copy is readily identifiable as a copy that is not the authoritative copy;²⁰ and
- Any revision of the authoritative copy is readily identifiable as an authorized or unauthorized revision.²¹

The general rule that Control exists can also be met if the Controller’s identity may be reliably established by the method used to manage transfers of interests. Significantly, the courts to date have used this general rule.²²

V. THE MORTGAGE INDUSTRY INFRASTRUCTURE SUPPORTING ENOTES

The first practical guide for compliance with the eCommerce Law’s Transferable Record rule was published by Freddie Mac in 2005 and described in detail the obligations of loan originators hoping to sell residential mortgage loans evidenced by eNotes.²³ At roughly the same time, Fannie Mae and Freddie Mac (collectively, the “GSEs”) added special language to the Uniform Instruments²⁴ to address the use of eNotes (“Uniform Instrument eNote Provisions”).²⁵ Mortgage loan originators originating eNotes are required to include this language in eNotes tendered for sale to the GSEs.²⁶

As a natural outgrowth of MERSCORP Holdings, Inc (“MERSCORP”) services,²⁷ MERSCORP developed the MERS[®] eRegistry in cooperation with a number of mortgage industry stakeholders who supported the effort. The MERS[®] eRegistry quickly became the industry-standard system of record for identifying the current Controller and location of the eNotes. While there is no provision in the eCommerce Laws that *mandates* the use of a centralized electronic registry, a registry system such as the MERS[®] eRegistry was expressly contemplated by the drafters of UETA and has maintained industry backing for over a decade.²⁸

The MERS[®] eRegistry does not store the actual eNote, but instead only stores and tracks identifying information about it, including the eNote’s digital fingerprint,²⁹ the name of the

Controller and the location of the eNote. The authoritative copies of the eNotes themselves are stored in an eVault.³⁰

Because any electronic copy of an eNote is identical to any other copy—since they are simply bit-for-bit copies of computer files—no one copy of an eNote can contain data that would identify it as the authoritative copy.³¹ Therefore, some external mechanism is required to resolve the question of which of the copies of an eNote is the authoritative copy. The MERS[®] eRegistry allows eNotes to be registered and uniquely identified for tracking and verification.³²

In this environment, determination of the eNote's Controller and the right to designate the location of the authoritative copy of eNote are determined solely by reference to the MERS[®] eRegistry. The primary preconditions for the MERS[®] eRegistry to perform its registration function, and support compliance with the Safe Harbor if so desired, are:

- Each eNote contains language placing anyone viewing it on notice that its true Controller must be determined by reference to the central registry,³³ and states that the authoritative copy is identified through the MERS[®] eRegistry.
- The centralized registry (a) stores the digital fingerprint; (b) identifies the Controller, and (c) references the location of the eNote's current authoritative copy.³⁴
- A transfer of control is accomplished by receipt of a secure authorization to transfer from the current Controller to the new Controller.³⁵

Beyond use of the MERS[®] eRegistry, the Controller's obligations include establishing the terms of the eNote, effectively presenting the eNote for execution, obtaining enforceable signatures, and managing the executed eNotes while the debt is outstanding—all in compliance with underlying law and the certain procedural requirements set forth in ESIGN and UETA. As such:

- The relationship between MERSCORP and the Controller is interdependent; and
- As it stands today, the function of the MERS[®] eRegistry is separate and distinct from the other functions undertaken by the Controller (and any designated custodian) to satisfy eCommerce Laws general rule for establishing Control, and (when desired) complying with the Safe Harbor.

VI. THE PROCESS FOR CREATING AND TRANSFERRING CONTROL OF eNOTES

The creation of an eNote begins with the loan document origination system used by the original lender. The system holds templates for the various documents used in the closing process. The templates contain all the standard language used in the closing documents, as well as placeholders, or "fields", for the variable data that is added to represent the details relevant to the specific loan—such as interest rate, principal amount of the loan, and so forth. The templates also have fields indicating where the various participants in the closing are supposed to supply initials or signatures on the documents. The closing package for the loan is created and data specific to the loan is added to the templates.

The template for the eNote will usually be one of the Uniform Instruments. If the Uniform Instrument is going to be electronically signed and managed as an eNote, as noted above,

guidance from the GSEs calls for the Uniform Instrument eNote Provision to be added to the document.³⁶

As part of the closing process, the eNote will be assigned the same Mortgage Identification Number (“MIN”) as used for its corresponding underlying mortgage registered on the MERS[®] System. After signing the eNote, along with a cryptographic hash of its contents, i.e., the digital fingerprint of the eNote, the eNote will be registered with the MERS[®] eRegistry under its MIN, together with the location of the authoritative copy and the identity of the originating lender, who is listed as the party in Control of the eNote and its authoritative copy.

Thereafter, each transfer of control is also recorded in the MERS[®] eRegistry. A transfer of control requires the participation of both the transferor and the transferee. The transferor must initiate the transfer and the transferee must accept it. The transferee is then able to specify the new location of the authoritative copy. In this manner, it is possible to identify the person currently in control of an eNote and the eNotes location by consulting the MERS[®] eRegistry.

VII. POST-CLOSING MANAGEMENT; THE ROLE OF THE DOCUMENT CUSTODIAN

Traditionally, the role of a document custodian is to act as a legal fiduciary designated to administer the safekeeping of the paper promissory note. eNotes are now also maintained by a document custodian in the controlled system commonly referred to as an “eVault.” Some Controllers utilize third-party services to maintain the eVault, and some operate the eVault software platform within their own internal data processing services. The software solutions used to maintain and identify the current authoritative copy of the eNote, and also maintain its integrity as a business record eligible for admission under the Rules of Evidence, are integrated into the eVault.³⁷ Responsibility for the management and integrity of the eVaults rests with the party in Control of the eNote.

As noted above, the use of a registry system for identifying the party in Control of an eNote was expressly contemplated by the drafters of the UETA.³⁸ Because the language of each eNote itself points to the MERS[®] eRegistry, any person reviewing a copy of the eNote is on inquiry notice that the MERS[®] eRegistry must be consulted to identify the current Controller. The use of the MERS[®] eRegistry to identify the location of the authoritative copy works in much the same way—a person reviewing any copy of the eNote is on notice that the location of the authoritative copy is established by the MERS[®] eRegistry. If the copy they are reviewing is not the copy in the location specified in the MERS[®] eRegistry by the registered digital fingerprint, then it is not the authoritative copy. In this way, every copy of the authoritative copy should be regarded as “readily identifiable.”³⁹

VIII. INTRODUCTION OF ENOTES INTO EVIDENCE

A number of laws determine whether an eNote is admissible into evidence: UETA or E-SIGN, the Federal Rules of Evidence (in federal cases), the Uniform Rules of Evidence (adopted in many states) (collectively, the “Rules of Evidence”) and the Business Records Act. Read together, and properly applied, the eCommerce Laws, the Rules of Evidence and the Business Records Act allow for both the admissibility of the eNotes themselves into evidence, as well as the records attendant to the systems of record for storing and tracking transfers of eNotes.

a. UETA AND ESIGN

UETA authorizes retaining a record in electronic form, so long as the electronic record continues to accurately reflect the information set forth in the record after it is generated in its final form, and remains accessible for later reference.⁴⁰ ESIGN has an equivalent provision.⁴¹ UETA also expressly states that electronic records are admissible in evidence. Specifically, Section 13 of UETA states that in a proceeding, “evidence of a record or signature may not be excluded solely because it is in electronic form.” Consequently, an eNote and related electronic records are entitled to treatment under the same evidentiary standards as other records in a state or federal court.

b. FEDERAL AND UNIFORM RULES OF EVIDENCE

The Rules of Evidence contain two rules that, taken together, impact electronic records admissibility into evidence: the “Business Record” Rule⁴² and the “Best Evidence” Rule.⁴³

i. BUSINESS RECORDS RULE

The Rules of Evidence generally exclude the admission of “hearsay” evidence in court unless the evidence falls within certain exceptions. Hearsay is defined as an oral or written statement, other than one made by the declarant while testifying, offered in evidence to prove the truth of the matter asserted.⁴⁴ Business records that are submitted in proceedings to prove the truth of documented matters (*e.g.* “this is what the security instrument said when the borrower signed it” or “the security instrument was filed of record in Broward County, Florida, on date X at time Y”) constitute hearsay.⁴⁵ However, the Rules of Evidence permit the introduction of business records of regularly conducted business activity. A business record will be admissible:

- If it is a record, *in any form*, of acts, events, conditions, opinions, or diagnoses, made at or near the time by, *or from information transmitted by*, a person with knowledge;
- If the record is kept in the course of a regularly conducted business activity;
- If it was a regular practice of that business activity to make the record, all as shown by the testimony of the custodian or other qualified witness, or by certification that complies with the Rules of Evidence;
- Unless the source of information or the method or circumstances of preparation indicate the record is not trustworthy.⁴⁶

Electronic records prepared by third parties and incorporated into business records are also admissible if the incorporating business relied upon them, and there are other indications of trustworthiness.⁴⁷ To the extent that a person relies upon third party documents in the ordinary course of its business and creates and maintains them in a manner that ensures that they are both accurate and accessible, electronic records may qualify as a business record admissible under the business records exception to the hearsay rule, absent any other indication that the record is not trustworthy.⁴⁸

ii. THE BEST EVIDENCE RULE

Even if an electronic record is admissible under the business records exception to the hearsay rule, it must also satisfy the Best Evidence Rule. The Best Evidence Rule as set forth in the Federal Rules of Evidence, sometimes called the “Original Writing Rule,” provides that “[a]n original writing, recording, or photograph is required in order to prove its content unless these rules or a federal statute provides otherwise.”⁴⁹ An “original” is defined in the Federal Rules of Evidence as:

An “original” of a writing or recording means the writing or recording itself or any counterpart intended to have the same effect by the person who executed or issued it. *For electronically stored information, “original” means any printout — or other output readable by sight — if it accurately reflects the information.*”⁵⁰

A printout of an electronic record stored in a computer or similar device, including a scanned document, should therefore be regarded as an “original” of the electronic record, so long as the electronic record storage system is demonstrated to accurately store and protect the source record.⁵¹

Once admissibility of the electronic record is established through the business records rule, the Best Evidence Rule would permit introduction of a printed copy of that electronic record.

The key is evidence of data integrity. To date, the few court decisions focusing on the introduction of electronic records, or copies of such records, have emphasized the systemic protections—division of labor, complexity of backup systems, activity logs or audit trails, use of digital fingerprints to verify content—which make it difficult to counterfeit or other alter a record without leaving a discoverable trail.⁵²

c. BUSINESS RECORDS ACT

The Business Records Act permits business records that are reproduced to be admitted, as long as they are satisfactorily identified, even if the original is no longer in existence and the reproduction is accurate.⁵³ Specifically, the act provides:

If any business, institution, member of a profession or calling, or any department or agency of government, in the regular course of business or activity has kept or recorded any memorandum, writing, entry, print, representation or combination thereof, of any act, transaction, occurrence, or event, and in the regular course of business has caused any or all of the same to be recorded, copied, or reproduced by any photographic, photostatic, microfilm, micro-card, miniature photographic, or other process which accurately reproduces or forms a durable medium for so reproducing the original, the original may be destroyed in the regular course of business unless its preservation is required by law. Such reproduction, when satisfactorily identified, is as admissible in evidence as the original itself in any judicial or administrative proceeding whether the original is in existence or not and an enlargement or facsimile of such reproduction is likewise admissible in evidence if the original reproduction is in existence and available for inspection under direction of court. The introduction of a reproduced record, enlargement,

or facsimile does not preclude admission of the original. This subsection shall not be construed to exclude from evidence any document or copy thereof which is otherwise admissible under the rules of evidence.⁵⁴

The Uniform Photographic Copies of Business and Public Records as Evidence Act (the “UPCBPREA”), which has also been adopted by a number of states, contains provisions very similar to the foregoing provision of the Business Records Act. Specifically, the UPCBPREA states that a reproduction made by any “process which accurately reproduces or forms a durable medium for reproducing the original . . . is admissible in evidence as the original itself. . . .”⁵⁵

IX. WHAT THE COURTS HAVE SAID ABOUT ENOTES

There are a few reported appellate decisions in the eNote enforcement area. The first reported decision offered guidance on the evidence required to establish the party in Control of an eNote. Two later decisions, building on that guidance, have determined that the Controller has established Control, and found that the Controller has the right to enforce the eNote.

*Good v. Wells Fargo*⁵⁶ is the first reported decision to directly address ownership and enforcement of an eNote. In *Good*, Wells Fargo sought to enforce a debt evidenced by an eNote governed by the provisions of ESIGN (because the eNote was secured by real property) and registered on the MERS[®] eRegistry.⁵⁷ Wells Fargo was not the original lender, and instead received the mortgage by assignment. Wells Fargo moved for summary judgment. However, the affidavits supporting Wells Fargo’s motion did not provide any evidence on the question of “control.” The district court granted Wells Fargo partial summary judgment, finding that Wells Fargo had standing to enforce the promissory note. The debtor appealed.

The Indiana Court of Appeals reversed and remanded for further proceedings. The court held that because the eNote was secured by real property, issues related to “control” were governed by ESIGN. The court went on to find that in order to enforce the eNote, Wells Fargo needed to show that it controlled the eNote (referred to by the court as the “Note”) as of the date the foreclosure action was filed, and had not done so because it had failed to present any evidence supporting its claim to control. The court observed that under the terms of the eNote itself, control and location of the authoritative copy were to be determined by reference to a note holder registry, and that Wells Fargo had not provided any evidence of entries in a note holder registry establishing that it was the party in control.⁵⁸

However, the Court also held that Wells Fargo was correct that pursuant to ESIGN, “a person having control of a transferable record, which includes the Note, is the holder for purposes of the UCC and that delivery, possession, and endorsement are not required...[and] to show it controlled the note, Wells Fargo was required to designate evidence that a system employed for evidencing the transfer of interests in the Note reliably established Wells Fargo as the person to whom the Note was transferred.”⁵⁹

The court indicated that if Wells Fargo could establish on remand that (i) it held the authoritative copy, and (ii) the transfer of control to Wells Fargo on the MERS[®] eRegistry occurred prior to the date the foreclosure suit was filed (as required by the terms of the Note itself), Wells Fargo

would have the same rights as a holder under UCC Article 3 and would be entitled to enforce the note on that basis.⁶⁰

Two later reported decisions pick up where the *Good* decision leaves off, and confirm its view of the requirements for establishing control and the rights of the controller. On April 13, 2015, a New York appellate court, in *New York Community Bank v. McClendon*, issued an opinion reversing a lower court order dismissing a foreclosure action against a borrower who signed an eNote.⁶¹ In the proceedings below, the lower court had granted the borrower's motion to dismiss because the plaintiff could not produce a chain of valid assignments of the eNote from the original lender to itself. However, the mortgagee had submitted in evidence a copy of the eNote and a print out of an electronic record of the transfer history of the eNote on the MERS[®] eRegistry showing a chain of transfers from the original lender to itself. The appellate court concluded that the transfer history, together with the eNote, were sufficient to establish that the plaintiff mortgagee had control of the eNote under E-SIGN and therefore had standing to foreclose as the holder.

In the second case, a Florida court of appeals issued an opinion in *Rivera v. Wells Fargo Bank, N.A.* affirming a lower court's judgment in favor of a bank in a foreclosure action against borrowers who signed an eNote.⁶² In the proceedings below, the bank had presented a sworn certificate of authentication which articulated, among other things, the Bank's role as servicer of the eNote for Fannie Mae, and described the Bank's practices and systems used for the receipt and storage of authoritative copies of electronic records and for protecting electronic records against alteration. The Bank also provided evidence from the same system records, and the records of the MERS[®] eRegistry showing that the eNote was last transferred to Fannie Mae and that the authoritative copy of the eNote was maintained in the Bank's systems as Fannie Mae's custodian. On appeal, the borrowers challenged the adequacy of the bank's demonstration that the eNote had properly transferred to Fannie Mae. Applying the Florida enactment of the UETA and relying on the evidence provided in the certificate of authentication, the court held that the bank presented competent evidence proving that Fannie Mae owned the eNote and had authorized the bank to pursue the foreclosure.⁶³

X. CONVERTIBILITY OF AN ENOTE TO A PAPER ORIGINAL

a. REASON AND BASIS FOR CONVERTIBILITY

From time to time, a person in Control of an eNote may want to convert the record into a paper promissory note for ease of transfer. The conversion of the eNote into the form of a paper original permits it to be transferred as a negotiable instrument to a party without the infrastructure or procedures in place to act as a Controller (a "Paper Original").

b. PROCESS AND LEGAL SUFFICIENCY

As part of the initial creation and signature process, the borrower adopts his or her signature with the intent to sign the eNote. If the eNote contains the Uniform Instrument eNote Provision,⁶⁴ then the borrower has agreed that (1) the holder of the note may convert the electronic record into a Paper Original, (2) the electronic signing and delivery of the Record also constitutes signing and delivery of the Paper Original, (3) the electronic signature(s) associated with the

electronic record, when evidenced on the Paper Original, constitutes a legally valid and binding signature(s), and (4) the borrower's obligations will be evidenced by the Paper Original after such conversion. In that case, by associating his or her signature to the eNote at the time of the initial signing, the borrower has also agreed and demonstrated his or her consent, pre-conversion, to the representation of the electronic signature as a graphic signature on the Paper Original.⁶⁵

Additional processes to complete the conversion include, among others, deactivating the eNote in the eVault, noting the new status on the MERS[®] eRegistry, and attaching a schedule of any prior transfers of control as an equivalent to indorsement.⁶⁶

XI. CONCLUSION

There is a solid and judicially tested legal framework to support the creation, transfer and enforcement of eNotes. The MERS[®] eRegistry, together with the platform(s) utilized by lenders to create and manage eNotes, are in place today and provide a robust industry infrastructure supporting protection of the integrity of eNotes and evidence of control. In some respects, this widely-supported infrastructure offers more controls and better risk management options than historical paper-based systems, by providing evidence of key lifecycle events for the eNote and a reliable history and digital audit trail reflecting the eNote's creation and ownership.

The benefits of eNotes to both the mortgage industry and borrowers are readily apparent. The way is now clear for mortgage lenders to take the final steps on the long path to a fully digital mortgage lending process.

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² This White Paper was prepared at the request of MERSCORP Holdings, Inc. It is not intended as legal advice and cannot be relied upon by any third party as such.

³ ELECTRONIC SIGNATURE IN GLOBAL AND NATIONAL COMMERCE ACT, Pub. L. No. 106-229, 114 STAT. 464 (codified at 15 U.S.C. §§7001-31). ESIGN creates legal certainty that the use of electronic signatures and records under most state and federal laws will be enforced to the same extent as a paper record or signature that the electronic version replaces. ESIGN became effective on October 1, 2000.

⁴ OFFICIAL TEXT OF THE UNIFORM ELECTRONIC TRANSACTIONS ACT (Nat'l Conf. of Comm'rs On Unif. State L. 1999). The UETA provides a set of uniform rules for adoption by the states, which would establish the equivalence of an electronic record or signature to a traditional paper record or signature that the electronic version replaces. With the exception of Illinois, New York, and Washington, every state, as well as the District of Columbia and the U.S. Virgin Islands, has adopted a variation of UETA. Illinois, New York, and Washington each have their own unique alternative statutes to address electronic commerce. ESIGN gives states limited authority to "modify, limit or supersede" 15 U.S.C. 7001 (which contains the Act's provisions giving legal recognition to the use of electronic

records and signatures) by adopting the official text of the UETA or another law that is consistent with the substantive provisions of ESIGN. 15 U.S.C. 7002. Note that this “reverse preemption” rule does not apply to ESIGN’s provisions governing eNotes at 15 U.S.C. 7021.

⁵ See CASE CLOSED: eNOTES ARE LEGAL, AN ANALYSIS OF eNOTE ENFORCEABILITY NATIONWIDE, jointly published by the Mortgage Industry Standards Maintenance Organization, the Electronic Records and Signatures Association, and the American Land Title Association (2008), available at https://www.pria.us/files/resource_library_files/eRecording_eXcellence/eNoteWhitePaper.pdf (last visited August 10, 2017).

⁶ See Section IV *infra* for a discussion of “control”; See also, JEREMIAH S. BUCKLEY. BUCKLEY, MARGO H. K. TANK, R. DAVID WHITAKER & JOHN P. KROMER, THE LAW OF ELECTRONIC SIGNATURES, 2017 Edition, Thomson Reuters (2017), Section 11:4.

⁷ *Id.*

⁸ See Reporter’s Comments to UETA § 16.

⁹ UETA § 16. ESIGN §201 (codified at 15 USC § 7021). The definition of Transferable Record in ESIGN was modeled on the definition in the UETA, but is limited to electronic records that evidence a loan secured by real property.

¹⁰ The Reporter’s Comments to the UETA specifically state that a Transferable Record must, by definition, be electronic at the time it is issued. A Transferable Record cannot be created by scanning or otherwise converting a signed paper original to electronic form. See UETA § 16 cmt. 2.

¹¹ Legally, the agreement to treat the electronic record as a Transferable Record may be placed either in the Transferable Record itself, or in a separate record. As a practical matter, however, placing the agreement in a separate record will create complications in transferring the rights. For example, how will the transferee know that the transferred record has been issued subject to the required agreement?

¹² UETA § 16.

¹³ UETA § 16(d); UCC Article 3, §3-301 The Controller must also meet the other statutory criteria otherwise applicable under Article 3 of the Uniform Commercial Code, other than possession or indorsement, to obtain the same rights as a holder or holder in due course.

¹⁴ UETA §16 cmt. 3.

¹⁵ For example, the record management system used to store the electronic record may use location indexing to identify a specific copy of the electronic record as the unique, authoritative copy. By definition, all copies not held at the indexed location are not the authoritative copy.

¹⁶ For example, there are a variety of encryption techniques and processes available to prevent undetected alteration to an electronic record. Note that as used in the Safe Harbor, the term “unalterable” should not be taken too literally. Practically speaking, no record is unalterable. Ordinary writings may be altered, and so may almost any type of electronic record. All records are also subject over time to decay and deterioration. The requirement that a Transferable Record be unalterable is also modified by UETA §16(c)(6) and ESIGN §201(c)(6), which permits revisions that are readily identified as authorized or unauthorized. In other words, UETA does not require that a Transferable Record be unalterable in a metaphysical sense, but only that it be unalterable without detection.

¹⁷ The framework adopted by the mortgage industry accomplishes this by establishing a registry (discussed in more detail below) and placing a reference to the registry in the eNote itself, instructing interested parties to consult the registry to determine the current Controller. Under the terms of the eNote, a change in control is only effective when it is recorded in the registry. The registry, in turn, requires every transfer of control to be initiated by the Controller or the Controller’s authorized representative.

¹⁸ For example, the current party in control may designate a custodian to hold the authoritative copy.

¹⁹ See note 17, *supra*.

²⁰ There are multiple strategies for accomplishing this, including storing the authoritative copy in an indexed location, or watermarking all non-authoritative copies.

²¹ UETA §16(c). Of course, if no post-execution alterations are permitted, then any later alteration to the eNote is, by definition, unauthorized. There are multiple strategies available for determining whether an eNote has been altered post-execution.

²² See Section IX *infra* for a discussion of recent judicial decisions.

²³ FREDDIE MAC, EMORTGAGE HANDBOOK (Version 1.0 2005). Note that as of the date of publication of this White Paper, Freddie Mac no longer publishes the eMortgage Handbook, and instead publishes an eMortgage Guide. See FREDDIE MAC, EMORTGAGE GUIDE (Version 9.0 March 2018).

²⁴ Freddie Mac and Fannie Mae use the term “Uniform Instrument” to refer to forms for promissory notes, mortgages, deeds of trust, and other related documents that are approved for use by both entities.

²⁵ See note 33, *infra*. The terms for the eNote include agreement that it will be treated as a transferable record, that transfers of control will be recorded on an identified registry, and that the location of the authoritative copy will also be specified in the registry.

²⁶ See, e.g., FANNIE MAE, GUIDE TO DELIVERING EMORTGAGE LOANS TO FANNIE MAE (November 1, 2016); FREDDIE MAC, EMORTGAGE GUIDE (Version 9.0 March 2018); FANNIE MAE, SELLING GUIDE: FANNIE MAE SINGLE FAMILY, A2-5.1-04 (April 3, 2018); FREDDIE MAC, SINGLE-FAMILY SELLER/SERVICER GUIDE, Ch. 1401 (March 30, 2018). See also FANNIE MAE, EMORTGAGE TECHNICAL REQUIREMENTS (Version 2.0 January 2018), which contemplates both registration of the eNote on the MERS[®] eRegistry and delivery of the authoritative copy of the eNote to Fannie Mae for vaulting. In the GUIDE TO DELIVERING EMORTGAGE LOANS TO FANNIE MAE, for example, Fannie Mae specifies that a lender selling an eNote to Fannie Mae represents and warrants all of the following:

1. Each eMortgage delivery is evidenced by an eNote that is a valid and enforceable Transferable Record pursuant to the Uniform Electronic Transactions Act (“UETA”), or the Electronic Signatures in Global and National Commerce Act (“eSIGN”), as applicable, and there is no defect with respect to the eNote that would confer upon Fannie Mae, or a subsequent transferor, less than the full rights, benefits and defenses of Control (as defined by UETA and eSIGN) of the Transferable Record;
2. Prior to transfer to Fannie Mae, the lender is an entity entitled to enforce the eMortgage;
3. All electronic signatures associated with the eMortgage are authenticated and authorized;
4. The lender has established procedures and controls limiting access to eMortgage Delivery and the MERS[®] eRegistry to duly authorized individuals, and Fannie Mae is entitled to rely on any transmission, transfer or other communication via these systems to be the authorized act of the lender;
5. Any prior transfers of Control of the eNote are authenticated and authorized;
6. The Authoritative Copy of the eNote has not been altered since it was electronically signed by its issuers;
7. There has been, at all times, one and only one Authoritative Copy of the eNote in existence, and all copies other than the Authoritative Copy are readily identifiable as non-authoritative copies; and
8. The eNote is not subject to a defense, claim of ownership or security interest, or claim in recoupment of any party that can be asserted against the lender.

As an additional example, Freddie Mac requires each seller of loans to Freddie Mac using eNotes and eVaults to perform an initial and annual technical and legal review of the closing system and eVault for compliance with all applicable federal and State laws, including ESIGN and UETA. See FREDDIE MAC, EMORTGAGE GUIDE, Version 9.0, §§2.1.3, 2.1.4 (March 2018).

²⁷ MERSCORP also owns and operates the MERS[®] System which is a national electronic registry system tracking the changes in servicing rights and beneficial ownership interests in residential mortgage loans that are registered on the System. Its subsidiary, Mortgage Electronic Registration Systems, Inc. (“MERS”) serves as the recorded mortgagee as the nominee for promissory note-owners in the land records. See <http://www.mersinc.org/about-us/about-us>.

²⁸ See UETA §16 cmt. 3.

²⁹ A cryptographic hash of the eNote is required to be stored with the MERS[®] eRegistry at the time of registration. This process permits testing to confirm, at any time in the future, that the authoritative copy has not been altered since it was registered on the MERS[®] eRegistry, and is a true and accurate copy of the eNote that was presented for registration.

³⁰ NAT’L ENOTE REGISTRY REQUIREMENTS DOCUMENT (Mar. 7, 2003).

³¹ *Id.*

³² *Id.*

³³ The additional language in the Uniform Instrument eNote Provision required for each eNote by the GSEs includes the following:

I agree that this Electronic Note will be an effective, enforceable and valid Transferable Record ... and may be created, authenticated, stored, transmitted and transferred in a manner

consistent with and permitted by the Transferable Records sections of UETA or E-SIGN ... [T]he identity of the Note Holder and any person to whom this Electronic Note is later transferred will be recorded in a registry maintained by [Insert Name of Operator of Registry here] or in another registry to which the records are later transferred (the “Note Holder Registry”). The Authoritative Copy of this Electronic Note will be the copy identified by the Note Holder after loan closing but prior to registration in the Note Holder Registry. If this Electronic Note has been registered in the Note Holder Registry, then the authoritative copy will be the copy identified by the Note Holder of record in the Note Holder Registry or the Loan Servicer (as defined in the Security Instrument) acting at the direction of the Note Holder, as the authoritative copy.

See FANNIE MAE, GUIDE TO DELIVERING EMORTGAGE LOANS TO FANNIE MAE (November 1, 2016); FREDDIE MAC, EMORTGAGE GUIDE, (Version 9.0 March 2018).

³⁴ Note that the “location spotting” function of the registry could be accomplished in one of two ways – either by specifying the location in the registry, or by providing information on the identity of the custodian holding the authoritative copy and directing the inquiring party to the custodian for further information on the authoritative copy’s precise location.

³⁵ As part of the services available to Controllers, MERSCORP provides, in connection with foreclosure proceedings, affidavits concerning the current Controller reflected in the MERS[®] eRegistry and location of the authoritative copy as reflected in the MERS[®] eRegistry.

³⁶ See note 33, *supra*, for the key language of the Uniform Instrument eNote Provision.

³⁷ The unique characteristic of the authoritative copy of the eNote is established and maintained in the eVault. The authoritative copy is held by the controlling party or its authorized custodian, and is logically associated with a registry entry of the identity of the Controller and the location of the authoritative copy. The registry is referenced in the electronic record itself. Control may only be transferred with the consent of the current controlling party, and the authoritative copy may not be altered, once executed, without detection. 12 U.S.C. § 7021(c)(1), (3)-(6).

³⁸ See UETA § 16 cmt. 3.

³⁹ UETA § 16(c)(6).

⁴⁰ UETA § 8(a).

⁴¹ 15 U.S.C. § 7001(d)(1).

⁴² Fed. R. Evid. 803(6).

⁴³ Fed. R. Evid. 1002.

⁴⁴ Fed. R. Evid. 801.

⁴⁵ Using a contract to prove its terms may not be a hearsay issue. See *Mueller v. Abdnor*, 972 F.2d 931 (8th Cir. 1992) (contract is a verbal act and is not hearsay). However, to the extent it is hearsay, it would be permitted under the business records exception.

⁴⁶ For a general discussion of the steps required to establish a foundation for the admission of electronic business records into evidence, see *Lorraine v. Markel American Insurance Company*, 241 F.R.D. 534 (D. Md. May 4, 2007).

⁴⁷ See, e.g., *Air Land Forwarders, Inc. v. United States*, 172 F.3d 1338 (Fed. Cir. 1999).

⁴⁸ In addition, it may also be permitted by the FRE Section 803(14) which applies to documents affecting an interest in property. Note, however, that if a record contains multiple layers of hearsay (e.g., is double hearsay), it may not be considered to be admissible evidence unless the record completely fits one or more exemptions to the hearsay rule.

⁴⁹ Fed. R. Evid. 1002.

⁵⁰ Fed. R. Evid. 1001(d) [emphasis added].

⁵¹ See *United States v. Nixon*, 694 F.3d 623, 635 (6th Cir. 2012) (“[T]he simple act of printing out the electronically stored records does not change their status for admissibility.”); *Vining v. State Farm Life Ins. Co.*, 409 So. 2d 1306, 1311 (La. Ct. App. 1982) (“[T]here is no question but that computer printouts are admissible in evidence in this state when the proper foundation is laid for their admission.”); *King v. State of Miss. (Miss.)*, 222 So 2d 393, 398 (1969) (“Records stored on magnetic tape by data processing machines are unavailable and useless except by means of the printout sheets such as those admitted to evidence in this case.”). See also William A. Fenwick, Gordon K. Davidson, *Admissibility of Computerized Business Records*, 14 AM. JUR. PROOF OF FACTS 2D § 17 (1997 & Supp. 2001), superseded by Catherine Palo, *Admissibility of Computerized Business Records*, 155 AM. JUR. PROOF OF FACTS 3D 455 (2017). (“The most common reason that courts have rejected computerized evidence is that an insufficient foundation was laid to show the accuracy and trustworthiness of the evidence.”)

⁵² See, e.g., *United States v. Greenlee*, 380 F. Supp. 652 (E.D. Pa. 1974), aff'd 517 F.2d 899 (3d Cir. 1975), cert. denied, 423 U.S. 985 (1975); *Transp. Indem. Co. v. Seib*, 132 N.W.2d 871 (1965). See also *In re Vinhnee v. American Express*, 336 B.R. 437 (B.A.P 9th Cir. 2005) (Focusing on computer policy and system control procedures, including control of access to the database, control of access to the program, recording and logging of changes, backup practices, and audit procedures to assure the continuing integrity of the records).

⁵³ 28 U.S.C. § 1732. It is worth noting that the Act has been in place since 1948, and was last amended in 1975. Almost all the significant cases interpreting the Act were decided before 1972.

⁵⁴ *Id.*

⁵⁵ OFFICIAL TEXT OF THE UNIFORM PHOTOGRAPHIC COPIES OF BUSINESS AND PUBLIC RECORDS AS EVIDENCE ACT (Nat'l Conf. of Comm'rs On Unif. State L. 1949), Section 1.

⁵⁶ *Good v. Wells Fargo Bank, N.A.*, No. 20A03-1401-MF-14, Ind. Gov. Jud. Op. (Ind. Ct. App. Sept. 1, 2014), <http://www.in.gov/judiciary/opinions/pdf/09291401mpb.pdf>.

⁵⁷ While a complete discussion of the doctrine of federal preemption is beyond the scope of this White Paper, it is likely that ESIGN preempts the UETA, with respect to the rules related to establishing control, when the eNote is secured by real property. See 15 U.S.C. §7002 and 7021. A state may supersede the provisions of § 7001 of ESIGN by adopting the Official Text of the UETA – the transferable record provisions of ESIGN are in § 7021, and are not affected by the state adoption of the UETA.

⁵⁸ More recently, two other courts have emphasized, in interim orders, that the plaintiff bringing a foreclosure action on an eNote must present competent evidence that the plaintiff was in control of the eNote on the date the action was filed. See *Wells Fargo Bank, N.A. v. Benitez*, No. 13-15433, 2016 NY Slip Op 32564(U) (2016) (Plaintiff seeking to enforce an eNote must provide evidence that a system employed for evidencing the transfer of interests in the eNote reliably establishes that control has been transferred to the Plaintiff); See also *The Bank of New York Mellon Trust Company, N.A. v. Carpenter*, Index N0. 701473/2015 (N.Y. Sup. Ct. 2017) (Where the evidence showed that a party other than the Plaintiff had control of the eNote on the date the foreclosure action was filed, the Plaintiff failed to establish standing to bring the foreclosure action).

⁵⁹ *Id.* at 10-12. We note that while the question was not before the court, the court erred in stating that “a person having control of a transferable record ... is the holder for purposes of the UCC.” Under ESIGN, a party in control of a transferable record has the same rights conferred upon them by ESIGN as are conferred by the UCC on a holder, but is not a holder under the UCC. The rights are conferred by Section 201 itself. See 15 U.S.C. § 7021(d) (2000). See also UETA § 16 cmt. 6 (subsection 16(d) is a stand-alone provision, incorporating the relevant rules into subsection (d) by reference).

⁶⁰ The foreclosure suit was later voluntarily dismissed.

⁶¹ *New York Cmty. Bank v. McClendon*, 29 N.Y.S.3d 507 (App. Div. 2016).

⁶² *Rivera v. Wells Fargo Bank, N.A.*, 189 So. 3d 323 (Fla. Dist. Ct. App. 2016)

⁶³ The court should probably have applied 15 U.S.C. § 7021, rather than the UETA. It is likely ESIGN preempts the UETA with respect to questions related to control of the eNote, where, as in *Rivera*, the eNote was secured by real property. See fn. 57, *supra*. Because the standards are virtually the same under UETA and ESIGN, however, it is the authors' view that the error was harmless.

⁶⁴ The language required for each eNote by the GSEs includes the following:

I expressly agree that the Note Holder and any person to whom this Electronic Note is later transferred shall have the right to convert this Electronic Note at any time into a paper-based Note (the "Paper-Based Note"). In the event this Electronic Note is converted into a Paper-Based Note, I further expressly agree that: (i) the Paper-Based Note will be an effective, enforceable and valid negotiable instrument governed by the applicable provisions of the Uniform Commercial Code in effect in the jurisdiction where the Property is located; (ii) my signing of this Electronic Note will be deemed issuance and delivery of the Paper-Based Note; (iii) I intend that the printing of the representation of my Electronic Signature upon the Paper-Based Note from the system in which the Electronic Note is stored will be my original signature on the Paper-Based Note and will serve to indicate my present intention to authenticate the Paper-Based Note; (iv) the Paper-Based Note will be a valid original writing for all legal purposes; and (v) upon conversion to a Paper-Based Note, my obligations in the Electronic Note shall automatically transfer to and be contained in the Paper-Based Note, and I intend to be bound by such obligations. (E)

Any conversion of this Electronic Note to a Paper-Based Note will be made using processes and methods that ensure that: (i) the information and signatures on the face of the Paper-Based Note are a complete and accurate reproduction of those reflected on the face of this Electronic Note (whether originally handwritten or manifested in other symbolic form); (ii) the Note Holder of this Electronic Note at the time of such conversion has maintained control and possession of the Paper-Based Note; (iii) this Electronic Note can no longer be transferred to a new Note Holder; and (iv) the Note Holder Registry (as defined above), or any system or process identified in Section 11 (C) above, shows that this Electronic Note has been converted to a Paper-Based Note, and delivered to the then-current Note Holder

See FANNIE MAE, GUIDE TO DELIVERING EMORTGAGE LOANS TO FANNIE MAE (November 1, 2016); FREDDIE MAC, EMORTGAGE GUIDE (Version 9.0 2018).

⁶⁵ The ability to create or adopt a signature to be effective at the time of signing and also at a later date when on a different record or document is well established. “Present intention” means an intention to authenticate a writing at the time the symbol is adopted. *See* First National Bank v. Ford Motor Credit, 748 F. Supp. 1464, 1468 (D. Colo. 1990). A signature purposely made by a person on a previous occasion may be adopted for a new writing with the same effect as when originally made. 80 C.J.S. Signatures § 8 (2017). “[A] signature, one purposely made by the party on a previous occasion, may be adopted for a new writing then made, with the same effect as if made anew. This is a sufficient compliance with the requirements of the statute of frauds.” *Pontrich v. Neimann*, 271 S.W. 1049, 1050 (1925). The North Carolina Supreme Court has held that mechanical reproductions of an authorized official’s signature on DMV records are satisfactory if the official intends to adopt the reproduction as his signature. *State of N.C. v. Watts*, 222 S.E.2d 389, 392 (1976):

“We are of the opinion that the weight of authority and the better rule is that public documents may be authenticated by mechanical reproduction of the signature of the authorized officer when he intends to adopt the mechanical reproduction as his signature. In instant case, when the authorized officer of the Division of Motor Vehicles provided these records of the Department pursuant to the provisions of G.S. 20—222, it may be presumed that he intended to authenticate the documents and to adopt the mechanical reproduction of his name as his own signature.”

⁶⁶ Under UCC 3-204, a “paper affixed to the instrument is part of the instrument.”