HOME EQUITY LITIGATION IN TEXAS

2016 - 2018 CASE LAW AND 2017 CONSTITUTIONAL AMENDMENTS

Michael Baumer
Law Office of Michael Baumer
7600 Burnet Rd., Suite 530
Austin, TX 78757
512-476-8707
michael@baumerlaw.com
baumerlaw.com

November 2017 Amendments to the Texas Constitution

Proposition 2 was a constitutional amendment regarding home equity loans which was approved by a vote of Texans on November 7, 2017. There are five subparts.

Part A reduces the cap on closing costs from 3% to 2% of the principal amount of the extension of credit. This may sound like it will benefit borrowers, but the reduction in fees is offset by the fact that fees which were previously included in the cap are no longer included, including appraisal costs, survey costs, and title insurance costs. (Title insurance was often one of the larger closing costs under prior law.) The end result is that the borrower's "fees" may actually increase by the simple expedient of calling them something other than fees. It would appear that in most cases the actual increase will not be substantial. See discussion of 50(a)(6)(E).

Part B changes the list of authorized equity lenders. Before, the list included banks, S&Ls, credit unions and others not really relevant here. The new list includes the same list but now includes their subsidiaries. (Apparently so they can put their less credit worthy loans in the sub rather than the parent.) See discussion of 50(a)(6)(P).

Part C allows a lender to refinance an equity loan as a "traditional" mortgage rather than an equity loan. Potential downsides:

* An equity loan must be non-recourse, but a regular mortgage imposes personal liability on the borrower. If the borrower refinances a home equity loan into a conventional mortgage the loan will change from non-recourse to recourse.
- A traditional loan can be foreclosed without a court order which expedites the foreclosure process by at least 38 days.
- See discussion of 50(a)(6)(xi)(f).

Part D changes the limit on how much a borrower can draw on an equity line of credit. Previously, the borrower could only draw 50% of the value of the property on an equity line of credit. Now a borrower may draw up to 80% of the vale of the property as of the date of the loan agreement. This basically aligns equity lines of credit with equity loans which do not have a line of credit feature. See discussion of 50(a)(6)(t).

Part E allows a lender to take a lien on property which has an agricultural exemption for property taxes. Previously, a lender could only take a lien on the portion of the property designated as homestead but not on the remaining (ag exempt) property. For property tax exemption purposes, you designate a hypothetical one acre tract as homestead and the remainder as ag exempt. (The ag exemption reduces your taxes far more than the homestead exemption.) I say hypothetical because there is no survey to identify the actual homestead acre. If the lender wanted to make an equity loan on the one acre, it would have to survey out the actual acre which was fee subject to the 3% cap. With this amendment, "problem" solved. See discussion of 50(a)(6)(I).

Case Law – 2016 – 2018

Garofolo and ***Wood***

Tick tock of the clock is painful
All sane and logical
I want to tear it off the wall

Eve Six – Inside Out

The Texas Supreme Court issued two opinions on May 20, 2016 regarding issues related to the home equity loan forfeiture provisions of the Texas Constitution. These opinions make significant changes to Texas case law regarding applicability and enforcement of those provisions including the applicable statute of limitations. The first case was *Garofolo v. Ocwen Loan Servicing, L.L.C.*, 497 S.W.3d 474 (Tex.2016) and the second is *Wood v. HSBC Bank USA, N.A.*, 2016 WL 2993923 (Tex.2016). It is important that the cases are read in sequential order as *Wood* relies on *Garofolo* in reaching its conclusion. (All references to the Texas Constitution herein are to Article XVI, section 50(a)(6) and its subsections unless otherwise noted.)

I found these cases to be confusing (as did my sister who edits my papers) so I write to provide my understanding/interpretation of what they mean. To help you understand where we are going let me summarize at the beginning. *Garofolo* holds that there is no ***constitutional*** violation if a lender violates 50(a)(6) by not curing a violation if none of the cures enumerated in 50(a)(6)(Q)(x) will ***actually*** cure the violation. The court goes on to state (in dicta) that a borrower may have a ***breach of contract*** claim if the lender fails to cure after notice from the borrower and suffered actual damages. More significantly, *Wood* holds that if an equity lien does not include all of the terms and conditions required by 50(a)(6), it is not a valid lien under 50(c), and since it is not a valid lien, limitations does not start to run until the lender fails to cure after notice. (The statute of limitations ruling is the big news out of these two cases.) *Wood* also confirms *Garofolo*'s statements that a borrower may assert a claim for forfeiture as a breach of contract claim if the claim is asserted under 50(c) as opposed to 50(a).

In *Garofolo*, the Fifth Circuit certified two questions to the Texas Supreme Court because they involved interpretation of the Texas Constitution. Those two questions were:

1. Does a lender or holder violate Article XVI, Section 50(a)(6)(Q)(vii) of the Texas Constitution, becoming liable for forfeiture of principal and interest, when the loan agreement incorporates the protections of Section 50(a)(6)(Q)(vii), but the lender or holder fails to return the cancelled note and release of lien upon full payment of the note within 60 days after the borrower informs the lender or holder of the failure to comply?

2. If the answer to Question 1 is "no," then, in the absence of actual damages, does a lender or holder become liable for forfeiture of principal and interest under a breach of contract theory when the loan agreement incorporates the protections of Section 50(a)(6)(Q)(vii), but the lender or holder, although filing a release of lien in the deed records, fails to return the

Title search: Home Equity Litigation in Texas

First appeared as part of the conference materials for the
14th Annual Consumer Bankruptcy Practice session
"Recent Developments in Home Equity Litigation"