

## SELECTED CASE SUMMARIES TEXAS HOME EQUITY LAW

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### EQUITABLE SUBROGATION

***LaSalle Bank N.A. v. White*, 246 S.W.3d 616 (Tex. 2007).**

In this pivotal case decided in a unanimous opinion by the Texas Supreme Court, the Court held that the forfeiture penalty of the Texas Constitution does not preclude the lender's recovery of a refinance portion of loan proceeds that were used to pay pre-existing debt. The Court reasoned that the lender was equitably subrogated to the rights of the prior lienholders.

*Background Facts:* LaSalle Bank's predecessor extended a home equity loan in the amount of \$260,000.00 to Lorae White to refinance her homestead. The note was secured against a 10-acre portion of White's 53-acre property, which the trial court found was designated for agricultural use. The original lender used a portion of the loan proceeds to pay off a \$185,010.51 mortgage on the property and a \$9,410.96 property tax lien. The remaining loan proceeds were distributed to White. White failed to make any payments on the loan, and LaSalle filed an application for a judicial home-equity loan foreclosure.

*Procedural Posture:* The trial judge found the property was designated for agricultural use and signed a judgment quieting title free and clear of LaSalle's lien. The San Antonio Court of Appeals affirmed, holding that the Constitution prohibited equitable subrogation for the

refinance portion of the loan. LaSalle then appealed to the Texas Supreme Court.

*Home Equity Law & Equitable Subrogation:* The Texas Constitution provides that a lender can not extend a loan secured by property designated for agricultural use. TEX. CONST. art. XVI, § 50(a)(6)(I). LaSalle argued that it had a common law right of equitable subrogation. That is, the right as a third party to step into the shoes of the original lienholders and assume the original lienholders' rights to the security interest against the borrower. White argued that the Texas Constitutional provision prohibits all equitable subrogation rights, even those arising from payment of valid debts.

*Holding:* The Court held that "the forfeiture penalty does not preclude the lender's recovery of the refinance portion of the loan proceeds that were used to pay the debtor's constitutionally permissible pre-existing debt because the lender was equitably subrogated to the prior lienholders' interests." The Court reasoned that without equitable subrogation, lenders would not refinance due to the increased risk that the lenders could forfeit the entire amount of their liens. LaSalle was entitled to receive the amount used to pay White's purchase-money and property tax liens (\$194,421.47 of the loan in the original principal amount of \$260,000.00).

As previously noted, White filed a Motion for Rehearing in late January, which is pending before the Court. A quick ruling is expected

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given that the case was decided by unanimous opinion of the Court.

#### ACCUAL OF THE STATUTE OF LIMITATIONS FOR FORECLOSURE

***Burney v. Citigroup Global Mkts. Realty Corp.*, 244 S.W.3d 900 (Tex. App.—Dallas 2008, no pet.).**

The Dallas Court of Appeals broadened the list of events constituting a trigger of the accrual of the statute of limitations for foreclosure of a home equity loan in Texas. Even if a lender does not serve a borrower with a notice of acceleration of the loan, the lender's application for an order for foreclosure of the loan starts the four-year clock for foreclosure.

*Background Facts:* On March 15, 1999, Joe Burney executed a home equity loan payable to Long Beach Mortgage Company (which subsequently assigned the loan to Norwest Bank Minnesota) for \$42,250.00. The deed of trust stated that upon default the lender would provide notice of default, the action required to cure, and that failure to cure would result in acceleration of the note. On October 18, 1999, Norwest sent Burney a letter notifying her of default. The letter further stated that Norwest would accelerate amounts owed on the loan and proceed to judicial foreclosure if Burney did not cure within thirty days. Burney did not cure.

On April 5, 2000, Norwest filed an application for expedited foreclosure. The application was dismissed for want of prosecution. Norwest assigned the note to Citigroup. On November 15, 2004, Citigroup filed an application for foreclosure.

*Accrual of the Statute of Limitations:* In Texas, lenders have four years to file a suit for recovery or foreclosure of a real property lien. TEX. CIV. PRAC. & REM. CODE § 16.035(a). A cause of action accrues from the date of acceleration of the note. *Citing Holy Cross Church of God in Christ v. Wolf*, 44 S.W.3d 562, 569 (Tex. 2001).

Both parties agree the October 18, 1999 letter was a notice of intent to accelerate the note. Burney argued that the April 5, 2000 suit for foreclosure provided notice of acceleration. Citigroup argued that the application for foreclosure did not provide unequivocal notice of acceleration as required by the deed of trust.

*Holding:* The Court that under the facts of the case, "notice of filing an expedited application for foreclosure after the requisite notice of intent to accelerate is sufficient to constitute notice of acceleration." The court relied on cases involving non-judicial foreclosures that hold that notice of a trustee's sale is sufficient notice of acceleration if preceded by the required notice of intent to accelerate. *Citing Meadowbrook Gardens, Ltd. V. WMFMT Real Estate Ltd. P'ship*, 908 S.W.2d 916, 918-19 (Tex. App.—Fort Worth 1998, pet. denied); *McLemore v. Pacific Southwest Bank*, 872 S.W.2d 286, 292 (Tex. App.—Texarkana, writ dismissed by agr.).

#### CURE LOAN

***Summers v. Ameriquest Mortgage Co.*, No. 14-06-00734-CV, 2008 Tex. App. LEXIS 254 at \*1 (Tex. App.—Houston [14<sup>th</sup> Dist.], January 15, 2008, no pet.).**

The Houston Court of Appeals affirmed a trial court judgment that the lender did not violate the Texas Constitution's prohibition against closing more than one home equity loan in one year when the loan was extended under the Constitution's provision to cure a defect in the first loan.

*Background Facts:* Kelly Lee Summers executed a home equity note and security instrument with Ameriquest in July 2002. Summers then refinanced and paid the 2002 loan in full with another home equity loan from Ameriquest on March 19, 2003. Ameriquest offered the March 2003 loan as part of a settlement agreement between the parties after Summers complained that the July 2002 violated the Texas Constitution.

*Constitutional prohibition against multiple home equity loans in one year:* The Texas

Constitution provides means for a lender to cure Constitutional defects in a home equity loan within a reasonable time in order to validate a lien and avoid forfeiture of all principal and interest. TEX. CONST. art. XVI, § 50(a)(6)(Q)(x). However, the Constitution also provides that a home equity loan can not close before “the first anniversary of the closing date of any other” home equity loan secured by the same property. *Id.* at § 50(a)(6)(M)(ii). Summers argued that the March 2003 home equity loan was invalid because it closed less than one year after the July 2002 loan. Ameriquest argued that the March 2003 loan was offered under the Constitution’s cure provision and was therefore valid.

*Holding:* The court held that the March 2003 loan was valid despite the fact it was closed within the same calendar year as the July 2002 loan because it was a cure loan given under the Texas Constitution. The Court heavily relied on *Doody v. Ameriquest*, 49 S.W.3d 342 (Tex. 2001) to support its holding that the cure provision is intended to apply to all home equity loans given under Section 50(a)(6) of the Texas Constitution.

\*The court also addressed a res judicata issue argued by the parties based on a prior declaratory judgment action between them. However, the Court’s res judicata analysis is of little significance to the applicability of home equity laws in Texas.

#### CURE LOAN AND DTPA

***Fix v. Flagstar Bank, FSB*, 242 S.W.3d 147 (Tex. App.—Fort Worth 2007, pet. filed).**

The Fort Worth Court of Appeals addressed two issues: (1) whether the September 2003 Constitutional amendments on home equity cure loans were retroactive; and (2) whether borrowers on a refinance loan qualified as consumers under the DTPA.

*Background Facts:* In March 2002, the Fixes obtained a home equity loan in the amount of \$288,000.00 from Flagstar’s predecessor. In January 2003, the Fixes refinanced with a loan through Flagstar. The January 2003 loan violated two provisions of the Texas

Constitution: (1) it was given less than one year from the March 2002 loan; and (2) it allowed for personal liability against the debtors and for non-judicial foreclosure.

In December 2003, Mr. Fix had a phone conversation with Flagstar’s vice president. Both Flagstar’s vice president and claims counsel for the title insurance company sent letters to the Fixes informing that the Fixes had contested the validity of the second loan, without specifying the details of the contest. Mr. Fix replied in a February 2004 letter, detailing the two alleged Constitutional violations. Twenty one days later, Flagstar offered to cure the alleged defects by re-closing the loan at a lower interest rate and paying the Fixes \$1,000.00. The Fixes refused and requested Flagstar and the title company forfeit the entire amount of the loan. The Fixes claimed the attempt to cure was not made within 60 days of their original complaint, as required by the Texas Constitution.

*September 2003 cure provision in Constitution not retroactive:* In 2003, the Texas Constitution provided that a lender had a “reasonable time” to cure defects in a home equity loan. Act of May 24, 2003, 78<sup>th</sup> Leg., R.S., S.J.R. 42, 2003 Tex. Gen. Laws 6219 (amended 2003) Current version at TEX. CONST. art. XVI, § 50(a)(6)(Q)(x). The provision was changed in September 2003 to give lenders a strict sixty-day time limit to cure defects.

*Holding:* The court held that the September 2003 Constitutional amendment was not retroactive, and applied the version of the Constitution in effect at the time the parties signed the loan documents (January 2003). The court further held that, assuming the December 2003 phone call gave Flagstar notice of the alleged defects, the offer to three months later was a given in a “reasonable time.” The court affirmed the trial court’s decision to deny the Fixes request for forfeiture.

*Consumer status under the DTPA:* To qualify as a consumer: (1) a person must seek to acquire goods or services by lease or purchase; and (2) the goods or services must form the basis of the

person's complaint. A person can not qualify if "the underlying transaction is a pure loan because money is considered neither a good nor a service." *Quoting Riverside Nat'l Bank v. Lewis*, 603 S.W.2d 169, 173-74 (Tex. 1980). The Fixes argued that they were consumers under the Texas Deceptive Trade Practices Act. Flagstar and the title company argued that the Fixes were not consumers under the DTPA because the January 2003 loan was not for the purchase of a good or service.

*Holding:* The court held that the Fixes did not qualify as consumers under the DTPA because they sought refinancing services. The refinance "merely extended credit to the Fixes," and as such was not a good or service. The court found that, assuming the title policy was a service under the DTPA, it was not the basis of the Fixes complaint.

\*The Petition for Review was filed on January 28, 2008, and a Response to the Petition for Review was filed on May 15, 2008 pursuant to the Court's request. As of May 30, 2008, the Court had not yet granted or denied the request for review.

#### **BREACH OF CONTRACT, USURY, DTPA**

***Allen v. American Gen. Fin., Inc.*, No. 04-06-00273-CV, 2007 Tex. App. LEXIS 9236 at \*1 (Tex. App.—San Antonio, November 28, 2007, pet. filed).**

*Background Facts:* Kyle Allen obtained a home equity loan from American General Finance on May 18, 1998 in the amount of \$15,000.00 for the purpose of paying delinquent taxes that he owed. The closing documents indicated \$4,988.29 of the loan proceeds were to be paid for the back taxes. However, Allen owed more than \$6,000.00 in taxes, as evidenced by the tax suit previously brought against him. The taxing authorities later obtained a default judgment against Allen and sold the property at a tax foreclosure sale. In addition, Allen defaulted on the loan with AGF.

*Breach of Contract:* Allen sued AGF for breach of contract for failing to pay the full amount of the tax lien. AGF alleged that its promise to pay

all amounts due in the tax lawsuit was not sufficiently definite to support a contract.

*Holding:* The court held that the promise by AGF to pay the taxes was "an integral part of the loan transaction," and not a separate agreement. Allen and AGF exchanged mutual promises because AGF promised to pay the tax lien and Allen promised to pay on the home equity loan. Allen's promise to make monthly payments on the note was sufficient consideration to support the lending of money and the promise to pay off the tax debt. The court also found that AGF breached the contract before Allen because AGF did not pay off the full amount of the tax lien upon closing of the home equity loan. Allen's first missed payment under the note occurred subsequent to AGF's promise to pay the taxes.

*Usury:* Upon Allen's default on the note, AGF's counsel sent a letter to Allen demanding a payment that included an interest rate higher than the greatest rate allowed by law. The letter was not actually received by Allen because it was not sent to his residence. To be a "charge" within the meaning of the usury statute, the charge must be communicated outside the business and must be expressly demanded from the borrower. AGF argued that there was no usurious "charge" because the rate was not actually communicated to Allen.

*Holding:* The held that "a demand for usurious interest in a letter addressed and sent to the debtor is a 'charge' within the meaning of the statute without requiring proof that the intended recipient actually received the letter."

*DTPA Consumer Status:* Allen argued that he is a consumer under the DTPA. AGF argued that Allen was not a consumer because he only sought an extension of credit, which is not a good or service under the DTPA.

*Holding:* The court broadened the definition of 'good or service' and held that Allen presented enough evidence to show that he could be a consumer. The court based its ruling on the determining factor that Allen sought the "service" of getting his tax suit "taken care of," and that the sole purpose was not just to obtain a

loan. The court remanded for proceedings on Allen's DTPA causes of action.

\*AGF argued additional grounds in its appeal, which are not relevant to a discussion of home equity lending law.

\*\*The Petition for Review was filed on March 6, 2008. The Court requested a response, which had not been filed as of May 30, 2008.

#### AMOUNT IN CONTROVERSY FOR REMOVAL

***Wiggins v. Wells Fargo Bank, N.A., No. H-07-1143, 2007 U.S. Dist. LEXIS 44216 at \*1 (S.D. Tex., June 19, 2007).***

*Background Facts:* During the Plaintiff's divorce, his wife obtained a home equity loan in the amount of \$61,250 in violation of the divorce decree. The decree granted Plaintiff a \$45,000 lien on the subject property and granted the wife possession until the property sold. Plaintiff filed suit in state district court seeking a declaration that Wells Fargo's lien was void. The defendants removed the action to federal court on the basis of diversity jurisdiction and Plaintiff sought remand to state court.

*Amount in Controversy:* Defendants argued that it was facially apparent from the petition that the amount in controversy exceeded \$75,000. The defendants claimed that Plaintiff sought to protect his \$45,000 lien *and* to declare Wells Fargo's \$74,699 lien void.

*Holding:* The court relied on a Fifth Circuit holding that in an action for equitable relief, the proper measure of the amount in controversy is the benefit or value to the Plaintiff, not the cost to the defendant. *Relying on Webb v. Investacorp, Inc.*, 89 F.3d 252, 257 n.1 (5th Cir. 1996). The court held that Plaintiff only sought to protect his \$45,000 interest and that declaring Wells Fargo's lien void would not benefit the Plaintiff. The court remanded the case because it was not facially apparent that the potential benefit to the Plaintiff was more than \$75,000.

\*\*\*It is important to note that the defendants did not argue that the amount in controversy is actually the market value of the property. The Southern District relied on the *Webb* opinion, which was not a case regarding a real property lien dispute. *See Waller v. Professional Ins. Corp.*, 296 F.2d 545, 547-48 (5<sup>th</sup> Cir. 1961) ("when the validity of a contract or a right to property is called into question in its entirety, the value of the property is the amount in controversy"); 14B Charles A. Wright & Arthur R. Miller, *Federal Practice & Procedure* § 3702, at 85 (1998).

#### COMPULSORY COUNTERCLAIMS & WAIVER OF REMEDIES

***Witt v. Countrywide Home Loans, Inc., No. 3:06-CV-1384-D, 2007 U.S. Dist. LEXIS 58688 at \*1 (N.D. Tex., August 10, 2007).***

*Background Facts:* Plaintiff took out a first money purchase mortgage on her home in the amount of \$122,771. In June 2000, Plaintiff defaulted on payments and Countrywide accelerated the total amount due and posted the property for a non-judicial foreclosure (which is available for mortgage loans in Texas). The parties thereafter entered into a Loan Modification agreement, which added the past-due amounts to the principal amount of the loan. Plaintiff again fell behind in her loan payments. However, this time Countrywide sent Plaintiff a notice under Section 50 of the Texas Constitution (dealing with home equity loans). The notice informed Plaintiff of Countrywide's intent to conduct a judicial foreclosure in accordance with Section 50. Plaintiff filed for bankruptcy and avoided foreclosure.

In 2004, Plaintiff again defaulted under the Note. Countrywide sent Plaintiff another notice of its intent to conduct a judicial foreclosure sale pursuant to Section 50. Plaintiff filed suit against Countrywide for breach of contract and DTPA violations. Countrywide did not file a counterclaim for foreclosure in that action. Countrywide obtained a judgment in its favor. Plaintiff then filed suit against Countrywide seeking to declare its lien invalid because it did not file a compulsory counterclaim for foreclosure in the first suit. Countrywide maintained that it

mistakenly referred to Plaintiff's loan as a home equity loan instead of a purchase money mortgage.

*Compulsory counterclaims:* Texas recognizes an exception to compulsory counterclaims for foreclosure of mortgages because a "borrower should not be able to force its lender to elect judicial foreclosure by merely filing an action challenging the validity of the note." *Quoting Douglas v. NCNB Tex. Nat'l Bank*, 979 F.2d 1128, 1130 (5th Cir. 1992). However, if the lender waives its right to non-judicial foreclosure, the borrower is no longer forcing the lender to elect judicial foreclosure.

*Holding:* In this case, the court found that there was a genuine issue of fact concerning whether Countrywide waived its right to judicial foreclosure by representing that the Note and Modification Agreement were components of a home equity loan.