

Supreme Court of Texas; Recent Texas Home Equity Lending Decisions

06.02.16

On May 20, 2016, the Supreme Court of Texas (the "Court") issued its opinions in two cases involving Texas home equity lending – *Garofolo v. Ocwen Loan Servicing* and *Wood v. HSBC Bank USA*. The decisions are important for the industry and certain highlights are noted below.

***Garofolo vs. Ocwen Loan Servicing*, ____ S.W.3d ____ (Tex. 2016)** (This case involved a borrower's claim for forfeiture because the lender failed to timely provide a release of lien to the borrower upon final payment after notice by the borrower of such failure.)

Highlights include:

- Foreclosure – eligible home equity loans must include specific terms and conditions.
- Loans must include the specific provisions set forth in Sections 50(a)(6)(A)-(P) and Sections 50(a)(6)(Q)(i)-(xi).
- These specific terms and conditions do not amount to constitutional rights and obligations.
- The Texas Constitution does not create a constitutional cause of action or remedy for a lender's subsequent breach of those terms or conditions.
- A post-origination breach of those terms and conditions may give rise to a breach-of-contract claim for which forfeiture can sometimes be an appropriate remedy.
- The Texas Constitution prohibits foreclosure when a loan fails to include a constitutionally – mandated term or condition.
- Forfeiture is an available remedy only if one of the six corrective measures in Section 50(a)(6)(Q)(x)(a)-(f) can actually correct the underlying problem and the lender nonetheless fails to timely perform the corrective measure.
- In the vast majority of cases the catch-all cure will present a fix that will actually correct the borrower's complaint when no other corrective measure would.
- Forfeiture is an unavailable remedy under the case's facts (e.g., refinance of a paid-off loan is ridiculously futile, and refinanced loan on different terms would not repair the underlying deficiency – providing the borrower with a release of lien).
- The remedy in this case is a traditional breach of contract claim, in which the borrower seeks specific performance or other remedies contingent on a showing of actual damages.

***Wood vs. HSBC Bank USA*, ____ S.W.3d ____ (Tex. 2016)** (This case primarily involved allegations of closing charges exceeding the 3% fee limit and application of a 4 year statute of limitations.)

Highlights include:

- Constitutionally noncompliant home-equity loans are invalid until cured and thus not subject to a statute of limitation for a quiet title action.
- Home equity loans must include terms and conditions, including the forfeiture term, to be foreclosure eligible.
- If constitutionally noncompliant, the lien is not valid before a defect is cured.
- A lender or holder should maintain records throughout the life of the loan.
- The forfeiture provision does not create a constitutional cause of action but rather must be litigated in the context of the borrower's loan agreement.

Some Considerations:

- The Court introduces the concept of "foreclosure-eligible home equity loans." The term refers to Texas home equity loans that include the specific constitutionally mandated terms and conditions. See art XVI, §§ 50(a)(6)(A)-

(P) and 50(a)(6)(Q)(i)-(xi). Accordingly, lenders should review their loan documents to insure the specific terms and provisions are included.

- Essentially, a home equity loan is invalid unless it strictly complies with the Texas Constitution.
- Lenders and holders also should review procedures for curing so corrective action is taken timely (*i.e.*, within 60 days after the borrower's notification).
- A breach-of-contract claim may serve as the basis for a borrower to recover attorney's fees pursuant to Tex. Civ. Prac. & Rem. Code § 38.001.
- The Court does not address various issues. For example, in connection with a traditional breach of contract claim seeking forfeiture pertaining to a violation or failure to take corrective action the Court did not expressly state:
 - Whether the statute of limitations applies (a four year limitations period applies to a breach of contract claim), or
 - If a four year limitation period applies, whether the cause of action accrues when the violation accrues (in most cases at the time of origination) or when a lender fails to take corrective action within 60 days after notification by the borrower.

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