Beck Redden, Lane Law Firm Win a Victory for Texas Homeowners

By Natalie Posgate

(June 14) – Since Stephen F. Austin founded the Lone Star State, Texans have enjoyed the benefit of homestead exemption laws designed to protect them from losing their homes at the beck and call of the "big, bad banks."

Texas was even the last state to allow home equity loans. When the Legislature finally did in 1998, it imposed many rules that banks were not required to follow in other states. This helped Texas emerge as arguably the state least affected by home foreclosures after the housing bubble burst. The protections even dubbed Texas's regulations as the "first state anti-predatory lending" laws.

Three years ago, a federal appeals court ruling jeopardized all that.

In *Priester v. JPMorgan Chase Bank*, the U.S. Court of Appeals for the Fifth Circuit ruled that a homeowner with a constitutionally defective lien on a homestead had only four years after the origination of the home equity loan to file suit. This meant that borrowers taking out home equity loans in Texas could face foreclosure, even if the liens on their homesteads violated the requirements of the Texas Constitution.

Fortunately for Texas homeowners, a group of lawyers led by appellate expert ***Connie Pfeiffer*** of Beck Redden fought hard to regain those protections in a recent Texas Supreme Court case that reversed the Fifth Circuit's ruling. In *Wood v. HSBC Bank USA*, Texas' High Court determined that no statute of limitations applies when challenging unconstitutional liens securing home equity loans – since such liens are void until the defects are cured.

This ruling provides a crucial shield for the roughly 15 percent of Texas homeowners who take out home equity loans. It also marks a happy ending for two Houston law firms, Beck Redden and The Lane Law Firm, who were forced to play hopscotch across different courts before getting to the Supreme Court of Texas.

"It's a fantastic victory for homeowners, who I think will get the benefit of the bargain when they voted in 1997 on these types of loans," said Chip Lane of The Lane Law Firm, who represented the Woods before the trial court.


Chip Lane

Lane said the Fifth Circuit's decision has negatively affected more than 100 homeowners who have filed complaints since. And many more homeowners decided it was not even worth the fight, due to their dauntingly small chances of prevailing, he said.

"We were turned away by an awful lot of folks who said, 'I don't want to fight it; I'm not going to waste my time.' So they got foreclosed on and moved out," Lane said. "Now those people have the fighting chances that they deserve."

Pfeiffer, a partner in Beck Redden's Houston office who handled the Woods' appeal, said the number of homes affected is also likely higher because many homeowners facing foreclosure cannot afford a lawyer to fight for them.

"It's the homeowner facing foreclosure because they can't afford their mortgage versus the big national bank," she said. "That disparity is always going to be David versus Goliath. They're strapped for cash, and all they know is they're about to lose their home."

Fifth Circuit's Wrong 'Guess' on Texas Law

John and Bettie Priester sued a group of lenders led by JPMorgan Chase in 2010 after discovering their $180,000 home equity loan, which they obtained in 2005, violated the Texas Constitution. They had closed on the loan at their home instead of an attorney's office, the lender or a title company, as required by the state's constitution.

Though the Priesters sued in state court, JPMorgan Chase succeeded in moving the case to federal district court. Since the claim involved the interpretation of state law, the Fifth Circuit ruled on an *Erie* guess, which Pfeiffer described as an educated guess of what the Supreme Court of Texas would do if facing the same issue.

Pfeiffer said this erroneous *Erie* guess had a negative impact on subsequent cases involving homeowners who discovered constitutional violations in their home equity loans more than four years after signing – which she said was most of the time, since few homeowners discover defects in their loans until they face foreclosure.

Once the Fifth Circuit issued its decision, "everyone thought it was the right answer," Pfeiffer said. "It created a huge bandwagon effect." After that, every lender moved to get their cases into federal court, where Priester was binding.

She would discover this firsthand while representing the homeowners in *Moran v. Ocwen Loan Servicing*, which moved from state court to federal district court to the Fifth Circuit.

Ronald and Jean Moran currently face foreclosure on their Houston home, despite the fact that their home equity loan agreement with Appellee Bank of New York Mellon and Ocwen Loan Services allegedly violated the Texas Constitution by exceeding 80 percent of the value of their home, said Lane, who represented the Morans at the trial level. The Morans entered their loan agreement with the lenders in 2002 and sued them more than 10 years later.

Since the issue had already been decided in *Priester*, the Fifth Circuit denied review of the Morans' case because internal circuit rules do not allow it to revisit a decision.

Fortunately, a case came along that would finally get Pfeiffer to the Texas Supreme Court to seek clarity on the issue.

Around the same time, Lane had hired Pfeiffer to handle the appeal of another case – *Wood v. HSBC Bank USA*. The difference in this case was that it remained in state court since the original lender was headquartered in Texas.

Alice and Daniel Wood obtained a $76,000 home equity loan in 2004 from a bank now owned by HSBC. Nearly eight years later, Mr. Wood became ill and the couple missed some payments on their house, located in the greater Houston area. Fearing foreclosure, Mrs. Wood contacted Lane's firm, which specializes in helping homeowners evaluate the status of their loans and challenge the banks if something was wrong.

And indeed, there was something wrong. The Woods claimed that their home equity loan violated the Texas Constitution in several respects, including the fact that the closing fees exceeded 3 percent of the loan amount.

They filed suit in July 2012 in state court against HSBC and Ocwen. The lawsuit sought a judgment to quiet title, to forfeit principal and interest from the lenders and to excuse the Woods from any further obligation to pay their loan. The trial judge rejected the Woods' arguments and granted summary judgment for the lenders on all claims, citing *Priester*, which barred such claims after the four-year statute of limitations had expired.

The Woods appealed to the Fourteenth Court of Appeals on only one issue: whether their claims based on non-constitutional compliance were subject to a statute of limitations. The appeals court affirmed the trial court's opinion.

Pfeiffer finally had enough of courts citing *Priester* as the authority. She decided to seek an overruling of *Priester*, and appealed the case to the Supreme Court of Texas.

Arguing *Wood* to Texas' High Court

On Dec. 8, 2015, Pfeiffer emphasized during oral arguments that banks would have no incentive to cure their constitutional violations if the four-year statute of limitations were upheld since it places "the burden on the homeowner to notice the defect, hire a lawyer and file suit within four years.

"Whereas the lender would much rather have a King's X and not have to cure."


Connie Pfeiffer

She said the Texas Supreme Court's prior decision in *Doody v. Ameriquest Mortgage Co.* and the plain text of the Texas Constitution, which she argued states no lien secured by a home equity loan is valid unless it meets the entirety of a list of requirements, are designed to protect homeowners from predatory loans.

If the High Court ruled that the constitution states there is a statute of limitations, there will be banks "that will flout this much more creatively to try to avoid homeowners figuring out" flaws in their agreements within four years, she argued.

"Just imagine for a moment that if a particular lender decided to target a neighborhood, go door to door and solicit borrowers, close a home equity loan in someone's house without their spouse present, and charge interest-only payments for four years with a big balloon in year five, that homeowner, if there's a statute of limitations, would have no remedy," she told the justices. "They wouldn't be able to set aside a constitutionally defective lien, and they wouldn't have any forfeiture of principal and interest.

"If there is no statute of limitations, the effect is that lenders will not comply or cure the problems, because they were curing them until the Priester decision," she added.

But Scott Hastings, representing HSBC and Ocwen, argued that the language in the state constitution doesn't suggest that these home equity liens are void until corrected, but rather, they are voidable. If Pfeiffer's "void but curable" interpretation of this clause in the constitution is correct, he said it opens the door to all kinds of "absurdities."

For example, what if the borrower decides not to pay the loan, and the lender figures out it needs to be cured? Hastings asked.

"Can you be in breach of a void loan?" Hastings, a partner in Locke Lord's Dallas office, asked the justices. "It reaches all kinds of absurd results that we'll spend years trying to figure out what they'll mean if this is where we end up."

He also argued that lenders already have three major incentives to comply with the Texas Constitution with a four-year statute of limitations in place. The first incentive he said, is if the loan does not comply, "we are here dealing with issues of cure, notice and forfeiture."

He said the other two issues are laid out in the Texas Supreme Court's *Doody* decision – the very same ruling that Pfeiffer cited in her oral argument – which he said states there are already regulatory and business incentives in place.

On the regulatory side, Hastings said the previous opinion states if a lender is not in compliance with the constitution, "they might even have licensing issues to be able to stay in business."

He said the business incentives are that lenders want to comply with the Texas Constitution because it will hurt their business if they do not.

"Eventually customers won't want to do business with the lender that doesn't follow the rules," he said.

SCOTX: 'No statute of limitations applies'

In a 6-3 decision, the Texas Supreme Court agreed with Pfeiffer's interpretation of *Doody* and the text of the Texas Constitution that the Woods could bring forward their claims under no time limit because the lien securing their home equity loan was void, not voidable. The ruling overturned the Fifth Circuit's *Priester* decision, as well as five Texas appellate decisions that followed *Priester*.

"Constitutional mandates need not be shoehorned into common-law concepts when those concepts conflict with the Constitution's plain text," ruled Justice Debra Lehrmann in the majority opinion. She was joined by Justices Phil Johnson, Eva Guzman, Jeffrey Boyd, John Devine and Jeff Brown.

"The text of the Constitution and our decision in *Doody* do not support a holding that liens securing constitutionally noncompliant home equity loans are merely voidable," Justice Lehrmann wrote. "A voidable lien is presumed valid unless later invalidated… while section 50 and *Doody* contemplate precisely the opposite: that noncompliant liens are invalid until made valid. Holding otherwise would essentially permit lenders to ignore the Constitution and foreclose on the homesteads of unwitting borrowers who do not realize that their home equity loans violate the Constitution.

"We agree with the Woods that a lien securing a constitutionally noncompliant home equity loan is not valid before the defect is cured," the opinion states. "We therefore conclude that no statute of limitations applies to an action to quiet title on an invalid home equity lien."

The court did not, however, rule on the validity of the Woods' claim on whether their closing fees exceeded 3 percent of their loan amount. The justices remanded that issue to the trial court.

"That issue is not before us," Lehrmann wrote.

In dissent, Chief Justice Nathan Hecht argued that the majority opinion, which injects "instability into land titles, has been rejected by the Fifth Circuit and by four Texas Courts of Appeals – every appellate court that has considered the matter. I would join them and therefore respectfully dissent.

"Because the court holds that a homestead lien is invalid from the moment of noncompliance, a borrower has forever to challenge it – after evidence and witnesses are gone, and proof has become difficult or impossible," added Hecht, who was joined in his dissent by Justices Paul Green and Don Willett.

Scott Hastings of Locke Lord, who argued at the Texas Supreme Court for HSBC, the note holder, and Ocwen Loan Servicing, the loan servicer, declined to comment on the case. Houston Baker Donelson lawyers Kari Robinson and Valerie Henderson, who represented the lenders at the trial level, could not be reached for comment.

In addition to Pfeiffer and Lane, the Woods' legal team included Houston appellate partner ***Russell Post*** from Beck Redden and trial attorney Anh Thu Dinh from The Lane Law Firm.