CORNERSTONE CREDIT UNION LEAGUE

Independent Bankers Association of Texas

TexasBankers Association
Strong Banks. Stronger Communities.

TEXAS MORTGAGE BANKERS ASSOCIATION

November 13, 2019

Blake A. Hawthorne
Clerk of the Court
Supreme Court of Texas
201 W. 14th Street, Suite 104
Austin, Texas 78701

Re: Federal Home Loan Mortgage Corporation v. Zepeda; No. 19-0712

Dear Sirs/Madams:

The amici represented by this letter include the Independent Bankers Association of Texas, Texas Bankers Association, Texas Mortgage Bankers Association, and Cornerstone Credit Union League. These four trade associations represent virtually all the residential mortgage lenders in the State of Texas. The amici strongly support the arguments in favor of equitable subrogation as briefed by Appellant Federal Home Loan Mortgage Corporation ("Freddie Mac") and adopt them as their own. The purpose of this letter is to provide some additional industry context for your consideration in evaluating the policy impact of upending 125 years of settled lien law.

Virtually all the amici's members make and refinance homestead secured loans in Texas, and most of them make home equity loans. According to the June 30, 2019 Call Report data for all Texas FDIC insured institutions, there was $5.425 billion in outstanding home equity loans held by such institutions, and there was $333.7 million held by credit unions. In addition to these amounts, mortgage bankers originate and sell substantial amounts of home equity loans to Freddie Mac, Fannie

Mae, and other participants in the secondary market. Furthermore, the Texas Real Estate Center's "Outlook for the Texas Economy" from October 10, 2019 reported that Texas refinance mortgage applications have more than doubled since year-end. Accordingly, the amici's members have a strong interest in assuring that their portfolios, which rely on current Texas decisions regarding lien validity, are protected.

The current case involves a refinancing of a valid home equity lien against a homestead in which additional funds were advanced to cover the closing costs. There is no dispute that the prior transaction created a valid lien against the homestead. However, due to a technical defect in the current transaction as to the absence of a countersignature on the acknowledgement of fair market value, Appellee Sylvia Zepeda argues that both the new lien and the prior, admittedly valid lien must fail. If this position is upheld, significant amounts of Texas real estate loan portfolios will be adversely affected.

Although borrowers may apply for a second lien home equity loan (or home equity line of credit), they often will refinance an existing lien in order to qualify for a lower interest rate, as Zepeda did. In addition, the consumer may prefer to have only one mortgage payment to make rather than two. Further, the principal on a home equity loan could be spread over a longer term than on a home equity line of credit, thereby lowering the amount of each monthly installment. A first lien transaction also presents lower risk to the lender and thus justifies a lower interest rate for the borrower. Banks and credit unions are examined for appropriate risk management and are expected to implement a sound program for effective management of risks. (See, for example, *Supervisory Guidance on Model Risk Management,* OCC 2011-12 and Interagency *Advisory on Interest Rate Risk Management*, January 6, 2010.) A cash-out refinancing transaction is a more attractive product for lenders to offer as it reduces the potential risk of loss that would occur in the event a borrower defaults on a prior lien transaction that has precedence over its lien. Thus, equitable subrogation is equally important in preserving lien position.

A refinancing of an existing lien does not occur only in the context of home equity loan transactions, either. It is common for interim construction financing to be provided by one lender while the permanent take-out loan is offered by a different one. Thus, the concept of equitable subrogation is important in a wide array of transactions that could be adversely affected by a reversal of long-standing Texas law authorizing that concept. A reversal of equitable subrogation precedent would

make a large swath of real property secured loans more risky. Ultimately, this could reduce the availability of credit in certain product lines (like home equity cash-out refinancings and traditional construction financing) or alternatively make it more costly as lenders price for risk.

The higher risk that would result from denying equitable subrogation is not just a problem for lenders, however, it also presents a significant cost to consumers. As home equity lending has matured in the last twenty years, such loans and home equity lines of credit have become more available to small business sole proprietors who can now use their homestead for their operating lines. Families use home equity transactions to finance college expenses, home improvements, medical expenses, and debt consolidation at a significantly lower cost than is available for other consumer credit products, which are perceived to be riskier. Further, the Comptroller of the Currency notes in its *Residential Real Estate Lending Handbook* that the Tax Reform Act of 1986 changed the income tax laws so that interest on loans secured by a borrower's residence is the only deductible consumer interest. This change led to increased refinancing of purchase-money loans that included the extension of new money or credit. According to the Comptroller's Handbook, the proceeds were used for many purposes, including home renovations, repairs, education, debt consolidation and other general needs. (page 2: https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/residential-real-estate-lending/pub-ch-residential-real-estate.pdf)

In conclusion, the amici respectfully request that this court clearly educate the Fifth Circuit Court of Appeals on Texas equitable subrogation, concluding that this well-established concept in Texas law continues to be valid, including as to home equity refinancing transactions as well as other refinancings.

No fees other than usual salary for in-house or retained counsel have been paid in the preparation of this brief.

Sincerely,

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CERTIFICATE OF COMPLIANCE

I certify that this document contains 879 words in the portions of the document that are subject to the word limits of the Texas Rule of Appellate Procedures 9.4(i), as measured by the undersigned's word-processing software.

/s/ Karen Neeley
Karen Neeley

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of this Brief of Amicus Curiae is being served electronically through the electronic filing service provider, efile.txcourts.gov, in compliance with Supreme Court of Texas T.R.A.P. 9.5(d)(e) on November 13, 2019, to all counsel of record as follows:

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