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To: Clients and Friends

From: Daniel S. Engle

Subject: Recent Texas Appellate Decision Highlights Texas Inheritance Law Complexities

In a decision delivered July 27, 2023, the Texas Court of Appeals, Fort Worth reaffirmed potential hazards for lenders concerning Texas inheritance laws. The case, *Grooms et. al. v. The Bank of New York Mellon Trust Company, N.A. as Trustee et. al., 2023 WL 4780584* dealt with the aftermath of a reverse mortgage loan after the borrower passed away. While not creating any significant precedent, the case did highlight the complexity of Texas inheritance laws.

The reverse mortgage loan in question was taken out by Evelyn Grooms in 2006 on property that she had owned along with her late husband as community property. In 2001, her husband died intestate—that is, without a Will—and he was survived by Evelyn and three children. One of the three children was also a child of Evelyn while the other two were from a prior marriage. When taking out the loan in 2006, Evelyn stated that she was the sole owner. She was the only person who signed the reverse mortgage loan documents. After some time, Evelyn died intestate (the court did not specify the date).

After her death, the reverse mortgage holder (The Bank of New York Mellon Trust Company, N.A. as Trustee for Mortgage Assets Management Series I Trust) and mortgage servicer (Compu-Link Corporation) notified her estate that the mortgage was in default. The estate responded by filing a lawsuit against the mortgage holder and mortgage servicer stating, among other things, that the reverse mortgage was invalid and to seek a declaration that the lien was not foreclosure eligible. The defendants counter-claimed and sought, among other things, an order of foreclosure. At the trial court level, the defendants obtained a summary judgment that the reverse mortgage complied with the Texas Constitution and obtained a foreclosure order (the defendants also obtained a summary judgment involving an alleged violation of the Texas Debt Collection Act "TDCA" that is beyond the scope of this memo). The estate appealed the trial court's decision.

Essentially, the estate's argument against foreclosure was that Evelyn Grooms was not the sole owner of the property when the reverse mortgage was made. This was because of Texas intestacy law governing the distribution of community property in Section 201.003 of the Texas Estates Code. If Evelyn's late husband did not have any children or if all of her husband's children were born to both Evelyn and her husband, then Evelyn would have inherited her late husband's interest in the property by intestacy (see Texas Estates Code Section 201.003(b)). But Evelyn's husband had two children born from a previous marriage. Under Section 201.003(c) of the Texas Estates Code, this meant that her late husband's interest did not pass to her but rather to her husband's three children:

> If the deceased spouse is survived by a child or other descendant who is not also a child or other descendant of the surviving spouse, the deceased spouse's undivided one-half interest in the community estate passes to the deceased spouse's children or other descendants. The descendants inherit only the portion of that estate to which they would be entitled under Section 201.101. In every case, the community estate passes charged with the debts against the community estate." (Texas Estates Code Section 201.003(c)).

The estate then pointed to the requirements of the Texas Constitution governing reverse mortgages that state a reverse mortgage requires the consent of all owners and their spouses (see Texas Constitution Article XVI, Section 50(k)(1)) and argued that there was no evidence that the three children of Evelyn's husband along with their spouses consented to the reverse mortgage. Therefore, the estate argued that the foreclosure order should be overruled as the Texas Constitutional requirements were not met.

The appellate court agreed with the estate's arguments and reversed the trial court's findings that the reverse mortgage met the Texas Constitution and reversed the foreclosure order (the appellate court affirmed the trial court's decision on the TDCA issue). The appellate court remanded the case back to the trial court for a trial to determine whether the children and their spouses consented to Evelyn's reverse mortgage as well as other issues including whether the mortgage holder was equitably subrogated to the amount of any valid liens paid off by the reverse mortgage (these other issues were mooted by the trial court).
The takeaway from this case is that Texas lenders should be cautious in situations in which an owner has passed away. On first-lien products, which generally have a lender's title insurance policy, the loan policy will provide protection to reassure a cautious lender—and in course of providing title insurance, the insurer will investigate these matters to establish ownership. However, in current market conditions, second lien HELOCs and second lien closed-end home equity loans have become more common. Under normal circumstances, whether to obtain a lender's title insurance policy on a second lien product is up to a lender's risk assessment and business judgment depending on factors such as the loan amount. However, in any situation in which an owner has passed away, Black, Mann and Graham LLP strongly recommends obtaining a lender's title insurance policy on loan products due to Texas inheritance law complexities.