16-20

No. _____

In The

Supreme Court of the United States

DAVID BILLINGS, TRESSA BILLINGS, BLANCA TORRES, CHERYL THIERY and DAVID LEONARD OROSCO

Petitioners

v.

PROPEL FINANCIAL SERVICES, L.L.C., TEXAS TAX SOLUTIONS, L.L.C., and OVATION LENDING, L.L.C.,

Respondents

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

Introductory Statement

The Petitioners obtained property tax loans secured by liens against their homes from Respondents. These loans were made pursuant to the Texas statutes authorizing licensed property tax lenders to make secured loans to property owners to pay property taxes. The Petitioners maintain that the loans constitute the extension of "credit" under the federal Truth in Lending Act in accordance with the clear and unambiguous provisions of the Act, Regulation Z (the rule implementing the Act), and the Official Staff Interpretations of Regulation Z.

Question Presented

The question presented is whether the Fifth Circuit erred in holding the loans are *not* extensions of "credit" under the Act, and, accordingly, are *not* governed by the Act. This important question of federal law has not been resolved by the Supreme Court. If the Fifth Circuit's holding stands, thousands of Texas homeowners will be denied consumer protections mandated by Congress under the Act. The Consumer Financial Protection Bureau, the federal agency with jurisdiction over the Act, deemed this case to be sufficiently important to file an *amicus* brief in support of the Petitioners, and, at the Bureau's request, participate in oral argument before the Fifth Circuit. The National Association of Consumer Attorneys and the Texas Family Council also filed *amici* briefs in support of the Petitioners.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners David Billings, Tressa Billings, Blanca Torres, Cheryl Thiery and David Leonard Orosco respectfully submit this petition for a writ of certiorari for review of the judgment of the Fifth Circuit Court of Appeals.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit, filed on April 29, 2016, is reported at *Billings v. Propel Fin. Servs., L.L.C.*, 2016 U.S. App. LEXIS 7843, and is reprinted in Appendix A.

The order of the United States District Court for the Western District of Texas of February 9, 2015 in *Orosco v. Ovation Lending, LLC*, No. 5:14-cv-897 (5th Cir. No. 15-50437), denying Respondent Ovation Lending, L.L.C.'s Motion to Dismiss, is unpublished, and is reprinted in Appendix B.

The order of the United States District Court for the Western District of Texas of January 22, 2015 in *Torres v. Propel Financial Services, LLC*, No. 5:14-cv-1040 (5th Cir. No. 15-50199), denying Respondent Propel Financial Services, L.L.C.'s Motion to Dismiss, is unpublished, and is reprinted in Appendix C.

The amended order of the United States District Court for the Western District of Texas of January 15, 2015 in *Thiery v. Texas Tax Solutions, LLC*, No. 5:14-cv-940 (5th Cir. No. 15-50340), denying Respondent Propel Financial Services,

L.L.C.'s Motion to Dismiss in pertinent part, is unpublished, and is reprinted in Appendix D.

The order of the United States District Court for the Western District of Texas of November 28, 2014 in *Billings v. Propel Financial Services, LLC*, No. 5:14-CA-764 (5th Cir. No. 14-51326), granting Respondent Propel Financial Services, L.L.C.'s Motion to Dismiss, is reported at *Billings v. Propel Fin. Servs., LLC*, 2014 U.S. Dist. LEXIS 179738, and is reprinted in Appendix E.

The order of the Fifth Circuit denying a rehearing and rehearing *en banc*; filed on May 27, 2016, is unpublished, and is reprinted in Appendix F.

JURISDICTION

The Fifth Circuit rendered its decision on April 29, 2016 and denied the Petitioners' petition for rehearing and rehearing *en banc* on May 27, 2016. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS AT ISSUE

15 U.S.C. § 1602(f)

The term "credit" means the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment.

12 C.F.R. § 1026.2(a)(14)

Credit means the right to defer payment of debt or to incur debt and defer its payment.

12 C.F.R. § 1026, Supp. I, Sub. A, cmt. 2(a)(14)(1)(ii)

The following situations are not considered credit for purposes of the regulation:

. . .

Tax liens, tax assessments, court judgments, and court approvals of reaffirmation of debts in bankruptcy. However, third-party financing of such obligations (for example, a bank loan obtained to pay off a tax lien) is credit for purposes of the regulation.

STATEMENT OF THE CASE

A. Facts Giving Rise To This Case

1. Texas Property Tax Loans.

Each of the credit transactions involved in this case is a "property tax loan"[1] made by a "property tax lender"[2] under Texas law. Under the Texas Tax Code a property owner may authorize a property tax lender to pay property taxes owed by the property owner. Tex. Tax Code § 32.06(a-1). Upon the

[1] *See* Tex. Fin. Code § 351.002(2).

[2] *See* Tex. Fin. Code § 351.002(1).

payment by the property tax lender of the taxes, penalty, interest and collection costs owed by the property owner, the property tax lender is issued a receipt evidencing that the tax obligation has been paid and receives a transfer of the taxing units' tax lien against the subject property. *Id.* §§ 32.06(a-2); 32.06(b). Only the tax *lien* is transferred and assigned to the third-party lender, not the tax *claim* that the tax lien secures. *Id.* § 32.06(a-2). The property tax lender is "subrogated to and is entitled to exercise any right or remedy possessed by the transferring taxing unit, including or related to foreclosure or judicial sale . . . ." *Id.* § 32.065(c). The taxing unit's tax lien is a "super-priority" lien, in that it "is always senior to and has priority over other liens." *ABN AMRO Mort. Group v. TCB Farm and Ranch Land Invs.*, 200 S.W.3d. 774, 779 (Tex.App.—Fort Worth 2006, no pet.). The property tax lender's lien that it obtains as transferee has the same priority as the lien enjoyed when possessed by the taxing units. *Id.*

The principal amount of the property tax loan may include not only the amount of the tax obligation, but also numerous and sundry additional closing costs and fees the property tax lender is authorized to advance and include in the loan (such as loan application, processing and underwriting fees, title research fees, appraisal fees and recording fees). Tex. Tax Code § 32.06(e); 7 TAC § 89.601. The property owner executes a new promissory note evidencing the total indebtedness owed to the property tax lender (the amount of the discharged tax obligation plus closing costs and fees), which is secured by the transferred tax lien. Tex. Tax Code §§ 32.065(a); 32.06(b); 32.06(e).

2. The Property Tax Loans To The Petitioners.

In each of the four consolidated cases the Respondents made property tax loans to the Petitioners. Each loan was evidenced by a new promissory note executed by the borrower (Petitioner) and payable to the lender (Respondent).[3] The promissory notes were each secured by a lien against the principal dwelling of the borrower transferred to the lender by the taxing authorities.[4] The promissory note executed by Petitioners David Billings and Tressa Billings is reprinted in Appendix G.[5] The promissory notes executed by the other Petitioners are identical to the one executed by the Billings in all respects pertinent to the issues on appeal.[6] The principal amounts of the promissory notes included not only the amount of the discharged tax obligations, but additional closing costs and fees charged to the Petitioners as well.[7]

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[3] *See* App. a61–a75; R. 15-50199.19–22; R. 15-50340.24–25; R. 15-50437.20–21.

[4] *See* App. a62; R. 15-50199.19; R. 15-50340.24; R. 15-50437.20.

[5] Although the instrument is titled "Property Tax Payment Agreement," it is a promissory note under Texas law, because it is a written instrument that "is signed by the maker; contains an unconditional promise or order to pay a sum certain; is payable on demand or at a definite time; and is payable to order or bearer." *Texmarc Conveyor Co. v. Arts*, 857 S.W.2d 743, 746 (Tex. App.—Houston [14th Dist.] 1993, writ denied).

[6] *See* R. 15-50199.19–22; R. 15-50340.24–25; R. 15-50437.20–21.

[7] *See* R. 14-51326.9; R. 15-50199.19-22; R. 15-50340.24–25; R. 15-50437.20–21.

3. The Truth In Lending Act.

The federal Truth in Lending Act[8] ("TILA") was passed by Congress in 1968 and was originally Title I of the Consumer Credit Protection Act. The regulations implementing the statute are known as Regulation Z.[9] The Homeowner Equity and Protection Act[10] ("HOEPA") was enacted in 1994 as an amendment to TILA to "protect vulnerable consumers from some predatory lending practices by providing additional consumer protections for a class of closed-end, non-purchase-money, relatively expensive home mortgage loans."[11] In 2008, the Federal Reserve Board adopted amendments to Regulation Z imposing additional restrictions and requirements applicable to these types of loans.[12] In the same vein, the Dodd-Frank Wall Street Reform and Consumer Protection Act[13] ("Dodd-Frank"), enacted by Congress in 2010, amended TILA to provide additional protections to borrowers that take out high interest-rate loans secured by their homes.[14] The Consumer Financial Protection Bureau ("CFPB"), created under Dodd Frank,[15] is the federal agency charged with the responsibility to interpret TILA and to promulgate rules to effectuate its

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[8] Pub. L. No. 90-321, 82 Stat. 146 (1968); 15 U.S.C. §§ 1601–1666j.

[9] 12 C.F.R. part 1026.

[10] Pub. L. No. 103-325, § 151 et seq., 108 Stat. 2160 (1994).

[11] National Consumer Law Center, Truth In Lending § 9.6.1.1 (Ninth Edition).

[12] 73 Fed. Reg. 44,522 (July 30, 2008).

[13] Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[14] *Id.* § 1011.

[15] *Id.* §§ 1400–1498.

purposes.[16] The CFPB has issued a series of rules amending Regulation Z to implement Dodd-Frank's changes to HOEPA.[17]

Under the current regulatory regime, a "consumer credit transaction" secured by a consumer's principal dwelling with an "annual percentage rate" which exceeds specified thresholds set out in HOEPA (depending on whether the loan is secured by a first lien or junior lien) is classified as a "high-cost mortgage" thereunder,[18] and is subject to a number of additional consumer protection provisions set out therein.[19] The interest rates charged by the Respondents for the Petitioner loans ranges from a low of 11.9 % per annum to a high of 15.9 % per annum.[20] The loans are secured by the Petitioners' homes. *See infra* p. 5. Accordingly, the Petitioners maintain that all of the loans qualify as "high-cost mortgages" under HOEPA, and are accordingly regulated under HOEPA as well as the provisions of TILA and Regulation Z that apply to the broader residential mortgage market.

The consumer protections afforded by TILA and HOEPA apply to the offering of "consumer credit" by "creditors" as those terms are defined by TILA. *See* 15 U.S.C. § 1602(f), (g), (i). The central

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[16] *See* 12 U.S.C. §§ 5481(12)(O); 5512(b)(1), (4); 15 U.S.C. § 1604(a).

[17] *See* 78 Fed. Reg. 68,343 (Nov. 14, 2013); 78 Fed. Reg. 62,993 (Oct. 23, 2013); 78 Fed. Reg. 60,381 (Oct. 1, 2013); 78 Fed. Reg. 35,429 (June 12, 2013); 78 Fed. Reg. 25,638 (May 2, 2013); 78 Fed Reg. 6856 (Jan. 31, 2013).

[18] *See* 15 U.S.C. § 1602(bb)(1)(A)(ii).

[19] *See* National Consumer Law Center, Truth In Lending §§ 9.7.6; 9.7.10; 9.7.11 (Ninth Edition).

[20] *See* App. a61; *See* App. a62; R. 15-50199.19; R. 15-50340.24; R. 15-50437.20.

issue on appeal is whether the loans to the Petitioners constitute "consumer credit" under TILA. *See* App. a10. The Fifth Circuit held that the loans do not constitute "credit" under TILA. *See* App. a16. The Fifth Circuit determined that it need not reach the issue of whether the loans are *consumer* credit. *See* App. a16, n.3.

TILA is a remedial statute, and is to be enforced strictly against creditors and construed liberally in favor of consumers. *Begala v. PNC Bank*, 163 F.3d 948, 950 (6th Cir. 1998); *Fairley v. Turan-Foley Imports, Inc.*, 65 F. 3d 475, 482 (5th Cir. 1995).

B. The District Court Proceedings.

No. 14-51326; DAVID BILLINGS; TRESSA BILLINGS, *Plaintiffs-Petitioners* v. PROPEL FINANCIAL SERVICES, L.L.C., *Defendant-Respondent*

On August 27, 2014, Petitioners David Billings and Tressa Billings filed a class action suit against Respondent Propel Financial Services. L.L.C. in the United States District Court, Western District of Texas, San Antonio Division, bearing Civil Action No. 5:14–cv–764. Petitioners' Complaint alleges numerous violations or TILA and HOEPA, and seeks statutory damages recoverable under TILA. Therefore, the court has subject matter jurisdiction pursuant to 28 U.S.C. § 1331. On November 28, 2014 the district court granted Respondent's Rule 12(b)(6) Motion to Dismiss. The Petitioners timely filed their Notice of Appeal on December 22, 2014.

No. 15-50199; BLANCA TORRES, *Plaintiff-Petitioner* v. PROPEL FINANCIAL SERVICES, L.L.C., *Defendant-Respondent*

On November 24, 2014 Petitioner Blanca Torres filed a class action suit against Respondent Propel Financial Services. L.L.C. in the United States District Court, Western District of Texas, San Antonio Division, bearing Civil Action No. 5:14–cv–1040. Petitioner's Complaint alleges numerous violations or TILA and HOEPA, and seeks statutory damages recoverable under TILA. Therefore, the court has subject matter jurisdiction pursuant to 28 U.S.C. § 1331. On January 22, 2015, the district court denied Respondent's Rule 12(b)(6) Motion to Dismiss and certified the case for an immediate interlocutory appeal to the Fifth Circuit. On March 10, 2015, the Fifth Circuit granted Respondent's petition for leave to appeal from the interlocutory order of the district court. On June 19, 2015, the clerk of the Fifth Circuit granted Petitioner's motion that the case be consolidated with case nos. 14-51326, 15-50340, and 15-50437.

No. 15-50340; CHERYL THIERY, *Plaintiff-Petitioner* v. TEXAS TAX SOLUTIONS, L.L.C., *Defendant-Respondent*

On October 24, 2014 Petitioner Cheryl Thiery filed a class action suit against Respondent Texas Tax Solutions, L.L.C. in the United States District Court, Western District of Texas, San Antonio Division, bearing Civil Action No. 5:14–cv–940. Petitioner's Complaint alleges numerous violations or TILA and HOEPA, and seeks statutory damages

recoverable under TILA. Therefore, the court has subject matter jurisdiction pursuant to 28 U.S.C. § 1331. On December 19, 2014, the district court denied Respondent's Rule 12(b)(6) Motion to Dismiss. On January 1, 2015, the district court withdrew and vacated its December 19, 2014 order. On January 15, 2015, the district issued an amended order denying Respondent's Rule 12(b)(6) Motion to Dismiss and certified the case for an immediate interlocutory appeal to the Court. On March 10, 2015, the district court granted Respondent's petition for leave to appeal from the interlocutory order of the district court. On July 15, 2015, the Fifth Circuit granted Respondent's petition for leave to appeal from the interlocutory order of the district court, and ordered that the case be consolidated with case no. 14-51326.

No. 15-50437; DAVID LEONARD OROSCO, *Plaintiff-Petitioner* v. OVATION LENDING, L.L.C., *Defendant-Respondent*

On October 14, 2014 Petitioner David Leonard Orosco filed a class action suit against Respondent Ovation Lending, L.L.C. in the United States District Court, Western District of Texas, San Antonio Division, bearing Civil Action No. 5:14–cv–897. Petitioner's Complaint alleges numerous violations or TILA and HOEPA, and seeks statutory damages recoverable under TILA. Therefore, the court has subject matter jurisdiction pursuant to 28 U.S.C. § 1331. On February 9, 2015, the district court denied the Respondent's Rule 12(b)(6) Motion to Dismiss Petitioner's TILA claims. On April 28, 2015, the district court certified the case for an immediate

interlocutory appeal to the Fifth Circuit. On May 19, 2015, the Fifth Circuit granted Respondent's petition for leave to appeal from the interlocutory order of the district court, and ordered that the case be consolidated with case no. 14-51326.

C. The Appellate Court Proceedings.

On April 29, 2016, the Fifth Circuit filed its opinion affirming the judgment of the district court in case no. 14-51326, and reversing the judgments of the district courts in case nos. 15-50437, 15-50340 and 15-50199. On May 27, 2016, the Fifth Circuit filed its order denying the Petitioners' petition for rehearing and rehearing *en banc*.

REASONS FOR GRANTING THE PETITION

I.

If The Fifth Circuit's Holding Is Not Reversed, Thousands Of Texas Homeowners Will Be Denied The Protections Afforded To Consumers Under TILA

The holding of the Fifth Circuit, if allowed to stand, will adversely impact not only the Petitioners, but thousands of Texas homeowners. The Texas Office of Consumer Credit Commissioner (the "OCCC") is the Texas regulatory agency with jurisdiction over the property tax lending industry in that state. According to the most recent annual property tax lending statistics compiled by the OCCC, in 2014 74 licensed property tax lenders

reported making a total of 13,471 property tax loans during the year. Of that total, 11,692 loans, or 86%, were residential loans.[21] The impact of the Fifth Circuit's ruling, if not reversed by this Court, is that Texas consumers who obtain property tax loans to pay off taxes assessed against their homes will be denied the protections that Congress has mandated they are entitled to under TILA.

II.

The Fifth Circuit Erred In Holding That The Loans To The Petitioners Do Not Constitute The Extension Of "Credit" Under TILA

A. The Fifth Circuit's Opinion Is Inconsistent With The Plain, Unambiguous Language Of TILA, Regulation Z, And The Official Staff Interpretations Of Regulation Z.

The loans are subject to TILA if they constitute "consumer credit" transactions under TILA. *See* 15 U.S.C. § 1602(f), (g), (i). The first level of analysis in this regard is whether the loans constitute "credit" under TILA. The term "credit" as used in TILA is defined very broadly to mean "the right to defer payment of debt or to incur debt and defer its payment." 15 U.S.C. § 1602(f); *see also* 12

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[21] *See* Texas Office of Consumer Credit Commissioner Property Tax Lending Consolidated Volume Report, Calendar Year 2014 (available at http://occc.texas.gov/sites/default/files/uploads/reports/ ptl-consolidated-2014.pdf).

C.F.R § 1026.2(a)(14). The term "debt" is not defined under TILA, and thus the meaning of that term is established under state law. 12 C.F.R § 1026.2(b)(3). Under Texas law the term is given its ordinary, commonly-understood meaning. "In legal usage, the word 'debt' refers ordinarily to a liquidated money obligation that is legally enforceable by the owner; that is to say, the legally enforceable obligation must be for a sum certain in money." *Cain v. State*, 882 S.W.2d 515, 516 n.1 (Tex. App.—Austin 1994, no writ) (emphasis removed).

Under this definition the promissory notes in question are clearly "debts" for purposes of TILA. They each contain a "promise to pay" the principal amount plus interest at the stated rate.[22] Moreover, by the terms of each note the payment of the debt is *deferred*—the principal amount is payable in monthly installments over time together with accrued interest.[23] It follows then that the loans to the Petitioners that are evidenced by the notes constitute the extension of "credit" under TILA. As stated by the CFPB in its *amicus* brief, "the property-tax loan between [Respondent] and the [Petitioner], in both form and substance, comfortably falls within TILA's definition of 'credit.'" CFPB Br. 23, ECF No. 00512999950. A property tax loan, in the CFPB's view, "is the quintessential example of an extension of credit of the type that TILA regulates." CFPB Br. 19.

District Judge Hudspeth, in his rulings denying the Respondents' Motions to Dismiss in *Torres* and *Thiery*, framed the issue as follows:

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[22] *See* App. a62; R. 15-50199.19; R. 15-50340.24; R. 15-50437.20.
[23] *Id.*

> Under TILA, the term 'credit' means 'the right to defer payment of debt or to incur debt and defer its payment.' TILA does not define the term 'debt,' so that term is defined by state law. Under Texas law, a tax lien is not a debt, but an obligation that arises by virtue of property ownership. The [Respondent] argues that the transaction between it and the [Petitioner] does not involve an extension of credit.

App. a34, a43–a44 (citations omitted). After then discussing at length the Respondents' arguments and authorities (App. a34–a38, a44–a47), Judge Hudspeth ultimately rejected those arguments, concluding that in both cases "the [Petitioner's] property tax loan *was* an extension of credit." App. a38, a47 (emphasis added).

The Fifth Circuit finds, somewhat cryptically, that the "transfers and promissory notes did not *create* new debts that would be subject to TILA, but rather transferred existing tax obligations, which are not 'debts' subject to TILA." App. a18. This language can only be read to mean that in the court's view the promissory notes *are not* "debts" under Texas law. This finding is not only contrary to Texas law (*see infra* p. 13), but to all common sense as well. The Petitioners concede that *tax obligations* are not considered "debt" under Texas law. *See Rochelle v. City of Dallas,* 264 F.2d 166, 169 (5th Cir. 1959); *Highland Park Independent School District v. Thomas*, 139 S.W.2d 299, 301 (Tex. Civ. App.–Dallas, 1940, no writ). The question is whether the promissory notes are "debts" or "tax obligations." They must be one or the other. The Fifth Circuit

finds, in effect, that they are the latter. But the notes are not tax obligations—they are debts incurred to a third party to *discharge* tax obligations.

Moreover, *because* the purpose of the loans is to discharge the Petitioners' tax obligations, as averred by the CFPB the "official interpretation to Regulation Z . . . eliminates any doubt" about the issue of whether the loans are "credit" under TILA. CFPB Br. 19. The Staff Interpretations provide that while "tax liens, tax assessments, court judgments, and court approvals of reaffirmation of debts in bankruptcy" are not considered credit for purposes of Regulation Z, "*third-party financing* of such obligations (for example, a bank loan obtained to pay off a tax lien) *is* credit for purposes of the regulation." 12 C.F.R. § 1026, Supp. I, Sub. A, cmt. 2(a)(14)(1)(ii) (emphasis added).

The loans to the Petitioners plainly evidence such "third-party financing" of the Petitioners' tax obligations, and accordingly clearly constitute "credit" under TILA. As held by District Judge Pitman in his order denying the Motion to Dismiss filed by the Respondent in *Orosco*, a Texas property tax loan "is precisely the sort of financing identified by the Board in its Staff Commentary as subject to the requirements of TILA." App. a31. The CFPB's position is in full accord with Judge Pitman's decision:

> Under the district court's decision [in *Billings*] . . . companies specializing in property tax-lending would be exempt from TILA's requirements because the funds they advance would not be considered 'credit.' Such a result cannot be reconciled with either the official interpretation of

> Regulation Z—which makes clear that TILA applies to all 'third-party financing of [tax] obligations'—or the animating purpose behind Congress' enactment of TILA.

CFPB Br. 27-28.

As the Fifth Circuit correctly notes, the Petitioners rely "primarily on the staff commentary to Regulation Z," and "contend that the tax lien transfers at issue here constitute third-party financing of tax obligations." App. a15. Curiously, however, the Fifth Circuit does not explain, or make any attempt to explain, why the loans to the Petitioners *do not* constitute third-party financing of the Petitioners' tax obligations. The failure to do so constitutes a glaring omission from the opinion. The Petitioners submit that the language of the Staff Interpretations is so clear and unambiguous that the *only* reasonable interpretation thereof is that the loans *are* third-party financings of the Petitioners' tax obligations, and accordingly *do* constitute the extension of "credit" under TILA, contrary to the holding of the Fifth Circuit.

The rule is well established that, unless demonstrably irrational, the Staff Interpretations should be dispositive. *Ford Motor Credit Co. v. Milhollin*, 444 U.S. 555, 565 (1980). Judge Pitman, in considering the rationality of the Staff Interpretations in *Orosco*, held that "[t]he staff opinion is not demonstrably irrational and . . . TILA and HOEPA are 'best construed by those who gave it substance in promulgating regulations thereunder.'" App. a25 (quoting *Ford*, 444 U.S. at 566). In the same vein, the CFBP finds the Staff Interpretation's "conclusion that 'credit' encompasses 'third-party

financing' of tax obligations 'eminently rational.'" CFPB Br. 26.

B. The Holding Of *Kizzee-Jordan* That The Underlying Tax Claim Is Not Extinguished When A Property Tax Loan Is Made To A Property Owner Is Not In Accord With Texas law.

1. The Promissory Notes Work A Novation Of The Tax Claims And Extinguish Them.

Central to the Fifth Circuit's opinion is it's holding in *Kizzee-Jordan,* 626 F.3d 239 (5th Cir. 2010), that under the Texas statutory scheme when a property tax loan is made to a property owner and the taxes are paid by the lender the "tax claim is *not* extinguished." App. a16. The Fifth Circuit concludes that as a result the loan transaction does not give rise to a "debt" subject to TILA:

> Applying our holding in *In re Kizzee-Jordan* to the instant cases, it is clear that the payments made by defendants to the relevant taxing authorities and the subsequent transfer of the tax liens and execution of the promissory notes did not extinguish the original tax obligations, but rather, simply transferred the preexisting tax obligations to new entities. Thus, the transfers and promissory notes did not create new debts that would be subject to TILA, but rather transferred existing tax obligations, which are not "debts" subject to TILA.

App. a18.

Under the reasoning adopted by the Fifth Circuit, a property tax loan apparently results in the existence of *two* separate debts—the "underlying debt" (App. a17) and the debt evidenced by the new promissory note. This of course is not the case. There is but one resulting debt, the debt evidenced by the new promissory note. Under Texas law, the new promissory note works a novation of and does in fact extinguish the original tax claim in its entirety. In Texas "[n]ovation is a mode of extinguishing one obligation for another—the substitution . . . of a new obligation in lieu of the old one—the effect of which is to pay or otherwise discharge it." *Cooper Grocery Co. v. Strange*, 18 S.W.2d 609, 612 (Tex. 1929); *see also Chastain v. Cooper & Reed*, 257 S.W.2d 422, 424 (Tex. 1953) ("[A] second contract will operate as a novation of a first contract only when the parties to both contracts intend and agree that the obligations of the second shall be substituted for and operate as a discharge of the obligations of the first."). Whether or not a novation has occurred is "ordinarily a question of fact, dependent upon the intention of the parties; but where there is no doubt as to the terms of the agreement it is a question of law." *Cooper*, 18 S.W.2d at 613.

Petitioners maintain that there can be no reasonable doubt that the original tax claims against them have been extinguished through novation. The Respondents could have relied on their statutory subrogation rights to collect the amounts advanced to pay the Petitioners' tax obligations. Petitioners are aware of no Texas law that would have prevented

them from doing so.[24] In that event, Petitioners concede that the tax claims would not have been extinguished, and would have survived in favor of the Respondents. The Respondents elected instead to substitute new debts under new terms (evidenced by the promissory notes) (*see infra* p. 5) for the existing tax claims, which are paid off and extinguished in the process.

A helpful way to view property tax loans from a structural standpoint is to consider a common analogous transaction, being the refinancing of a typical residential mortgage loan, which Petitioners assert for all intents and purposes is structurally identical to a property tax loan. In a typical transaction, the new lender will (i) have the borrower sign a new promissory note and deed of trust, and (ii) deliver the proceeds of the new loan directly to the existing lender.[25] The existing lender will, in turn, (i) endorse and deliver its promissory note to the new lender, and (ii) assign its deed of trust lien to the new lender.[26] In that situation, clearly the new promissory note is intended to and does, as a matter of law, work a novation of the existing promissory note and extinguish it. *See infra* pp.18–19. The new lender is not free to pick and choose which note to enforce. In the same vein a property tax lender is not free to pick and choose whether to assert the "unextinguished" tax claim or enforce its rights

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[24] By not doing so the Respondents were able to charge a higher rate of interest and include additional closing costs and fees in the principal balance of the loan. *See* App. a18; *infra* p. 4.

[25] *See* State Bar of Tex., Texas Real Estate Forms Manual (Second Edition, 2011) §22.2:8, at 22-3; Form 22-4, at 22-4-1.

[26] *Id.*

under the new promissory note executed by the borrower. Only the latter is available. *Id.*

2. The Fact That A Lien Cannot Be Assigned Without The Underlying Claim Also Being Assigned Does Not Support A Finding That The Tax Claim Is Not Extinguished.

The Fifth Circuit's holding that the tax claim is not extinguished in a property tax loan transaction rests in part on its finding in *Kizzee-Jordan* that under Texas law "a lien cannot be assigned without the underlying claim also being assigned to the new lienholder, and thus the tax lien could not be assigned if the tax claim had been extinguished by the lender's payment to the taxing authority." App. a16. But just because the underlying claim is assigned to a new lender it does not follow that the claim is therefore not extinguished. In a typical mortgage loan refinancing transaction in Texas, the existing note and lien are both transferred to the new lender. *See infra* p. 19. Upon the execution of the *new* promissory note, the *existing* promissory note is extinguished. *Id.* By the same token, in a property tax loan transaction the existing tax claim, although transferred as a matter of law to the property tax lender, is extinguished upon the execution of the new promissory note by the borrower.

3. The Fact That The Taxing Entity's Receipt Is Issued To The Property Tax Lender Does Not Support A Finding That The Tax Claim Is Not Extinguished.

Another rationale provided by the Fifth Circuit in reaching its conclusion in *Kizzee-Jordan* that the tax claim is not extinguished in a property tax loan transaction, is that under the Texas statutory scheme the tax collector issues a tax receipt to the property tax lender, and that "[i]f the tax claim against the property owner were extinguished, the tax collector would issue the tax receipt to that property owner, not the transferee." *Kizzee-Jordan*, 626 F. 3d at 244; *see* App. a16. The Fifth Circuit attaches wholly unwarranted significance to the fact that the tax receipt is issued to the property tax lender, which merely establishes the fact that the taxes have been paid. *See* Tex. Tax Code § 31.075(a). The tax receipt "constitutes prima facie evidence that the tax has been paid as stated by the receipt." Tex. Tax Code § 31.075(b). In terms of its legal effect it is wholly immaterial to whom the tax receipt is issued. No rights or privileges are transferred to the property tax lender by virtue of the issuance of the tax receipt. *See* Tex. Tax Code §§ 31.075, 32.06(b). The clerical act of issuing the tax receipt to the property tax lender on the one hand and the extinguishment of the tax claim through novation on the other are entirely consistent with one another.

4. The Extinguishment Of The Tax Claim Does Not Obviate The Need For Subrogation Rights.

A final rationale provided by the Fifth Circuit in reaching its conclusion that the tax claim is not extinguished is that

> the transferee is subrogated to all the rights and remedies of the taxing authorities upon transfer of the lien, reasoning that '[i]f the tax claim were extinguished . . . and replaced by a new debt, . . . the transferee could simply prosecute the new debt[,]' and there would be no need to provide for rights of subrogation.

App. a17 (quoting *Kizzee-Jordan,* 626 F.3d at 245) (alterations in original). This analysis overlooks the fact that when a property tax loan is made the underyling tax claim *is* in fact extinguished, and the property tax lender *does* in fact "prosecute the new debt," to-wit: the new promissory note, and not the "underlying tax claim." *See infra* pp. 18–19. Subrogation rights are *still* critical, however, because the property tax lender has rights of subrogation with respect to the *lien rights* of the taxing entity, which are transferred to the property tax lender and through which the property tax lender obtains the same super-priority lien rights securing its new promissory note as the taxing entity held to secure the original tax claim. *Id.* p. 4. The fact that the underlying tax claim is extinguished does not, then, compel a finding that there would therefore "be no need to provide for rights of subrogation."

C. The Fifth Circuit's Opinion Provides A Roadmap To A State Legislature Desiring To Exempt From TILA A Class Of Loans Made In That State.

The Fifth Circuit's ruling, if not reversed, will provide a ready roadmap to a state legislature seeking to adopt the Texas property tax lending model, but believing TILA and Regulation Z to be unduly burdensome. The state legislature could effectively exempt that class of loans simply by providing in the statutory scheme that (i) the tax receipt is issued by the taxing units to the lender, (ii) the tax lien as well as the tax claim is transferred to the lender, and (iii) the lender is subrogated to the rights and remedies of the taxing units.

Under such a scenario, even if the lender requires that the homeowner execute a new promissory note which would otherwise clearly constitute the extension of "credit" under TILA, the lender may arguably, in light of the Fifth Circuit's holding, conduct its business free from worry as to the requirements of TILA and HOEPA because "the underlying tax obligation" has not been "extinguished." *See infra* p. 17. A state's legislative body, of course, has no say whatsoever in what loan transactions entered into in that state do or do not constitute "consumer credit" transactions for purposes of TILA–only Congress may make that determination.

D. Even If The Underlying Tax Claim Is Not Extinguished In A Property Tax Loan Transaction Under Texas Law, That Fact Has No Bearing On Whether The Loan Is Subject To TILA.

As explained above, the Staff Interpretations mandate that a third-party financing of a tax obligation is "credit" for purposes of TILA. *See infra* pp. 15–16. Whether or not the underlying tax obligation is "extinguished" or not is irrelevant in this analysis. The Staff Interpretations draw no distinction between third-party financings which "extinguish" the tax obligation under applicable state law and those that do not. *See* 12 C.F.R. § 1026, Supp. I, Sub. A, cmt. 2(a)(14)(1)(ii). All that is required is that a third-party financing of the obligation occur, which the Petitioners have shown is quite clearly the case. *See infra* pp. 15–16.

E. The Fifth Circuit's Opinion Fails To Recognize That The Loans Finance Not Only The Petitioner's Tax Obligations, But Also Additional Costs And Fees Charged To The Petitioners.

At the heart of the Fifth Circuit's opinion is the holding that "the transfers and promissory notes did not *create* new debts that would be subject to TILA, but rather transferred existing tax obligations, which are not 'debts' subject to TILA." App. a18. A key fact that the Fifth Circuit overlooks in its analysis is that the promissory notes finance not only the Petitioners' tax obligations, but also additional costs and fees the defendants are authorized under Texas law to charge the Petitioners. *See infra* p. 4.

Even assuming *arguendo* that the principal amount of the notes *representing the tax obligations* are not "debts" under TILA, the same cannot be said for such additional costs and fees. As to those financed sums, they squarely fall within the meaning of the term "debt" under Texas law. *Id.* p. 13. Accordingly, the loan of those funds to the Petitioners by the Respondents constitutes the extension of "credit" under TILA. *Id.* . Contrary to the Fifth Circuit's assertion that the promissory notes "did not *create* new debts that would be subject to TILA," (App. a18) it is abundantly clear that the promissory notes, in part at the *very* least, do exactly that.

F. The *Pollice* Case Is Distinguishable From The Cases At Bar.

The Fifth Circuit cites *Pollice v. National Tax Funding, L.P.*, 225 F.3d 379 (3d Cir. 2000) in support of its holding. App. a18, n.4. The facts of *Pollice*, however, are fundamentally different from those in the cases at bar. *Pollice* dealt with delinquent tax obligations in the state of Pennsylvania. *See Pollice*, 225 F.3d at 385. The case did not involve Texas property tax loans in any respect. In *Pollice*, various taxing units accumulated a backlog of thousands of claims for delinquent property taxes. *Id.* The taxing units, in a factoring arrangement, sold the delinquent accounts in bulk to a third party at a discount. *Id.* The purchaser thereby became the owner of the accounts. *Id.*

Here it is important to understand that the Texas and Pennsylvania statutory regimes are fundamentally different. The Texas statutory regime authorizing property tax lenders to make property tax loans is unique to Texas. Texas does not permit

the *per se* selling and purchasing of delinquent tax accounts (i.e. the factoring of those accounts), which is allowed in Pennsylvania.[27] No other state follows the Texas model authorizing third-party property tax lenders to make tax loans to homeowners to pay off their tax obligations.[28] Under the Texas statutory scheme only the tax lien is transferred and assigned, not the tax claim that the tax lien secures. *See infra* p. 4. The transferred tax lien secures the repayment of the new promissory note executed by the homeowner. *Id.*

Subsequent to the sale of the accounts, the purchaser in *Pollice* then entered into payment plans with a number of the property owners deferring their obligation to pay the taxes owed. *See Pollice*, 225 F.3d at 386. The *Pollice* court reasoned that the payment plans constituted merely the granting of a right to defer payment of tax obligations, which are not "debts," and thus there was no extension of "credit" under TILA. *Id.* at 410. Unlike the Petitioners, the Pennsylvania property owners did not borrow funds from a third-party lender to pay off their property taxes. The distinction is critical, since it is the very fact that the Petitioners borrowed funds from third-party lenders to pay off their property taxes that causes the transactions to fall under TILA's ambit. *See infra* pp. 12–13, 15–16. The *Pollice* court in fact acknowledged the distinction, holding that the payment plans at issue were "not analogous to the situation in which a third party, such as a bank, makes a loan to a consumer which is then used

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[27] *See* Thomas Bonura, *Misdirected Hostility: Are Criticisms of Texas Property Tax Lenders Justified?*, 53 S. Tex. L. Rev. 569 at 572 (2012).

[28] *Id.*

to satisfy a tax obligation." *Pollice*, 225 F.3d at 410. If that were the case, reasoned the court, pursuant to the clear language of the Staff Interpretations, the third-party loan *would* be an extension of "credit" for purposes of TILA. *Id.*

CONCLUSION

For the foregoing reasons, Petitioners David Billings, Tressa Billings, Blanca Torres, Cheryl Thiery and David Leonard Orosco request the Court grant this petition for writ of certiorari.

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Respectfully submitted.

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APPENDIX