

## Transfers of Tax Liens to Tax Lenders: What You Don't Know Can Hurt You!

By Barry D. Johnson



Many lenders who do not escrow for real property taxes take a rather passive attitude toward their customers' payment of tax bills. However, a lender could lose its collateral if it fails to actively monitor loans that do not require escrow accounts for real property taxes.

Texas has long had a law which allows a third party – at the specific request of a property owner – to pay real property taxes for the owner. That third party tax lien lender was

able to obtain a certificate of transfer for real property tax liens which primes all existing mortgage liens, regardless of the date filed. Foreclosure of a real property tax lien extinguishes all existing mortgage liens on the property, subject to a two-year redemption period, with penalty. Lenders were protected under this system because tax lien

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lenders had to foreclose the transferred tax liens judicially – just like a tax authority.

A judicial tax lien foreclosure is a lengthy and expensive process which offers the existing lender a high level of protection. In a judicial foreclosure, the tax authority or tax lender has to comply with the basic requirements of Constitutional due process, such as providing legal notice by citation, service of process on the taxpayer and the lender, and an opportunity to be represented by legal counsel at trial. Thus, existing lenders receive formal, legal notice of the lawsuit and have adequate opportunity to respond, work a repayment agreement with the borrower, and avoid the loss of the property to a tax sale.

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The Texas Tax Code has changed the landscape for lenders. Texas now allows tax lien lenders to foreclose either by judicial foreclosure or by nonjudicial foreclosure, through the power of sale provision in the deed of trust. A nonjudicial foreclosure takes as little as 21 days to accomplish, does not involve a judge or other public authority, costs much less to complete and has few due process protections for a lender. Given the time and expense involved in a judicial foreclosure, the nonjudicial foreclosure sale is the sale of choice for tax lien lenders.

A tax lien lender accomplishes a nonjudicial foreclosure sale by posting a notice at the courthouse where the property is located and mailing a notice 21 days prior to the sale to the owner and to the holder of any recorded mortgage lien. While the lender may receive the notice, it will often arrive shortly before the sale, leaving little time to react to protect the lender's lien position. **If the property is sold at a tax lien nonjudicial foreclosure without intervention by the lender, the lender**

**must pay a statutorily mandated redemption penalty in order to recover the property after the sale.**

**Further increasing the risk of losing the collateral is section 32.065(g) of the Texas Tax Code, which appears to allow tax lien lenders for liens established prior to September 1, 2005, to foreclose without any notice to existing lienholders.**

Tax lien loans are close to a "sure thing," because tax lien lenders can charge up to 18% interest; obtain free and clear title in a quick, inexpensive nonjudicial foreclosure, and receive a 25% penalty payment if the

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first lienholder decides to redeem the property after the sale.

Tax lenders may aggressively market borrowers who fall as little as one day behind on their taxes. Many tax authorities make their delinquent account list available to third parties, so the odds are high that delinquent taxpayers will be solicited by tax lenders.

A mortgage lender can take several steps to help protect its position:

1. Aggressively collect and advance taxes. Don't wait too long before deciding to advance delinquent real property taxes. While many lenders do not like to advance delinquent taxes, the best defense against losing real property to a tax sale is the offense of advancing the taxes and recovering them via an escrow account with the borrower.
2. Educate borrowers. Let them know that financing real property taxes, which is frequently a technical violation of the deed of

3. Consider litigation options. The nonjudicial foreclosure process in the context of a tax lien foreclosure may violate due process because it involves state action (the transfer of the tax lien) which can deprive one of property without adequate legal safeguards. In a recent U.S. Supreme Court case styled *Gary Kent Jones v. Linda K. Flowers, et al.*, Case No. 04-1477, the Court held that "notice" by certified mail (which is now permitted by the Texas Tax Code) is a violation of due process if the tax lien foreclosure is conducted by the state. Whether the same law will apply to actions taken by a non-state entity remains an unanswered question.

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# Meet Your Lawyers:

## Jeffrey J. Porter

<b>Hometown:</b> <i>Dallas, Texas</i>	<b>Hobby:</b> <i>Texas History</i>	<b>Sport:</b> <i>College football (to watch) and golf (to play)</i>
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<b>Food:</b> <i>Sue's veal scaloppini</i>	<b>Music:</b> <i>Rock and Roll, Blues and Gospel</i>	
<b>Drink:</b> <i>#1 Red Wine or #2 Any beer in a green bottle</i>	<b>Vacation:</b> <i>On a beach, with Sue and favorite drink #2</i>	



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**Areas of Practice:**

Real Estate — Acquisitions and Divestitures, Development; Commercial Leasing and Management; and Golf and Resort

## Health Records and Electronic Prescribing: Costly to Affordable

By Bradford E. Adatto

Many years ago you may have seen a commercial where a patient in Hong Kong has medical records instantaneously sent from New York so that the physicians in Hong Kong could review them. Electronic medical records were going to be the wave of the future. Fast forward to 2006 and the vast majority of physician offices still do not have “paperless” offices. The cost and the subsequent laws that the

government has passed on protection of patient health information have prevented the facilitation of paper to electronic.

The Centers for Medicare and Medicaid Services (“CMS”) and the Health and Human Services Office of the Inspector General (“OIG”) issued Stark Exceptions and new Anti-kickback Safe Harbor which became effective on October 10, 2006. These new rules allow the dona-

tion of Electronic Health Records (“EHR”) and electronic prescribing (“E-prescribing”) to physicians and other medical providers. Both of these rules focus on accelerating the adoption of EHR and E-prescribing which is consistent with the Executive Office’s goal of transferring medical records into electronic health records technology by 2014.

CMS’ and the OIG’s simultaneous release of these

rules demonstrate the desire of the federal government to develop rules that will substantially increase the use of EHR and E-prescribing. In addition, both the Exception and Safe Harbor requirements overlap, making it easier for a physician or health-care entity to comply with both new rules. Whether a provider meets the Exception and Safe Harbor is determined on a case by case situation.

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Bradford E. Adatto

It is important to note that these rules do not give hospitals and vendors blanket authority to upgrade a provider's office by donating the newest and greatest computers and software. For example, physicians who already possess the equivalent technology are

not qualified to receive new software upgrades under these rules. In fact, only E-prescribing allows vendors to donate limited hardware, in limited circumstances.

Understand that all these new rules come with their headaches and unintended consequences. But before you write off the movement towards EHR as another fad, let us not forget the lessons of Katrina. After the worst disaster in the United States history, physicians and providers who had EHR systems were able to reestablish

their practices much more efficiently and quickly because most had off-site backups. Many providers with the paper records were left behind while they attempted to rebuild their files.

This dramatic change in the government's logic from preventing this type of donation to encouraging these arrangements should cause every physician office and medical provider to re-evaluate their paper charts and discover if they qualify for the new Stark Exception and Safe Harbor. By

adopting EHR and E-prescribing technology, a provider may reduce the overall cost of business while simultaneously improving the quality of care, reducing medical errors and protecting its business from disasters.

If you would like to learn more about how these new rules can help your business, please contact Michael S. Byrd of SettlePou at (214)520-3300 or ([mbyrd@settlepou.com](mailto:mbyrd@settlepou.com)) or Bradford E. Adatto ([badatto@settlepou.com](mailto:badatto@settlepou.com)).

## Meet Your Legal Support Team:

### Debbi White



Debbi White

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Debbi White has been with SettlePou since 1991. She is a member of Northway Christian Church where she chairs the Worship Committee and is active in the Dallas Emmaus Community. At SettlePou, she enjoys working with clients during the process of closing SBA guaranteed loans.

### Real Property Restrictive Covenants: Can They Be Waived in Texas?

By J. Allen Smith and  
C. Russell Woody

Restrictive covenants have not historically been favored in Texas because they place restraints on the free use of land. In 1987, however, the Texas Legislature amended the Property Code, to recognize restrictive covenants in order to uphold the drafter's intent in certain instances. See TEX. PROP. CODE § 202.003 (a) (Vernon 2005). The amendment allows enforcement of covenants that the original owner envisioned and that property owners within the contemplated development relied upon when their property was purchased.

Where Texas law formerly treated restrictions as a burden to the property, the courts have begun to recognize restrictive covenants in certain instances. One of the primary issues in determining whether an enforceable covenant exists is whether a general development plan was adopted by the original owner of the tract and whether the parties that initially purchased the subdivided properties intended for the covenant to benefit all owners. If such a scheme exists, each landowner in the planned

development is presumed to have an interest in enforcing the restrictive covenant because it was created, in part, for that owner's benefit.

However, a valid restriction may become unenforceable with respect to the entire development if there is an acquiescence of the property owners in the restricted area significant enough to amount to an abandonment of the covenant or a waiver of the right to enforce it. In order to prove waiver, the non-conforming party must show that the violations of the restriction at the time are such as to lead the mind of the "average man" to reasonably conclude that the restriction in question has been abandoned and its enforcement waived.

Among the factors the "average man" must consider are the number, nature, and severity of the existing violations, any prior acts of enforcement of the restriction, and whether it is still possible to realize a substantial degree of the benefits intended through the covenant. As one Court of Appeals has noted, in *New Jerusalem Baptist Church, Inc. v. City of Houston*, 598 S.W.2d 666, 669 (Tex.Civ.App. — Houston [14th Dist.] 1980), an "average man" may rea-

sonably conclude that a particular restriction had been abandoned if a single violation were severe, open, notorious, conspicuous, and unchecked for a substantial period of time.

The Texas Supreme Court, in *Sharpstown Civic Ass'n, Inc. v. Pickett*, 679 S.W.2d 956, 958 (Tex. 1984), has held simply that a restrictive covenant has been effectively waived if the proposed use of the property is not substantially different in its effect on the other properties in the development from any prior violation. However, no specific standard was given to guide courts or property owners in determining the degree of acquiescence that constitutes waiver; rather, the court merely explains that the failure to object to trivial violations of the covenant does not waive the right to enforce the restriction upon finding new and greater violations.

It is difficult to predict how Texas courts will rule with respect to waiver of a restriction because they have thus far avoided establishing strict guidelines to be used in determining if existing violations rise to the level of waiver of the right of enforcement. Further, this would depend on the facts

on a case by case basis. For more information on restrictive covenants on real property in Texas, please feel free to contact Allen Smith of SettlePou, at (214) 520-3300 or

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## Recent Insurance Cases of Note

By H. Norman Kinzy



- Texas Homeowners Policy Form B Provides No Coverage for Mold:

“In *Fiess v. State Farm Lloyds*, 49 TSCJ 996 (Tex. Aug. 31, 2006), the Texas Supreme Court answered a certified question from the United States Court of Appeals for the Fifth Circuit pertaining to the existence of coverage under the Texas Homeowners Form B Policy for a loss caused by mold. The Supreme Court held that Texas standard forms policy (revised Jan. 1, 1996), mandated by the Texas Department of Insurance, does not provide coverage for mold.

In so holding, the Court made it clear that it was not ruling on whether or not insurers should pro-

vide mold coverage in Texas as a public policy question, but rather that the language in the particular policy did not provide such coverage. The Court stated that Texas’ long standing rules for construction of insurance policies “require us to construe a policy according to what it says, not what regulators or individual insurers thought it said. Ambiguities in the plain language must be settled in favor of consumers, but they must appear in the policy itself — we cannot create ambiguities from previous policies, an agency’s interpretation, or a ‘mold crisis.’

The policy here provides that it does not cover ‘loss caused by mold.’ While other parts of the policy sometimes make it difficult to decipher, we cannot hold that mold damage is covered when the policy expressly says it is not.”

Although the exclusory language in more recent HO-B policies has been amended and differs somewhat, current policy provisions still provide that “we do not cover loss

caused by or resulting from mold, fungi or other microbes,” and hence it seems likely that current policy language will, subject to any qualifications contained therein, be likewise upheld by our Supreme Court.

- Duty to Defend — Extrinsic Evidence Regarding Absence of Coverage:

In *Guideone Elite Ins. Co. v. Fielder Road Baptist Church*, 197 S.W.3d 305 (Tex. 2006), the Supreme Court dealt with the “complaint-allegation or eight corners rule” which provides that when an insured is sued by a third party, the liability insurer is to determine its duty to defend solely from terms of the policy and the pleadings of the third party claimant. The Supreme Court held that under the circumstances of the present case, no reason existed to create an exception to the eight-corners rule, and that the trial court erred in using extrinsic evidence to negate the insurer’s duty to defend.

In this case, the insurer under a commercial general liability policy which provided coverage for sexual misconduct, sought a declaration that it had no duty to defend or indemnify the Church in an underlying sexual misconduct lawsuit arising out of the actions of a youth minister who ceased working for the Defendant Church before the policy in question took effect.

Since the proffered extrinsic evidence related to both coverage and to the merits of Plaintiff’s allegations, and thus was a “mixed” or “overlapping” type of extrinsic evidence, the Texas Supreme Court rejected the use of such “overlapping evidence” as an exception to the eight-corners rule because it “poses a significant risk of undermining the insured’s ability to defend itself in the underlying litigation.”

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The Supreme Court continues to recognize an exception to the eight-corners rule where the extrinsic evidence which is offered to defeat the duty to defend involves only a “pure coverage” question. That said, the court adhered to its earlier rulings that the duty to defend is broader than the duty to indemnify, and stated that “a plaintiff’s factual allegations that potentially support a covered claim is all that is needed to invoke the insurer’s duty to defend... whereas the facts actually established in the underlying suit control the

duty to indemnify.” Thus, even though a duty to defend exists, the duty to indemnify does not necessarily also exist, but rather depends upon the facts actually developed in the liability case after trial. Despite urging that it adopt a “true-facts exception” to the eight-corners rule to prevent the rule’s alleged recurring use as a tool for fraud, the Supreme Court rejected such an argument stating that “the record before us does not suggest collusion or the existence of a pervasive problem in Texas with fraudulent alle-

gations designed solely to create a duty to defend.”

Moreover, because the insuring provisions of the policy obligated the insurer to defend the insured “even if the allegations of the suit are groundless, false or fraudulent,” the court held that the insurer’s knowledge of untrue facts cannot be allowed to negate its contractual duty to defend against such untruthful allegations.

Of further significance, the Supreme Court agreed with the Court of Appeals’ holding that the term “bodily injury” contained in the insurance policy included allegations of sexual assault, abuse, molestation and violation.

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we extend our very best wishes for a  
Happy Holiday Season*

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