Financial Services Litigation | Alert

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Nevada Supreme Court Departs From Ninth Circuit Ruling And Finds HOA Lien Statute Does Not Implicate Due Process

On Jan. 26, 2017, the Nevada Supreme Court issued a 5-0-2 decision in *Saticoy Bay LLC Series 350 Durango 104 v. Wells Fargo Home Mortgage*, 133 Nev. Adv. Op. 5, holding that Nevada's HOA "super priority" lien statute, NRS § 113.3116, *et seq.*, (1) does not violate the due process requirements of the United States and Nevada constitutions and (2) does not constitute a governmental taking based on the extinguishment of a first priority deed of trust.

In *Saticoy Bay*, Roy and Shirley Senholtz had obtained a loan from Wells Fargo totaling $81,370 to refinance their existing mortgage. The loan was secured by a first priority deed of trust. The Senholtzes subsequently defaulted on both their mortgage and their HOA dues. Thereafter, the HOA conducted a nonjudicial foreclosure sale and sold the property to Saticoy Bay for $6,900. Simultaneously, Wells Fargo filed a notice of default and election to sell. Saticoy Bay brought an action to enjoin that foreclosure sale based on NRS § 113.3116 *et seq.* Wells Fargo successfully obtained an order dismissing the action based on the argument that the statute violated Wells Fargo's due process rights.

On appeal, the Nevada Supreme Court considered both the due process ruling as well as Wells Fargo's secondary argument that the statute violated the Takings Clauses of the United States and Nevada Constitutions.

The Court held that there was no due process violation because the HOA foreclosure did not involve any state actor. HOA foreclosures are conducted by private parties. *Charmicor, Inc. v. Deaner*, 572 F.2d 694, 696 (9th Cir. 1978). The Court rejected the argument that the Nevada Legislature's enactment of NRS § 116.3116 *et seq.* implicated due process "absent some additional showing that the state compelled the HOA to foreclose on its lien, or that the state was involved with the sale." *Id.*, at 7. As a result, the Court declined to address the notice provisions of NRS 113.3116 in effect at the time.

The Court also held the statute did not violate the Takings Clause. First, the Court found that the statute did not impose an unnecessary economic impact on Wells Fargo because it does not compel an HOA to foreclose and, in the event of a foreclosure, requires that excess sale proceeds be disbursed to subordinate lienholders after satisfaction

of the super priority claim. Second, the statute did not interfere with any legitimate investment-backed expectation because NRS § 116.3116 was enacted in 1991 and the HOA's covenants, conditions, and restrictions (CC&Rs) were recorded in 1994, both prior to Wells Fargo's acquisition of a security interest via the deed of trust. Thus, Wells Fargo had record notice of the statute and CC&Rs. Finally, the Court held that its adjudication of the Legislature's statutory alteration of the priority of a certain lien to create the super priority lien did not implicate the Takings Clause given this record notice. However, the Court did note that it was not ruling on whether the statute constituted a taking with regard to security instruments recorded prior to 1991.

The Supreme Court's ruling squarely contradicts the Ninth Circuit's ruling in *Bourne Valley Court Tr. V. Wells Fargo Bank, N.A.*, 832 F.3d 1154, 1159 (9th Cir. Aug. 12, 2016), which held that the statute's pre-2015 "opt-in" notice procedures for HOA foreclosures under NRS Chapter 116 were facially unconstitutional under the Due Process Clause of the Fourteenth Amendment.[1] The Ninth Circuit found that Nevada's enactment of NRS § 116.3116 *et seq*. constituted state action and that the statute violated the due process clause of the United States Constitution because it deprived lenders of property without notice. *Id*. The Court distinguished the case at bar from prior decisions finding no state action in the enactment of state foreclosure statutes because those cases involved disputes between lenders and borrowers, which were governed by contract. By contrast, the parties in *Bourne Valley* (the lender and the HOA) had no contractual relationship. The statute itself altered the relative rights of the parties and caused the lender to lose its lien without the benefit of mandatory notice of an HOA foreclosure. The Nevada Supreme Court did not address this distinction.

Prior to the *Saticoy Bay* ruling, Nevada federal district court judges had begun applying *Bourne Valley to* invalidate HOA foreclosures conducted under the pre-2015 statute. For example, in *Nationstar Mortgage, LLC v. Hometown West II Homeowners Association*, 2017 WL 58567, at *2–3 (D.Nev. 2017), the court granted a motion to reconsider a prior grant of summary judgment entered in favor of the HOA and purchaser of property at HOA sale. The court rejected the HOA's argument that Nationstar might have had actual notice. "Actual notice is inapposite here, because a facially unconstitutional law is void, and the HOA was therefore simply without power to extinguish Plaintiff's interest via the sale under Chapter 116. *See Journigan v. Duffy*, 552 F.3d 283, 289 (9th Cir. 1977). The Court also rejected "any conclusive presumption of notice under state law," finding that such a presumption "would itself be facially infirm under the Due Process Clause." "Reasonable notice under the Due Process Clause is a factual inquiry 'under all the circumstances' that cannot be obviated by legal presumptions under state (or federal) law." *See also Las Vegas Development Group, LLC, v. Steven*, 2:15-cv-01128-RCJ-CWH (dismissing quiet title claim as a matter of law, finding that the "*Bourne Valley* ruling is enough to settle the quiet title and declaratory judgment claims in favor of Wells Fargo as a matter of law as to the HOA's foreclosure. The HOA's foreclosure did not extinguish Wells Fargo's DOT against the Property.").

The Nevada Supreme Court is not bound by the Ninth Circuit and therefore its ruling will stand unless reversed by the United States Supreme Court. At the same time, federal district courts are bound by the Ninth Circuit and will continue to apply *Bourne Valley*. This conflict will likely lead to forum shopping with respect to cases involving HOA foreclosures conducted while the pre-2015 law was in effect.

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[1] On Nov. 4, 2016, the Court of Appeals denied a petition for *en banc* rehearing and the Court issued its mandate on Dec. 14, 2016. *See Bourne Valley Court Trust v. Wells Fargo Bank, NA*, No. 15-15.233 (9th Cir. Dec. 14, 2016).

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