

## [Banking and Finance Law Daily Wrap Up, TOP STORY—9th Cir.: Eliminating mortgage lien without notice violated creditor's due process rights, \(Aug. 16, 2016\)](#)

Banking and Finance Law Daily Wrap Up

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By [Richard A. Roth, J.D.](#)

A Nevada state law that allowed a homeowners association to extinguish Wells Fargo's first mortgage lien by foreclosing on the HOA's lien for unpaid condominium assessments was unconstitutional because the law did not require the HOA to give prior notice, the U.S. Court of Appeals for the Ninth Circuit has decided. The state legislature's enactment of the statute denied Wells Fargo due process of law in violation of the Fourteenth Amendment (*Bourne Valley Court Trust v. Wells Fargo Bank, N.A.*, Aug. 12, 2016, Nelson, D.).

Nevada state law gives HOA liens a "super priority," making them superior to other liens. This superiority includes making nine months of HOA assessments superior to first mortgage liens. The Nevada Supreme Court has decided that an HOA's foreclosure of its super priority lien extinguishes all junior liens, including a first mortgage (*SFR Investments Pool 1 v. U.S. Bank*, 334 P.3d 408 (Nev. 2014)).

**No notice required.** However, prior to a recent amendment, the state law included a scheme the U.S. appellate court termed both "strange" and "peculiar"—a mortgage creditor like Wells Fargo was entitled to notice of the planned foreclosure only if it had previously asked the HOA to notify it. Without this request by the creditor, the HOA could foreclose on its super priority lien and extinguish the mortgage lien without the creditor's knowledge. This "opt-in" scheme violated due process, the appellate court determined.

**Impermissible burden shifting.** The state law violated the Fourteenth Amendment when it shifted the notice burden to Wells Fargo, the court said. Only the HOA knew that a homeowner had not paid his assessments. Wells Fargo had no relationship with the HOA—in fact, the two might not have known of each other's existence—so how Wells Fargo should have known to ask to be notified "is anybody's guess," the court pointed out.

The Fourteenth Amendment requires a state to give reasonable notice before taking an action that could affect a person's interest in life, liberty, or property. An opt-in scheme does not satisfy the reasonable notice requirement, according to the court.

The appellate court also rejected the HOA's attempt to borrow a notice requirement from a different section of Nevada law. Borrowing the notice requirement would have made the opt-in provisions meaningless, the court said, and all provisions of a law should be interpreted to give them meaning when possible.

**State action.** The Fourteenth Amendment only applies when there has been action by the government, the court continued. This requires a deprivation of rights due to a person's exercise of a right or privilege given by the state, or of a rule of conduct established by the state. It also requires that the person said to have caused the deprivation be a state actor.

The foreclosure could not be characterized as a state action, the court conceded. However, that was irrelevant. The state action was the legislature's enactment of the opt-in scheme and imposition of that scheme on two persons, the HOA and Wells Fargo, who had no preexisting relationship.

The enactment of the state law "unconstitutionally degraded" Wells Fargo's security interest in the condo, the court said. Had the law not been in place, the bank's lien would have been fully secured while, with the law in place, its lien could be extinguished.

The absence of a prior relationship between the HOA and Wells Fargo meant the HOA was not permissibly exercising a contractual right, the court also explained. Rather, the HOA was exercising a right granted to it by state law.

**Dissenting opinion.** A dissenter rejected the entirety of the majority opinion. According to the dissenter:

- The state law could not have "degraded" Wells Fargo's security interest when the law was enacted 15 years before Wells Fargo acquired the loan.
- There was no state action because no government actor was involved in the foreclosure process.
- The notice requirement should be borrowed, and this would require an HOA to give a mortgage creditor prior notice of foreclosures and cure the opt-in defect.

**Amendment.** An amendment enacted by the Nevada legislature now requires that mortgage creditors be notified before foreclosures.

The case is [No. 15-15233](#).

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