No. 16-1208

IN THE

Supreme Court of the United States

BOURNE VALLEY COURT TRUST,

Petitioner,

v.

WELLS FARGO BANK, N.A.,

Respondent.

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

REPLY BRIEF FOR THE PETITIONER

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REPLY BRIEF FOR THE PETITIONER

Both parties to this litigation, as well as amici representing the banking industry and other parties in the thousand or more related pending cases, agree that the petition should be granted. They all recognize that the current conflict between the Ninth Circuit and the Nevada Supreme Court over the constitutionality of an important Nevada statute is untenable. They agree that only this Court can resolve the conflict. And they agree that the principles of law over which the courts are divided have broader implications for the constitutionality of similar statutes in other states. *See* Resp. Br. 11-12. The conflict thus casts a cloud on the title of vast numbers of properties sold pursuant to those laws, while also diminishing the ability of homeowners' associations ("HOAs") to fulfill their important obligations. *See* CAI Amicus Br. 4-16.

That is reason enough to grant certiorari, but there are other reasons as well. The conflict is even deeper than Wells Fargo recognizes, in part because the decision below is broader than respondent admits. Moreover, Wells Fargo's defense of the decision on the merits only confirms how far the Ninth Circuit has strayed not only from the law in its sister circuits but also from this Court's state action decisions. The petition should be granted.

I. The Conflict Between The Ninth Circuit And The Nevada Supreme Court Warrants Review.

As respondent and amici have confirmed, the conflict between the decision in this case and the Nevada Supreme Court's decision in *Saticoy Bay* has

created intolerable chaos and disparity in the administration of hundreds of pending cases in state and federal court. Resp. Br. 9-11; Mortgage Bankers Amicus Br. 4 & n.2; LVDG Amicus Br. 5-9. The breadth of that effect can be confirmed through a simple Westlaw search: the nine-month old decision in this case has already been cited more than 100 times, mostly by state and federal trial courts in Nevada. And more suits are being filed every day.

Respondent and amici are also correct that the recent amendment of the state statute's notice provisions provides no basis to deny review. Resp. Br. 10-11; LVDG Amicus Br. § II. Those changes do nothing to resolve the pending litigation or remove the cloud cast over the title of many other properties sold under the prior version.

In addition, respondents do not dispute that the decision below puts in very substantial doubt the constitutionality of the revised statute, which requires notice but affords no opportunity for a pre-deprivation hearing. *See* Pet. 24; Resp. Br. 10-11. A leading treatise has opined that if the Constitution "requires a hearing before chattel security can be seized even temporarily, surely the Due Process Clause prohibits the permanent taking of real estate with no opportunity for a hearing." GRANT S. NELSON ET AL., REAL ESTATE FINANCE LAW § 7:26 (6th ed. 2014) (hereinafter "REAL ESTATE FINANCE LAW"). A number of courts have agreed. *See, e.g., Turner v. Blackburn*, 389 F. Supp. 1250, 1254-60 (W.D.N.C. 1975) (three-judge court holding nonjudicial foreclosure statute in North Carolina unconstitutional for lack of pre-foreclosure hearing, where foreclosures deemed state action because of

substantial involvement of sheriff and clerk of the county court); REAL ESTATE FINANCE LAW § 7:26 & n.772 (collecting similar decisions).

Indeed, banks have already been arguing that the prior version of the Nevada statute was facially unconstitutional *both* because it "did not ensure notice" *and* because it did not provide "an opportunity to be heard prior to the elimination of property rights."[1] The latter objection inevitably will be made against the revised version as well, as it has been in numerous other states. *See* Pet. 24.

II. The Conflict Is Broader Than Wells Fargo Recognizes.

1. Wells Fargo does not dispute that at least six federal circuits and eight state supreme courts have rejected the argument that nonjudicial foreclosures constitute a form of state action, even though authorized by statute. Pet. 14-16. Respondent nonetheless denies that the Ninth Circuit's decision conflicts with these precedents. It says that the decision below addresses a narrow question, not

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[1] Defendant Bank of America, N.A.'s Motion for Summary Judgment Against Plaintiff § V.B, *Evening Sky, LLC v. Bank of America, N.A.*, No. 14A702578, 2016 WL 8259497 (D. Nev. Aug. 31, 2016); *see also, e.g.*, Opposition to Motion for Summary Judgment § I.E, *Las Vegas Rental & Repair LLC v. Doyle* § I.E, No. 15A720926, 2016 WL 8846746 (D. Nev. Dec. 5, 2016) ("Additionally, a line of cases holding lien statutes unconstitutional for lack of notice and a chance to be heard makes very clear that NRS 116.3116 is unconstitutional" given that statute "does not require notice *or a hearing* before extinguishment, as Due Process requires" (emphasis added)).

confronted elsewhere, regarding "whether a nonjudicial foreclosure implicates the Due Process Clause when it allows junior lienholders to jump the line and extinguish interests that are senior as a matter of private ordering." Br. 9 n.4. That is incorrect.

The critical fact for the Ninth Circuit was that "the homeowners' associations' ability to extinguish Wells Fargo's interest in the Property arose directly and exclusively from the Statute," rather than from an agreement between those two entities. Pet. App. 14a-15a. That conclusion did not turn on whether the statute conformed to, or modified, any "private ordering." *Compare id.* (distinguishing *Flagg Brothers, Inc. v. Brooks*, 436 U.S. 149 (1978), solely on the ground of lack of contractual privity) *with* Resp. Br. 16-17 (alleging, in addition, a "private ordering" distinction). To be sure, the court of appeals stated that absent the statute, the sale would not have affected Wells Fargo's lien under the pre-existing legal rules. Pet. App. 14a. But that simply showed that but for the statute, Wells Fargo would not have suffered any harm to its property, making the statute (rather than the private sale) the cause of its injury.

Respondent does not deny that if petitioner's reading of the opinion is correct, the Ninth Circuit's decision stands in conflict with an overwhelming body of contrary precedent, under which it makes no difference whether a foreclosure was authorized by statute or instead by contract. *See* Pet. 14-18.

2. In any event, even if the Ninth Circuit's decision were limited to nonjudicial foreclosures enforcing HOA super-priority liens, Wells Fargo

acknowledges that "[t]wenty-one States and the District of Columbia have adopted some form of super-priority lien statute for home owners' associations." Br. 11. By petitioner's count, at least six of these states permit nonjudicial foreclosure of HOA super-priority liens without requiring direct notice to all junior lienholders. *See* Ariz. Rev. Stat. §§ 33-1807(B), 33-807, 33-809; D.C. Code § 42-1903.13(c)(4)-(5); Mich. Comp. Laws §§ 559.208(1)-(9), 600.3208; Mo. Rev. Stat. §§ 443.320, 443.325; R.I. Gen. Laws §§ 34-36.1-3.16(b)(2), 34-27-4; Tex. Prop. Code Ann. §§ 51.002-51, 82.113(b).

As the petition explained, with the exception of Arizona, each of these jurisdictions already has in place state and/or federal precedent holding that nonjudicial foreclosure is not a form of state action, even when authorized by statute. *See* Pet. 14-15. Accordingly, even on Wells Fargo's narrow view of the precedent below, a broader conflict would be avoided only if the state and federal courts in *all five* of these jurisdictions were to adopt an exception to their existing precedent for foreclosures on super-priority liens. Given the weakness of respondent's argument on the merits (discussed next), there is no prospect of that happening.

Meanwhile, the mere existence of the Ninth Circuit's contrary precedent creates intolerable uncertainty about the lawfulness of nonjudicial sales enforcing a super-priority lien in any of the more than twenty state that permit it, given that five such states do not provide the notice the Ninth Circuit held was required and none provides for a pre-deprivation hearing.

II. Wells Fargo's Defense Of The Ninth Circuit's Decision Only Confirms The Need For Review.

It is perhaps understandable that Wells Fargo would seek to recharacterize the decision it must defend, as that decision flies in the face of this Court's established precedents. *See* Pet. § III. Respondent's arguments to the contrary only illustrate the need for review.

1. As the petition explained, there is no factual basis for the Ninth Circuit's claim that *Flagg Brothers* is distinguishable because the sale in that case was authorized by contract. Pet. 26-27. Wells Fargo seemingly admits that petitioner is correct that at least one of the plaintiffs in *Flagg Brothers* had no such contract. Resp. Br. 15; *see also* Pet. 26-27.[2] It nonetheless claims that the statute authorizing the sale "merely enforced the warehouse's undoubted *contractual* right to be compensated for storing the respondent's belongings." Resp. Br. 15 (emphasis added). But it never explains how the warehouse could have a contractual right without having a contract. In fact, as we have explained, this Court proceeded on the understanding that the power to conduct the sale arose solely from a state statute, but concluded that this fact did not render the sale state action. Pet. 26-27. To the extent Wells Fargo thinks that both the majority and the dissent misunderstood

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[2] Because the case was resolved on a motion to dismiss, the plaintiff's "alleg[ation] that she never authorized the storage of her goods," Resp. Br. 15 (quoting *Flagg Bros.*, 436 U.S. at 160), was "accept[ed] as true," *id.* at 153.

the facts of the case, that suggestion is unwarranted. *See id.*; *see also Flagg Brothers*, 436 U.S. at 169 n.2 (Stevens, J., dissenting) (noting that even the defendants "conceded in this Court that . . . there is no contractual issue in this case").

2. Wells Fargo also argues that *Flagg Brothers* did not involve a statute that altered what the bank calls the "private ordering" of liens. Br. 14, 16-17. Its theory seems to be that statutory authorization will render a foreclosure state action if, but only if, the statute fails to respects this "private ordering." *Id.* There are many problems with this theory.

To start, it is nonsense to talk about "private ordering" of liens. The entire premise of the decision below was that affected lienholders "had no preexisting relationship, contractual or otherwise" and may not even have been aware "of each other's existence." Pet. App. 14a-15a. Prioritization of liens is created by substantive state law precisely because it is impractical for such lienholding strangers to negotiate an order of priority among themselves.

Wells Fargo points to what it says is the "cardinal rule" that "the first in time is first in right." Resp. Br. 2 (quoting *United States v. City of New Britain*, 347 U.S. 81, 85-86 (1954)). But this is a *legal* rule, founded in common law and statute, not a principle lienholders actually agree to in the course of some "private ordering." *See, e.g.*, *United States v. City of New Britain, Conn.*, 347 U.S. at 82-84. It is also a gross simplification of the true complexity of the law of lien priority under which, for example,

later filed tax liens may well take priority over earlier filed mortgage liens. *See id.* at 85; REAL ESTATE FINANCE LAW § 9:9.[3]

Perhaps Wells Fargo means to argue that enactment of a statute will transform private action into state action if the statute fails to conform to some "cardinal rule" established, if not by contract, then at least by tradition, natural law, or some idea of fundamental fairness. But that simply shows the argument for what it really is – a substantive complaint about the policy judgment Nevada has made in establishing the order of priority among competing claims. *See also* Mortgage Bankers Amicus Br. §§ I.B-C, II (arguing exclusively that HOA super-priority liens are unfair and bad policy). That argument sounds in substantive, not procedural, due process.[4]

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[3] Petitioner does not agree, for example, that an HOA's lien would be treated as junior to a bank's deed of trust in the absence of the Nevada HOA lien statute.

[4] Wells Fargo betrays its true objection when it asserts that "super-priority lien schemes . . . conflict with important federal programs." Br. 12. A procedural due process ruling would do nothing to prohibit super-priority liens schemes; it would only alter the procedures for enforcing them. But in any event, there is no conflict. The Federal Housing Finance Agency (FHFA) has merely taken the position that during the period of Fannie Mae and Freddie Mac's conservancy, a special federal statute prevents enforcement of *any* liens (including super-priority liens) that would extinguish liens held by Fannie or Freddie without FHFA's consent. The Department of Housing and Urban Development rule respondent cites actually *refused* to implement a proposal that would have precluded certain assignments of mortgages subject to an HOA lien. *See* Resp. Br.

3. Respondent's focus on the statute's substantive alteration of lien priorities also highlights other departures from the Court's settled state action precedents.

In asking whether an otherwise private action "is fairly attributable to the State," the Court "begins by identifying 'the specific conduct of which the plaintiff complains.'" *American Mfrs. Mut. Ins. Co. v. Sullivan*, 526 U.S. 40, 51 (1999) (citation omitted). Here, Wells Fargo is not complaining about anything an *HOA* has done – the sale alone would not harm its interests so long as its lien carried over to the new owner. *See* Resp. Br. 14. Respondent's injury arises from the extinguishment of its lien, which, Wells Fargo emphasizes, is caused by "the statute itself," not by the HOA's foreclosure. *Id.* (explaining that absent the statutory extinguishment of the bank's mortgage as a junior lien, Wells Fargo's "deed of trust would have remained intact"). Accordingly, the "specific conduct" giving rise to the bank's injury is the passage or application of the statute decreeing that result, not the HOA's sale of the property.[5]

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13. The real impairment of federal interests arises from the Ninth Circuit's dramatic expansion of the state action doctrine, which provides new grounds for claiming that Fannie and Freddie are engaged in state action when they rely on nonjudicial foreclosure to enforce their mortgages. *See generally* William E. Eye, *Are Fannie Mae and Freddie Mac State Actors? State Action, Due Process, and Nonjudicial Foreclosure*, 65 EMORY L.J. 107 (2015).

[5] Wells Fargo does not claim that it was denied procedural due process during the legislative process leading to the statute's enactment. *See Texaco, Inc. v. Short*, 454 U.S. 516,

To be sure, state law extinguished respondent's lien only because the HOA foreclosed on the property. But that is simply to say that the deprivation of Wells Fargo's property interest was "caused by the exercise of some right of privilege created by the State," the first of *two* necessary conditions for finding state action. *Sullivan*, 526 U.S. at 50; Resp. Br. 14. Wells Fargo's theory collapses the two distinct parts of the state action test, insisting that the HOA's action is "fairly attributable to the state" simply because the HOA exercised a statutory right that caused the injury.

The principles respondent advances (and insists the Ninth Circuit has now enshrined in its precedents) thus "would intolerably broaden, beyond the scope of any of [this Court's] previous cases, the notion of state action under the Fourteenth Amendment to hold that the mere existence of a body of property law in a State . . . itself amounted to 'state action' even though no process or state officials were ever involved in enforcing that body of law." *Flagg Bros.*, 436 U.S. at 160 n.10. On respondent's view, private action is transformed into state action

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531-32, 536 (1982). And because extinguishment of the lien is a self-executing feature of state law, application of the law does not give rise to any Due Process right to notice. *See id.* at 533-37. Nor is petitioner's filing of a quiet title action the cause of respondent's injury. *Contra* Resp. Br. 17. The litigation (which afforded Wells Fargo ample notice and an opportunity to be heard) seeks only to *confirm* the elimination of Wells Fargo's lien, which occurred by operation of law at the time of the sale. The suit accordingly adds nothing to the state action analysis. *See Texaco*, 454 U.S. at 534.

whenever a private person takes an action that, through operation of state law (as opposed to private agreement), negatively affects another's property interests. But private conduct has such effects all the time.

For example, Wells Fargo never says what it thinks the result in *Flagg Brothers* should have been if petitioner is right that the sale of the evicted tenant's possessions was authorized only by statute, not by contract. But the logic of respondent's position must be that the sale would be a form of state action, rendering unconstitutional the long-established self-help procedure the warehouse employed. If that is the law, this Court should say so. If it is not, it should correct the Ninth Circuit's misapprehension.[6]

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[6] Respondent is correct that petitioner principally seeks review of the Ninth Circuit's state action decision. Resp. Br. 10. But by its plain terms, the Question Presented also encompasses whether the Nevada statute satisfies the Due Process clause if it applies. *See* Pet i. And the body of the petition expressly embraced Judge Wallace's position that the statute, properly read, satisfies Due Process by requiring direct notice to recorded lienholders in addition to the "opt-in" notice the panel found insufficient. *See id.* 30 n.23. The question presented also encompasses whether *facial* invalidation is the proper remedy for the statute's failure to require adequate notice, thereby invalidating even sales in which actual notice was provided. *See* Pet. i; Pet. App. 8a.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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