Case No. 63614

In the Supreme Court of Nevada

SFR INVESTMENTS POOL 1, LLC, a Nevada limited liability company,

Appellant,

vs.

U.S. BANK, N.A., a national banking association as Trustee for the Certificate Holders of Wells Fargo Asset Securities Corporation, Mortgage Pass-Through Certificates, Series 2006-AR4,

Respondent.

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APPEAL

from the Eighth Judicial District Court, Clark County
The Honorable DAVID BARKER, District Judge
District Court Case No. A-13-678814-C

APPELLANT'S REPLY BRIEF

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I.
INTRODUCTION

THIS IS NOT A TYPICAL 116.3116(2) APPEAL BECAUSE OF BANK'S ADMISSIONS ABOUT DUE PROCESS, EXTINGUISHMENT, AND SFR's DAMAGES.

- **Admission 1**: No state actor is involved in this case.[1]
- **Admission 2**: If 116 requires notice to holders of first security interests, then 116 is constitutional.[2]
- **Admission 3**: If notice is mandated, then Copper Ridge's ("Association") foreclosure extinguished Bank's deed of trust.[3]

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[1](RAB_21-22)("The claim [in *Charmicor, Inc. v. Deaner*, 572 F.2d 694 (9th Cir. 1978)] was **against the actors** who allegedly violated the constitutional rights. ….Here, the claim is not against the HOA or the trustee which conducted its sale; U.S. Bank does not contend their actions were 'state actions' which support a claim against them.")(emphasis in original); (RAB_22-23)("Here, again, the state action giving rise to a due process violation is the creation of an unconstitutional procedural scheme, and not the individual non-judicial foreclosures that arise from it. In other words, it is the procedural scheme that is challenged not the acts of the HOA and its foreclosure trustee."). SFR's opening brief contended "due process is not implicated because the Association's foreclosure did not involve state actors." (AOB_26.) Rather than challenge this assertion, Bank suggests state actors are unnecessary. (RAB_21-23.)

[2] (RAB_13-14)("If the right to receive notice from the statute is removed, and the first priority secured interest can be extinguished by the HOA lien foreclosure sale, then the holder of that interest suffers a violation of its right to due process."); (RAB_19)("In short, if the right to receive notice from the statute is removed, and the first priority secured can be extinguished by the HOA lien foreclosure sale, then the holder of that interest suffers a violation of its right to due process.").

- **Admission 4**: SFR is "entitled to compensatory damages for any loss of that interest in the Property."[4]

Here, Bank's first admission negates its due process arguments because any alleged deprivations must be caused by a state actor; Bank's acknowledgement that no state actor is present eliminates due process concerns. *Lugar*, the very case Bank misleadingly uses, bolsters this assertion. *Lugar v. Edmondson Oil Co., Inc.*, 457 U.S. 922, 937, 939 n.21, 941 (1982). Similarly, Bank's second admission is self-defeating because 116 does, in fact, require notice to first security interest holders. 116.31163(2); 116.311635(1)(b)(1)-(2); 116.31168(1). As such, and pursuant to Bank's own position, 116 is constitutional. And, because 116 necessitates notice, Association's foreclosure extinguished Bank's deed of trust─just as Bank's third concession provides. Lastly, Bank's fourth admission (i.e. SFR is entitled to damages) reveals dismissal's impropriety. At a minimum, dismissal should have been without prejudice so SFR could have filed an amended

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[3] (RAB_13)("When the Legislature adopted [116] in 1991, it … required that the foreclosure of HOA liens follow all the requirements of NRS 107.090. ….**Under those circumstances, it made some sense that the foreclosure sale could extinguish all liens because all lienholders got notice**.")(emphasis added); (RAB_16)("If the Nevada Legislature had intended for the foreclosure of an HOA lien to extinguish a first deed of trust, it would have required the HOA to notify the holder of the deed of trust *in every instance*.")(emphasis in original); (RAB_18)("Under those circumstances, it made some sense that the foreclosure sale could extinguish all liens because all lienholders got notice.").

[4] (RAB_40); *see also* (RAB_37)("SFR can easily be compensated with a monetary amount for any loss of 'title.'").

complaint to pursue damages Bank believes SFR is "entitled to." This Court should reverse and instruct the district court to: (i) vacate the order dismissing SFR's complaint and expunging SFR's lis pendens and (ii) enjoin Bank's foreclosure.

II.
<u>ARGUMENT</u>

A. <u>Due Process is Immaterial because Bank Concedes there is No State Actor</u>

1. ***<u>Bank Admits there is No State Actor</u>***

In order for due process to be implicated, there must be a state actor. *Brentwood Acad. v. Tenn. Secondary Sch. Athletic Ass'n*, 531 U.S. 288, 295 (2001). If a state actor is not involved, then due process─including concerns about "notice"─is inapplicable. *Id.*; *see also Jackson v. Metro. Edison Co.*, 419 U.S. 345, 349, 358-59 (1974). Here, Bank admits there is no state actor,[5] "Bank does not contend their [Association and its trustee] actions were 'state actions' which support a claim[.]" (RAB_21-22.)[6] Thus, all of Bank's arguments about due process, "notice," and why 116.3116 is supposedly "unconstitutional" are

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[5] (RAB_21-23.)

[6] Bank made this statement to distinguish the instant appeal from *Charmicor, Inc. v. Deaner*, 572 F.2d 694 (9th Cir. 1978), a case the opening brief discussed. *Compare* (AOB_27)(SFR's analysis of *Charmicor*), *with* (RAB_21-22)("The claim [in *Charmicor*] was **against the actors** who allegedly violated the constitutional rights . . . .Here, the claim is not against the HOA or the trustee which conducted its sale; U.S. Bank does not contend their actions were 'state actions' which support a claim against them.")(emphasis in original).

meritless.

2. **<u>Lugar</u>** ***<u>does not Eliminate the State Actor Requirement</u>***

Bank tries to sidestep the state actor requirement through a distorted reading of *Lugar*. According to Bank, *Lugar* held a state's creation of a procedural scheme "that violates due process constitutes state action." (RAB_22.) Then, Bank opines it can invoke due process regardless of whether a state actor is involved, as long as a state-created "procedural scheme" abridges due process. (RAB_21-23.) This is wrong for three reasons. First, Bank supports its proposition by citing page 2746 in *Lugar*. (RAB_22.) Yet, that page is part of the "Syllabus," which "constitutes no part of the opinion[.]" *Lugar*, 457 U.S. at 922 (citing *U.S. v. Detroit Lumber Co.*, 200 U.S. 321, 337 (1906)).[7]

Second, Bank is wrong to suggest *Lugar* allows Bank to avoid the state actor requirement; Bank cannot challenge 116.3116's constitutionality by merely claiming the statute is a state-created procedural scheme that purportedly defies due process. *Lugar* is quite clear about this:

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[7] Even if page 2746 was part of the *Lugar* opinion, Bank's description of 2746 is incorrect because that page still required a state actor, "the statutory scheme obviously is the product of state action, and a private party's joint participation with state officials in the seizure of disputed property is sufficient to characterize that party as a 'state actor' for purposes of the Fourteenth Amendment." *Lugar*, 457 U.S. at 922 (Holding number three on page 2746 of the Supreme Court Reporter (S.Ct.) version).

> While private misuse of a statute does not describe conduct that can be attributed to the State, the procedural scheme created by the statute obviously is the product of state action. This is subject to constitutional restraints and properly may be addressed in a § 1983 action, **if the second element of the state-action requirement is met as well**."

Lugar, 457 U.S. at 941 (emphasis added). In *Lugar*, the "second element of the state-action requirement" is "**the party charged with the deprivation must be a person who may fairly be said to be a state actor**." *Id.* at 937 (emphasis added). As mentioned above, Bank cannot satisfy this element because it acknowledged this case does not involve a state actor. (RAB_21-23.)

Third, *Lugar*'s footnote twenty-one noted "the holding today, as the above analysis makes clear, **is limited to the particular context of prejudgment attachment**." *Lugar*, 457 U.S. at 939 n.21 (emphasis added). Hence, even if Bank's description of *Lugar* was accurate, which it is not, *Lugar* was expressly limited to the prejudgment attachment context. *Id.* This quiet title/declaratory relief case, however, is not about "prejudgment attachment," making *Lugar* inapposite. (RAB_1.)

B. Under Bank's Logic 116's Notice Provisions Establish Extinguishment

Again, the absence of a state actor prevents inquiring into 116.3116's constitutionality, including the issue of notice. *Brentwood*, 531 U.S. at 295. Besides, Bank never denied the allegations in the complaint that the Association sent it foreclosure notices. Nevertheless, it is worth reviewing 116's notice provisions because Bank's answering brief included telling remarks about notice. (RAB_13-24. [8]) Bank proposed that if the Legislature intended for association foreclosures to extinguish deeds of trust, then it would have required notice to deed of trust holders. (RAB_16.) It conceded that, if 116 compels such notice, then 116—including extinguishment—is constitutional. (*See* n. 2 supra; RAB_13-14, 16.)

Here, several sections in 116 demand notice to deed of trust holders. Pursuant to 116.31163(2) and 116.311635(1)(b)(2), "the association or other person conducting the sale shall send" a notice of default and a notice of sale to any holder of a recorded security interest who notified the association "of the existence of the security interest." These provisions appear below, in pertinent part:

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[8] SFR did not have a duty to give Bank notice because Chapter 116 places that duty on associations and "person[s] conducting the sale." *See*, *e.g.*, 116.31162(1)(a); 116.31163; 116.311635(1); 116.31164(1). No such obligation binds purchasers. Thus, SFR did not have a duty to give Bank "notice" because SFR is not an association or "person conducting the sale." In fact, SFR, as the purchaser, could rely on the recitals in the Association's trustee's deed as conclusive proof that Bank was given the required notices, as discussed more fully in the text. NRS 116.31166 (1)-(2). (*See* 2JA_156.)

> **NRS 116.31163 Foreclosure of liens: Mailing of notice of default and election to sell to certain interested persons.**
> The association or other person conducting the sale shall also mail, within 10 days after the notice of default and election to sell is recorded, a copy of the notice by first-class mail to:
> 2. Any holder of a recorded security interest encumbering the unit's owner's interest who **has notified the association**, 30 days before the recordation of the notice of default, of the existence of the security interest; and
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> …
>
> **NRS 116.311635 Foreclosure of liens: Providing notice of time and place of sale; service of notice of sale; contents of notice of sale; proof of service.**
> 1. The association or other person conducting the sale shall also, after the expiration of the 90 days and before selling the unit:
> (b) Mail, on or before the date of first publication or posting, a copy of the notice by certified or registered mail, return receipt requested, to:
> (1) Each person entitled to receive a copy of the notice of default and election to sell notice under NRS 116.31163;
> (2) The holder of a recorded security interest or the purchaser of the unit, if either of them **has notified the association**, before the mailing of the notice of sale, of the existence of the security interest, lease or contract of sale, as applicable; and . . .

Because "**has notified**" is not defined by the statute, its plain meaning applies. Black's defines "notify" as "to provide notice." BLACK'S LAW DICTIONARY 1090 (8th ed. 1999). "Notice" is the "[l]egal notification required by law or agreement, or imparted by operation of law as a result of some fact (such as the recording of an instrument); definite legal cognizance, actual or constructive, of an existing right or title[.]" *Id.* at 1087. The act of recording, therefore, satisfies the requirement to notify the association, which obligates the association to provide notice of default and sale to “holder[s] of a recorded security interest[.]” 116.31163(2); 116.311635(1)(b)(2).[9] Here, Bank recorded its deed of trust—and commensurate with 111.320—it notified Association “of the existence of” its deed of trust, which presumably explains why Bank received notice of Association’s foreclosure. (1JA_099.)

Most importantly, 116.31168(1) makes “107.090 apply to the foreclosure of an association’s lien as if a deed of trust were being foreclosed.” 107.090(3)(b) necessitates notices of default to be sent to subordinate interest holders. Therefore, the Association had a duty to check the county recorder’s records and determine what interests were subordinate to its lien.

Here, Bank’s deed of trust was a “subordinate interest” to Association’s lien.[10] As a result, and under Bank’s own logic, 116’s notice provisions indicate: (i) Nevada’s legislature intended extinguishment (RAB_16); (ii) Association’s foreclosure extinguished Bank’s deed of trust (RAB_13, 16, 18); and (iii) 116 is constitutional. (RAB_13-14, 16.)

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[9] The language “has notified” is broad enough to allow for those persons who are holders of recorded interests, such as assignees, who for their own reasons have not yet recorded their interests to notify the association directly so as to receive the foreclosure notices.

[10] As set forth in the opening brief, the notices themselves provided the necessary information for Bank to protect itself and time to be heard. (AOB_26-35.)

C. 116.3116's Text Befuddles Bank

Aside from mishandling 116.3116's constitutionality, Bank also botches that law's text. For instance, it observes 116.3116(2) does not address extinguishment. (RAB_3.) Yet, and as the opening brief detailed,[11] this textual gap is supplemented by a property law principle concerning priority: foreclosure of a prior lien extinguishes junior liens; supplementation is authorized by 116.1108.[12] Next, Bank insists 116.3116(2) gives associations a "payment priority," another point disproved by the opening brief. (AOB_35-37.) But 116.3116(2)'s text does not support a "payment priority" because it requires this Court to use two definitions for "the lien" and "action" and ignore the plain meaning of "prior." (AOB_36-37.)

Additionally, Bank effectively agrees with SFR that 116.310312 (abatement lien) elucidates 116.3116(2)'s meaning. *Compare* (RAB_32), *with* (AOB_24-26.) To its credit, Bank concedes 116.310312 "**eliminates the priority of first deeds of trust** over abatement liens, present with assessment liens . . ." RAB_32.)(emphasis added.) But it then inexplicably alludes to so-called "legislative history" that shows 116.310312 (foreclosure of abatement liens) does not extinguish deeds of trust; no citation or supporting authority accompanies the avowed "legislative history." (RAB_32.) Regardless, this statement about non-extinguishment contradicts

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[11] (AOB_ 16-19.)

[12] 116.1108 provides "The principles of . . .the law of real property . . .supplement . . . this chapter, except to the extent inconsistent with this chapter."

Bank's concession that 116.310312 "eliminates" its deed of trust.[13] Bank's failure to reach this conclusion is caused by its manufactured "legislative history," which really does not exist.

D. Bank's Interpretation of "Action" Contravenes *Noscitur a Sociis*

A further illustration of Bank's misinterpretation of 116's text is its position that "action" in 116.3116(2) cannot include "non-judicial foreclosure." (RAB_24-30.) This interpretation is incorrect because Bank's construction disregards the interpretive precept *noscitur a sociis*. Before discussing this error, it is necessary to review "action's" context within 116.3116(2).

1. Textual Context of "Action" in 116.3116(2)

Statutory construction is contextual, requiring courts to actualize and respect a term's surrounding textual context. *Blackburn v. State*, 129 Nev. ___, ___, 294 P.3d 422, 426 (2013)(single phrase should not be detached from provision's remaining text). If a word is construed in isolation of its context, then such a construction is inaccurate. *Id.* Here, "action" has a particularized context in 116.3116(2). Pursuant to 116.3116(2),

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[13] Moreover, Bank's concession that 116.310312 "eliminates" its deed of trust applies with equal force to 116.3116(2) because 116.310312 is part of "the lien" addressed in 116.3116(2). (AOB_24.) The language after □in 116.3116(2) incorporates by reference 116.310312 ("The lien is also prior to all security interests described in paragraph (b) to the extent of any charges incurred by the association . . . pursuant to NRS 116.310312 . . . .").

> The lien is also prior to all security interests described in paragraph (b) to the extent of … the assessments for common expenses … which would have become due … during the 9 months immediately preceding **institution of an action to enforce the lien**, unless federal regulations … require a shorter period of priority for the lien.

"Action's" context is "**institution of _____ to enforce the lien**." These surrounding words─"institution" and "enforce"─will dictate whether "action" encompasses "non-judicial foreclosure." *Noscitur a sociis* bolsters this contention.

2. In the Context of 116.3116(2),"Action" Encompasses Non-Judicial Foreclosure

This Court has long adhered to *noscitur a sociis,* which instructs a word's meaning should be determined "by the words immediately surrounding it." BLACK'S LAW DICTIONARY 1087 (8th ed. 1999); *see Ford v. State*, 127 Nev. ___, ___, 262 P.3d 1123, 1132 n.8 (2011)(*citing Orr Ditch & Water Co. v. Justice Court of Reno Tp.,* 64 Nev. 138, 146, 178 P.2d 558, 562 (1947)). Here, "institution" and "enforce" surround "action" in 116.3116(2). By looking at where these words are used in 116, this Court can determine whether "action" can include "non-judicial" foreclosure. The term "enforcement" is in 116.31162 ─ 116.31168's treatment of association non-judicial foreclosures; "enforcement" is textually connected with non-judicial foreclosure. Consider 116.31162(1)(b)(2)'s mandate that a notice of default and election to sell must identify "the person authorized by the association to **enforce the lien by sale**." Similarly, 116.31162(1)(c) and 116.31164(2) discuss costs, fees, and expenses incident to an association's "**enforcement** of its lien" through non-judicial foreclosure. 116.665 even contemplates creating programs "relating to common-interest communities, including . . . the **enforcement, including by foreclosure**, of liens . . . for the failure . . . to pay . . . assessments[.]" Likewise, the textual link between "enforcement" and non-judicial foreclosure is further illustrated in 116.310312. Pursuant to 116.310312(4), an association's abatement lien "may be **foreclosed** under . . . 116.31162 to 116.31168." After this provision, 116.310312(6) emphasizes the association's lien has a "period of priority" that "must not be less than the 6 months immediately preceding the **institution of an action to enforce the lien**."

> 4. ….The association … has a lien on the unit for any unpaid amount of the charges. **The lien may be foreclosed under NRS 116.31162 to 116.31168, inclusive**.
>
> …
>
> 6. Except as otherwise provided in this subsection, a lien described in subsection 4 is prior and superior to all liens, claims, encumbrances and titles other than the liens described in paragraphs (a) and (c) of subsection 2 of NRS 116.3116. ….the period of priority of the lien must not be less than the 6 months immediately preceding the **institution of an action to enforce the lien**.

116.310312 is particularly telling because it is incorporated by reference in 116.3116(2) and 116.310312 unequivocally connects non-judicial foreclosure with the phrase "institution of an action to enforce the lien." 116.310312(6). That is, 116.310312(4) guarantees "the lien may be **foreclosed** under NRS 116.31162 to 116.31168[.]" Then, 116.310312(6) mentions "institution of an **action** to enforce the lien." As such, the word "**action**" structurally refers back to and encompasses "**foreclosed**" as used within 116.310312(4). The same holds for the word "institution." Within 116.310312(6)'s phrase "**institution** of an action," the term "**institution**" relates back to and includes 116.310312(4)'s word "**foreclosed**." Consequently, these textual links with non-judicial foreclosure defeat Bank's conclusory pronouncement that it "has not found anywhere in Chapter 116 language like 'institution of an action' used to mean anything other than commencing a judicial lawsuit." (RAB_29-30.) Ultimately, *noscitur a sociis* shows that "action's" context encompasses "non-judicial foreclosure."[14]

E. <u>CC&R Observations Abridge 116.1206(1)(a)</u>

Bank cannot find safe harbor in the CC&R lien subordination clause because certain provisions of NRS 116 cannot be waived: "**Except as expressly provided**

[14] "Action" is dependent on context. So, Bank is correct that in some instances, "action" refers to a lawsuit. For example, 116.3116(8) states "a judgment or decree in any action brought under this section must include costs and reasonable attorney's fees for the prevailing party." References to "judgment or decree" indicate this provision does not include "non-judicial foreclosures." Nonetheless, 116.3116(8) does not constrict the meaning of "action" in 116.3116(2) because these provisions have different contexts. Bank's protestations to the contrary are simply misguided because they do not account for these contextual distinctions.

in this chapter, <u>its provisions may not be varied by agreement, and rights conferred by it may not be waived</u>." NRS 116.1104 (emphasis added). Further, CC&R provisions conflicting with NRS 116 shall be "deemed to conform . . . by operation of law" and resolved in favor of the statute; conflicting CC&R provisions will not be enforced. NRS 116.1206(1); *Boulder Oaks Cmty. Ass'n v. B & J Andrews Enterprises, LLC*, 125 Nev. 397, 406, 215, P.3d 27, 32-33 (2009) "[A]ny other reading of the statute would be contrary to the express purpose of NRS Chapter 116, which is to 'make uniform the law with respect to the subject of this chapter among states enacting it.'" *Id.*, 215 P.3d 27 at 33 (internal citations omitted).

Nothing in 116.1104 or Comment 4 to UCIOA §1-104 allows an association to alter or waive 116.3116(2) (*see* AA_015, 090-91.); nothing in the plain language of 116.3116 "expressly provides for a waiver of the [Association's] right to a priority position for the [Association's] super-priority lien." *7912 Limbwood Court Trust v. Wells Fargo Bank, N.A. ("Limbwood")*, ___ F.Supp.2d ___, 2013 WL 5780793, at *7 (D.Nev. Oct. 28, 2013)(citing NRS 116.3116(2)); *see* James L. Winokur, *Meaner Lienor Community Associations: The "Super Priority" Lien and Related Reforms Under the Uniform Common Interest Ownership Act*, 27 WAKE FOREST L. REV. 353, 365-66 (1992)(**"The lien [under NRS 116.3116(2)] and its statutory priority may not be waived."** (emphasis added)(citing UCIOA §1-

104)). And, 116.3116(2) expressly provides that the super-priority lien cannot be for an amount less than six-months of common assessments even in the face of federal regulation. NRS 116.3116(2). Notably, Bank's suggestion that Association, via its CC&Rs, subordinated its lien to Bank's deed of trust would be a violation of 116.3116(2). Thankfully, 116.1206(1)(a) corrects this violation by providing, "any provision contained in a declaration, bylaw or other governing document of a common-interest community that violates the provisions of this chapter . . . shall be deemed to conform with those provisions by operation of law[.]" (AA_020.)

F. <u>Just as the Bank Distorts the 1993 Legislative History, the Bank also Misrepresents Later Legislative History</u>

Bank distorts 116.3116's legislative history by taking statements out-of-context.

1. <u>2009, AB 204</u>

Bank quotes Ellen Spiegel's testimony in 2009 in support of AB 204[15] on increasing the super-priority amount from 6 to 24 months. (RAB_10.) Bank contends the amendment "makes sense if the first deed of trust remains in first position." (RAB_10.) Nonetheless, if the Legislature intended to require an association to always wait for a bank foreclosure (as Bank suggests), then the

[15] SFR has attached a supplement to its Statutory Addendum with the full history of A.B. 204, S.B. 174 (2011), and S.B. 280 second reprint and as enrolled (2013), for this Court's convenience, pages referenced as (SSA).

Legislature would have extended the priority period for the full 24 months rather than just 9 months. And, the extension from 6 to 9 months makes sense because it gives associations more time to work with delinquent owners before foreclosure. (SSA_016-273.)

2. 2011, SB 174 and SB 204

While the Legislature may have expected banks, rather than associations to foreclose, nothing in the history supports finding an intent to deny associations that power. A complete reading of the legislative history of Senate Bill 174 in 2011 shows the two quotes by Michael Buckley cited by the Bank (RAB_10-11), [16] are simply examples of discussions about what happens to a super-priority lien **if** a bank forecloses on a common-interest community unit. Nothing in the discussions precludes foreclosure by the association. (SSA_320-48; 554-64.) Commissioner Buckley stated "**[t]he HOA's super priority lien dates from when the HOA starts the foreclosure.**" (SSA_557-58)(emphasis added). He further explained "**if there is no foreclosure by the first mortgage, the HOA could foreclose.**" (SSA_558.) Indeed, the history is devoid of any affirmative statement that an association foreclosure including super-priority amounts would not extinguish

[16] The discussion from which the quotes on May 17, 2011 arose were during the Committee's discussion of S.B. 204, which also involved changes to NRS 116, and involved some discussion of S.B. 174. (SSA_555-67.)

junior interests, including a first deed of trust. (SSA_274-625.) Similarly, nothing in the legislative history supports a finding that a lawsuit must be filed for the super-priority lien to come into existence.

Likewise, Bank pulls language from a discussion about the effect of a bank foreclosure on the junior portion of an association's lien to support its proposition that a super-priority lien does not extinguish a first security interest. (RAB_10-11.) This quote is out of context and misleading. Again, reading the full transcript, the purpose of the proposed legislation was to clarify that when a bank forecloses, only the super-priority portion of an association lien survives. This is because the junior portion of the lien is extinguished under real property common law principles. (SSA_554-64.) In responding to Assemblyman Carrillo's concern about eliminating an association's lifeblood─its assessments─Commissioner Buckley explained this limitation only exists if a bank forecloses on its first security interest. If a bank does not foreclose, then an association could foreclose on its full lien. [17] (SSA_557-58.) Put simply, if an association forecloses, then the

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[17] Without the foreclosure of a first deed of trust (or foreclosure of a lien from a different association on a property with a first deed of trust), the association has one lien that is never bifurcated. A lender's payment of the super-priority amount before the sale elevates a first deed of trust from "subordinate" to "prior to" an association lien; it does not split or extinguish the remainder of the association's lien. This is why the Legislature allowed an association to credit bid the full amount of its lien, instead of only the super-priority amounts, at an association foreclosure sale and why the scheme for distribution of proceeds in 116.31164

association's entire lien is gone. (SSA_555.) If the lender forecloses, then the only part that remains of the association's lien is the super-priority amount, which is senior to the first deed of trust. (SSA_558.) When read in context, these statements are consistent with NRED's Advisory Opinion and the interpretation of the UCIOA drafters. (AOB_39-41.)

Senator Allison Copening's testimony cited by the Bank is another example of the Legislature discussing the impact of the foreclosure of a first security interest on an association's lien. (RAB_11.) Nothing in her testimony indicates a first security interest is not extinguished when an association forecloses on a lien containing super-priority amounts. (SSA_565-79.) This Court should reject Bank's contention that the testimony "demonstrates that the 'super priority lien' merely allows HOAs a payment priority[.]" (RAB_12.)

3. __2013, SB 280__

Finally, Bank argues that existing law preserves the survival of a first deed of trust because the 2013 Legislature chose not to adopt language expressly providing for extinguishment. (RAB_12.) Again, Bank isolates one portion of the legislative session that does not give the entire picture. Bank conveniently omits that the Legislature also rejected language that would have stated expressly that

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refers to a single association lien, instead of differentiating between super-priority amounts and the rest of an association lien.

association foreclosure would not extinguish a first security interest. *See* S.B. 280, Second Reprint, p.1 (May 24, 2013), Legislative Counsel Bureau Digest discussing Sec. 10, and *compare* Second Reprint with S.B. 280 as enrolled. (SAA_ 631, 645.) Ultimately, the Legislature chose not to revise the priority language of NRS 116.3116(2) in either way.[18] *See* 2013 Nev. Stat., ch. 552, §7, at 3788.

G. Public Policy Supports SFR & not Bank

1. The One-Action Rule & Price are Irrelevant

Bank argues extinguishment would somehow violate the one-action rule. (RAB_39-40.) To be clear, NRS 116 is excluded from the one-action rule in NRS 40 and through NRS 116.3116(6).[19] Moreover, nothing an association does can force a bank to violate the one-action rule. The fact that neither the borrowers nor Bank paid association dues has no bearing on how the one-action rule is applied to Bank's loan.

[18]The Legislature did, however, adopt two new provisions consistent with NRED's interpretation of the current version of NRS 116.3116. S.B. 280 "authorizes the establishment of an impound account for advance contributions for the payment of assessments" and "authorizes the unit's owner, the authorized agent of a unit's owner or the holder of a security interest on the unit to request from the association a statement concerning certain amounts owed to the association." 2013 Nev. Stat., ch. 552, §7, at 3788.) These provisions are consistent with extinguishment.

[19] 116.3116(6), in the version before the October 2013 amendments, provided: "This section does not prohibit actions to recover sums for which subsection 1 creates a lien or prohibit an association from taking a deed in lieu of foreclosure." This is now found in 116.3116(7).

Equally inapplicable is Bank's argument that SFR bought the house for a "low price." (RAB_6, 10, 34, 38, 39.) In reality, the market dictates price. More precisely, lenders have, by repeatedly bringing meritless claims and advocating for self-serving interpolations of the statute, purposefully confused courts to manufacture ambiguity where none exists. *See J.E. Dunn Nw., Inc. v. Corus Const. Venture, LLC*, 127 Nev. ___, ___, 249 P.3d 501, 506 (2011)(ruling against a party "resorting to 'ingenuity to create ambiguity' that does not exist"). Accordingly, until lenders stop using "ingenuity to create ambiguity" SFR, like any prudent buyer, must price into its purchase the nuisance costs of possibly defending the marketability of its title from frivolous lawsuits.

Ultimately, Bank focuses on the one action rule and price to avoid the statute's text and to conceal Bank's own inaction. Specifically, Bank could have preserved its collateral by paying the super priority amount (a sum lower than the purchase price); it chose to pay nothing. Alternatively, if Bank believed Association's foreclosure was improper, then it had ample time to "seek relief in a court to enjoin the foreclosure, just as SFR has had to do here[.]" (AOB_31)(citing *CitiMortgage, Inc. v. Liberty at Mayfield Cmty. Ass'n*, No. 2:13-cv-02033-gmm-gwf, 2013 WL 6388727 (D. Nev. Dec. 5, 2013)). Instead, it sat on its rights.

2. <u>Extinguishment does not Impact the Foreclosure Mediation Program</u>

Bank also argues the statute should not be enforced as written because doing so undermines the purpose of the Foreclosure Mediation Program. (RAB_38.) Again, Bank manufactures conflict where none exists. Any potential for an association foreclosure to interfere with the purposes of the Foreclosure Mediation Program was already addressed by the Legislature in 2013. As of October 1, 2013, an association cannot foreclose on a person's primary residence where a bank has filed a notice of default until the State issues a certificate of mediation.[20] NRS 116.31162(6); 2013 Stat. Nev., Ch. 536, §4, at 3484.

3. <u>Requiring Lenders to Protect their Collateral does not Undo an Equitable Balance; Nor will Banks Stop Lending</u>

Requiring lenders to protect their investments does not impose an unfair burden on lenders. (RAB_30.) Nor will Bank's unsupported predictions of recession or lending freezes result from this Court correctly interpreting the statute. In fact, both arguments are disproven by policies adopted by Fannie Mae and

[20] Yet again recognizing the important purpose of NRS 116.3116 to provide associations with much-needed assessments, the 2013 Legislature balanced the restriction by requiring assessments to be paid during participation in the Foreclosure Mediation Program. NRS 107.086(10); 2013 Nev. Stat., Chap. 536, §10, at 3482.

Freddie Mac.[21] Rather than refuse to purchase loans in common-interest communities, Fannie Mae and Freddie Mac have adopted policies for their servicers to pay super-priority amounts to protect priority in states that grant super-priority liens to associations. Fannie Mae's servicing guidelines actually require servicers to protect its priority by paying the super-priority amounts in states that grant super-priority liens to associations. *See* Fannie Mae Servicing Guide Announcement SVC-2012-05 (April 11, 2012).[22] (5JA_755-57.) Similarly, Freddie Mac requires servicers to pay any association "assessments prior to the foreclosure sale date if they are, or may become, a First Lien priority on [the property] . . . ." Freddie Mac Bulletin, No. 2013-15 (Aug. 15, 2013).[23] *See also* James L. Winokur, *Meaner Liener Community Associations: The "Super Priority" Lien and Related Reforms Under the Uniform Common Interest Ownership Act*, 27 WAKE FOREST L. REV. 353, 389-90 (1992). Furthermore, Henry J. Judy, former General Counsel for Freddie Mac, expressly acknowledged that foreclosure, preferably by sale, of the super-priority lien extinguishes a first security interest. *See* Henry J. Judy and Robert A. Wittie, *Uniform Condominium Act: Selected Key Issues*, 13 REAL PROP.

[21] In fact, Fannie Mae and Freddie Mac were at the table with other industry players when the super-priority lien was conceived and included in the 1977 Uniform Condominium Act.

[22] *Available at* https://www.fanniemae.com/content/announcement/svc1205.pdf.

[23] *Available at* http://www.freddiemac.com/sell/guide/bulletins/pdf/bll1315.pdf.

PROB. & TR. J. 437, 480, 484, 515-16 (1978) ("Judy").[24]

H. Bank Misperceives UCIOA, NRED, & Extra-Nevada Law

SFR's opening brief reviewed how UCIOA § 3-116's comments supported extinguishment. (AOB_43-44.) In response, Bank—without any supporting authority—claims the UCIOA comments contemplate "a foreclosure by an HOA with a first deed of trust still encumbering the property." (RAB_31.) This is patently incorrect, disproved by the comments themselves and the statements made by one of the UCIOA's drafters. (AOB_44.)

Similarly, Bank offers a litany of justifications for discounting the Nevada Real Estate Division's ("NRED") Opinion 13-01. *Compare* (RAB_35-36), *with* (AOB_39-41.) Such justifications are, however, unpersuasive because NRED unambiguously noted "an association can foreclose its super priority lien and the first security holder will either pay the super priority lien amount or **lose its security**." (AOB_40)(emphasis added.) Urging the Court to accept one of its two contradictory interpretations of 116.3116, Bank claims that no other UCIOA state allows extinguishment of a first security interest through the nonjudicial

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[24] This article discusses the super-priority provisions of the Uniform Condominium Act, one of the Uniform Acts from which the UCIOA was developed. (2JA_207-12.) The language of UCIOA § 3-116 is almost identical to UCA § 3-115, discussed in the article. See UCIOA § 3-116 (2JA_213-18) with UCA § 3-115, Judy, at 534.

foreclosure of a super priority lien. (RAB_9.) Bank pretends as if the issue has been conclusively decided in every jurisdiction. It has not. Moreover, Bank's comparison conflates the affirmative choices made by each jurisdiction's legislature on *how* an association may foreclose with the *effect* of a proper foreclosure of a super-priority lien on a first security interest. For instance, at least one Rhode Island court interpreting almost the same exact super priority language,[25] found that not only did the association lien have partial priority over the first mortgage, but the nonjudicial foreclosure would extinguish the first and second mortgage. *Crestar Mortgage v. Woodland Est. Condo.*, NO. 91-7284, 1992 WL 813553 (R.I. Super. May 1, 1992)(unpublished)(nonjudicial foreclosure of an association lien with priority over first and second mortgages would extinguish both mortgages).

Furthermore, in those non-judicial foreclosure states opting to limit associations to judicial foreclosures of their super-priority amounts, the language was expressly incorporated into the statute by the legislature, not the courts. *See Harrah's Operating Co., Inc. v. State, Dep't of Taxation*, 130 Nev. ___, ___ P.3d ___ (Adv. Op. 15, March 20, 2013), at 9 n. 2 (noting that application of the law

[25] SFR notes that the Rhode Island Legislature amended the statute in 1992, but the amendment was not applicable to the case at bar. *Crestar Mortgage*, 1992 WL 813553 at *2 n.1. Therefore, the case is instructive in analyzing NRS 116.3116.

will result in tax revenue loss but recognizing that it is the law, not the outcome, that controls, stating "this Court must apply the statutes as written . . . [a]ny change must come from the Legislature, not this court."). When this Court looks to other UCIOA states it should do so for the effect of a properly held association foreclosure, authorized by a state's version of §3-116, on a first security interest. That review will lead this Court to the correct conclusion: non-judicial foreclosure on a lien arising under 116.3116 extinguishes a first security interest. *See, e.g., Summerhill Village Homeowners Ass'n v. Roughly*, 289 P.3d 645, 649 (Wash. Ct. App. 2012)(association foreclosure extinguished first deed of trust); *see also* Joint Editorial Board for Uniform Real Property Acts, *Six-Month "Limited Priority Lien" for Association Fees under the Uniform Common Interest Ownership Act* (June 1, 2013).[26]

I. **SFR is a Bona Fide Purchaser**

Though not raised in SFR's opening brief and not addressed by the district court in its order, Bank opines SFR is not a bona fide purchaser ("BFP") because the CC&Rs and deed of trust were recorded. Bank ignores that SFR reviewed the CC&Rs and applied 116.1206(1)(a) to those provisions that violate 116, including

[26] Available at:
http://www.uniformlaws.org/shared/docs/jeburpa/2013jun1_JEBURPA_UCIOA%20Lien%20Priority%20Report.pdf.

the mortgage protection clause. SFR also looked at the deeds of trust and determined which would be extinguished by a foreclosure under 116. Relying on 116 and real property law, SFR concluded that Bank's deed of trust was subordinate to the association's lien and purchased the property as a BFP.

J. <u>Bank's Arguments About Dismissal & Lis Pendens are Meritless</u>

According to Bank, SFR's case was properly dismissed because extinguishment did not occur. (RAB_36.) This is fallacious because Association's foreclosure did, in fact, extinguish Bank's deed of trust. (AOB_19-45.)[27] Also, Bank's defense of the court's decision to expunge the lis pendens is unavailing because SFR satisfied 14.010 and 14.015. (AOB_55.) In passing, Bank acknowledges SFR "can easily be compensated with a monetary amount for any loss of 'title.'" (RAB_37, 40.) This acknowledgement demonstrates that dismissal should have, at a minimum, been without prejudice.

/ / /

[27] Bank's remarks about the unjust enrichment claim are equally inapposite for the reasons stated in SFR's opening brief. (AOB_52-53.)

III.
CONCLUSION

Based on the foregoing, and for the reasons set forth in the opening brief, this Court should reverse and remand with instructions to vacate the district court's order, quiet title in SFR, and permanently enjoin Bank from foreclosing.

DATED this 20th day of March, 2014.

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CERTIFICATE OF COMPLIANCE

1. I certify that this brief complies with the formatting requirements of NRAP 32(a)(4), the typeface requirements of NRAP 32(a)(5) and the type style requirements of NRAP 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2007 with 14 point, double-spaced Times New Roman font.

2. I further certify that this brief complies with the page-or type-volume limitations of NRAP 32(a)(7) because, excluding the pages of the brief exempted by NRAP 32(a)(7)(C), it is proportionately spaced, has a typeface of 14 points or more and contains 6,205 words.

I hereby certify that I have read this appellate brief, and to the best of my knowledge, information, and belief, it is not frivolous or interposed for any improper purpose. I further certify that this brief complies with all applicable Nevada Rules of Appellate Procedure, in particular NRAP 28(e), which requires every assertion in the brief regarding matters in the record to be supported by a reference to the page of the transcript or appendix where the matter relied on is to be found.

///

I understand that I may be subject to sanction in the event that the accompanying brief is not in conformity with the requirements of the Nevada Rules of Appellate Procedure.

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I hereby certify that this document was filed electronically with the Nevada Supreme Court on the 20th day of March, 2014. Electronic service of the foregoing Appellant's Reply Brief and Appellant's Supplemental Statutory Addendum shall be made in accordance with the Master Service List as follows:

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