Shadow Wood Affirmed Established Legal Standards Relating to HOA Foreclosures

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The mortgage crisis triggered waves of non-judicial foreclosures and litigation in Nevada over the law governing the foreclosure of homeowner association ("HOA") assessment liens. The waters remain unsettled, even after *SFR Investments Pool 1, LLC v. U.S. Bank, N.A.*, 130 Nev. Adv. Op. 75, 334 P.3d 408 (2014) ("*SFR*"). Parties clash over commercial reasonableness, constitutionality of NRS 116.3116, *et seq.*, what the super-priority lien includes, and various other issues. Lower court rulings vary. On January 28, 2016, the Nevada Supreme Court released *Shadow Wood Homeowners Association, Inc., v. New York Community Bancorp, Inc.*, 132 Nev. Adv. Op. 5, _P.3d_, 2016 WL 347979 ("*Shadow Wood*"). Litigants disagree over the interpretation of *Shadow Wood*, some arguing that the case upheld current law and others claiming that it acted as a game changer in HOA foreclosure litigation.

The disparate interpretations of *Shadow Wood* created fodder for those who are displeased with how the Nevada Supreme Court has interpreted our laws.

Shadow Wood supports existing legal standards

The *Shadow Wood* decision built upon and did not overturn any existing law. In the twenty-five page decision, the Court referenced *SFR* three times, citing *SFR* for authority and clarification. 132 Nev. Adv. Op. 5, at 3, 8, 23. The Court amplified "history and basic rules" and "common law" principles of equity, and urged lower courts to consider, weigh and assess "competing equities" and the "entirety of circumstances." *Id.* at 2, 20, 24.

It should be noted that NRS 116.3116, *et seq.*, is founded upon a uniform statutory scheme, with *vetted* foreclosure procedures, long accepted by *all* industry players – banks and government sponsored enterprises included. *See*, *Can Associations Have Priority over Fannie and Freddie?* Probate and Property Magazine: Volume 29 No. 04; R. Wilson Freyermuth, Dale A. Whitman, http://www.americanbar.org/publications/probate_property_magazine_2012/2015/july_august_2015/2015_aba_rpte_pp_v29_3_article_freyermuth_whitman_can_associations_have_priority_over_fannie_and_freddie.html. Within that framework, *Shadow Wood* reinforced fundamental legal concepts. Had the Court intended to overturn or distinguish precedent, it would have done so unequivocally. *Shadow Wood* reinforces the integrity and fairness of non-judicial foreclosure law, upon which innocent developers, HOAs, property managers, trustees, bona fide purchasers ("BFPs"), and lenders, have collectively relied for decades.

Shadow Wood unequivocally affirms that there must be a showing of "fraud, unfairness, or oppression" to set aside an HOA foreclosure sale, and rejected any blanket rule or formulaic approach. *Id.* at 15 (citing, *inter alia*, *Long v. Towne,* 98 Nev. 11, 13, 639 P.2d. 528, 530 (1982); *Brunzell v. Woodbury*, 85 Nev. 29, 449 P.2d 158 (1969)). "Black-letter" law in Nevada in this regard remains unchanged. A sale cannot be set aside as commercially unreasonable based on price alone. The Court did not adopt the Restatement (Third) of Property: Mortgages § 8.3, cmt. b., but quoted

part of the Restatement: "courts can properly take into account the fact that the value shown on a recent appraisal is not necessarily the same as the property's fair market value on the foreclosure date." This suggests that fair market value of a foreclosure property would not be the same as a fair market non-foreclosure sale. *Shadow Wood*, at p. 16, n. 3.

Shadow Wood shed light on the bona fide purchaser doctrine in non-judicial foreclosure sales, emphasizing equity vis-à-vis a bona fide purchaser (BFP). *Shadow Wood* noted that "[c]onsideration of harm to potentially innocent third parties is especially pertinent here where NYCB did not use the legal remedies available to it to prevent the property from being sold to a third party . . . ." *Id.* at 21, n. 7. Where the bank had access to all the facts surrounding the HOA foreclosure, and made a mistake as to the legal consequences of its actions, "equity should normally not interfere, especially where the rights of third parties might be prejudiced thereby." *Id.* at 24. *Shadow* quoted longstanding Nevada precedent governing who is a BFP. *Id.* at 22. It appears that in certain circumstances, upon weighing competing equities, and even in cases involving fraud, unfairness or oppression in HOA foreclosures, BFPs who purchase without notice hold free and clear title. *Id.* at 24. It follows in those cases that banks would be entitled to pursue any legal remedies for damages versus the HOA and Trustee, as applicable.

Shadow Wood left no doubt that it is plausible for an HOA to include fees and costs in the super-priority amount: "We conclude, though, that the district court erred in limiting the HOA lien amount to nine months of common expense assessments . . . ." *Id.* at 1. "[B]ecause the parties did not develop in district court what the fees and costs represent, when they were incurred, their (un)reasonableness, and the impact, if any, of Shadow Wood's covenants, conditions and restrictions (CC&Rs) on their allowance, we leave this issue to further development in the district court on remand." *Id.* at 18. (n. 5 omitted.)

Ultimately, the Court noted that the bank "did not tender the amount provided in the notice of sale, as statute and the notice itself instructed, and did not meet its burden to show that no genuine issues of material fact existed regarding the proper amount of Shadow Wood's lien or Gogo Way's bona fide status." *Id.* at 24.

Conclusion

Certain litigants relish Mark Twain's maxim: "Never argue with a fool; onlookers may not be able to tell the difference." The disparate interpretations of *Shadow Wood* created fodder for those who are displeased with how the Nevada Supreme Court has interpreted our laws. Before *SFR*, banks interpreted the uniform HOA lien law in a way to disregard the consequences of not paying off the super-priority lien. *SFR* clarified the law, but it has received the same treatment. The banking institutions deploy massive resources . . . arguing. They pluck quotes from background and dicta, twisting the effect of the law against the intentions of the Court. *Shadow Wood* did say: "the record demonstrates too many unresolved issues of material fact for the district court to assess the competing equities in this case as between Shadow Wood and NYCB on the summary judgment record assembled." *Id.* at 20. (emphasis added.) The Nevada State Supreme Court also left issues *in that case* for "further development in the district court on remand."

Nonetheless, the Court in *Shadow Wood* did not intend to prevent district courts from granting summary judgment. The Court admonished otherwise. *Id.* at 7-8. Although different factions disagree as to interpretation of *Shadow Wood*, given the right circumstances, judges need not hesitate to grant summary judgment post-*Shadow Wood*.

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