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# Whose Lien is it Anyway? A Comparative Analysis of Approaches to Homeowner Association Lien Priority

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## INTRODUCTION

No one likes to play against a stacked deck, yet both homeowners' associations ("HOAs") and banks tend to make the complaint that this is exactly what is happening post-foreclosure crisis. HOAs complain that when a bank forecloses, the foreclosure wipes away any chance at recovery against unpaid assessments. Banks claim that the priority-adjustment remedy to that problem deals their chances of recovery a bad hand from the bottom of the deck despite having what they thought was an ace up their sleeve: priority of time. How a jurisdiction sets lien priority between an HOA and lender largely determines who will have the winning hand. Where to set that line is an exceedingly difficult problem for which jurisdictions are struggling to find a practical solution. This Comment seeks to explore this balancing act in detail.

Assume a homeowner's residence is located within a neighborhood with an HOA,<sup>1</sup> and was purchased through a first deed of trust with a lender. The homeowner falls on hard times and is unable to pay either the monthly assessments required by the HOA or payments on their loan to the lender. Both the HOA and the lender initiate separate non-judicial foreclosure proceedings relatively close in time, but the lender's sale is postponed for an unrelated reason. In the meantime, the HOA holds their foreclosure sale and the home is bought by a subsequent purchaser for much less than market value. Having knowledge of the deed of trust, the subsequent purchaser brings a quiet title action, alleging the lender's first deed of trust was extinguished by the HOA's foreclosure on its lien.

This is the situation that confronted the Nevada Supreme Court in the 2014 case, *SFR Investments Pool 1, LLC v. U.S. Bank*.<sup>2</sup> In a decision that "set off bank alarms," the court held that according to the state's lien priority statute, after the non-judicial foreclosure sale for \$6000, the HOA lien, valued at \$4542, took priority over *and extinguished* the lender's \$800,000 first deed of trust.<sup>3</sup>

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<sup>1</sup> This note groups together all common interest communities ("CICs"), which include both planned housing communities with homeowners' associations ("HOAs") and condominium communities. While there are differences in general law between these two types of communities, there are no major general differences with respect to lien priority. Therefore, HOAs, condominium associations, and CICs will be used interchangeably throughout this Comment.

<sup>2</sup> See *SFR Investments Pool 1, LLC v. U.S. Bank*, 334 P.3d 408, 409–10 (Nev. 2014).

<sup>3</sup> Mark Gardberg, *HOAs vs. Banks vs. Homeowners: Nevada Shifts Ground on Superiority HOA Liens*, NEV. LAW., June 2016, at 13, 14; see also Katie McConnell, *The Super Priority of Homeowners' Associations*, NEV. LAW., June 2016, at 22, 23; *HOA Foreclosures Leave Banks Empty-Handed*, REALTOR MAG. (Oct. 15, 2014),

Although some may find such an outcome shocking, a contrary conclusion would also have negative consequences. The inability to collect dues (if not aided by such statutory priority adjustments) can be crippling to the ability of an HOA to operate, sometimes causing it to pass on these costs to other association members.<sup>4</sup> Such a limitation on an association's ability to collect is particularly perceptible during a slump in the real estate market.

Consider just one example from Kings Lake Townhomes in Gibsonton, Florida.<sup>5</sup> During the financial recession following the 2008 foreclosure crisis, sixty percent of the 242 condominium owners of this community association were delinquent in paying their \$194 monthly assessments.<sup>6</sup> The Kings Lake neighborhood association had over \$150,000 in delinquent dues and did not have enough funding in its reserve to even replace a broken security gate when needed.<sup>7</sup> In order to fix the gate, the association had to levy an additional assessment on its member homeowners of \$230 each for three months.<sup>8</sup>

By both raising fees for paying members and foreclosing on non-paying member's homes, the association at Kings Lake was able to prevent itself from becoming insolvent.<sup>9</sup> In response to outcry from members footing the bill of the higher fees, the association began to aggressively pursue foreclosures on its delinquent members.<sup>10</sup> The association's option to foreclose was aided by Florida's statutory priority allowing an association to collect a year's worth of dues upon foreclosure by a lender.<sup>11</sup> Counsel for the Kings Lake Association noted foreclosure is typically a more effective method of collecting assessments

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<http://realtormag.realtor.org/daily-news/2014/10/16/hoa-foreclosures-leave-banks-empty-handed> [<http://perma.cc/E3EA-DBJX>]; Davis S. Vaughn, *Lien Back: Why Homeowner Association Super-Priority Lien Statutes Should Be Repealed* (2017), <https://ssrn.com/abstract=2903577> [<http://perma.cc/7RP4-VDEB>].

<sup>4</sup> Jeff Collins, *O.C. homeowners associations in a cash crunch*, ORANGE COUNTY REGISTER (Sept. 29, 2008, 6:00 PM), <https://www.oregister.com/2008/09/28/oc-homeowners-associations-in-cash-crunch/> [<http://perma.cc/CW87-EH53>] (“A Placentia complex with at least 33 homes in foreclosure or default ended up raising monthly fees and levying a \$1,000 special assessment.”).

<sup>5</sup> Shannon Behnken, *Foreclosing Isn't Just For Lenders These Days*, TAMPA BAY TIMES, <http://www.tbo.com/business/business/2008/dec/28/bz-foreclosing-isnt-just-for-lenders-these-days-ar-111034/> [<http://perma.cc/5Q9L-8B9J>] (last updated May 22, 2013, 3:10 PM).

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.* According to the report, the association board will be raising fees an additional \$31 to a total of \$225 per month in hopes it will be enough, but will be “keeping the association's foreclosure attorney on speed dial.” *Id.*

<sup>11</sup> *Id.*

against delinquent members than other methods, such as pursuing a money judgment against the debtor.<sup>12</sup>

Nevertheless, this remedy's potency and power is dependent on the laws governing lien priority in the home state of the foreclosing community association. In some jurisdictions, a lender's lien has priority over an association's lien.<sup>13</sup> In such a jurisdiction, a lender's foreclosure on the property first for less than the amount of its lien will leave no residual for the association to pursue.<sup>14</sup> Similarly, a foreclosing association will have difficulty finding a buyer under such law because a purchaser would take the property with a large mortgage lien still attached.<sup>15</sup> Under these circumstances, the HOA's most reliable option for recovery of the delinquency is rendered impotent and inadequate.<sup>16</sup> HOAs responded to these circumstances by joining and supporting interest groups, such as the Community Associations Institute ("CAI"), which lobbied in support of increased association lien priority under state law.<sup>17</sup>

These contrasting vignettes set the scene for the conflict: choosing which lien should have priority, the lien held by the association or the lien held by the lender. These tales of competing claims also raise a larger question of who should bear the cost of unpaid homeowner association dues when the delinquent owner is not a practical option. In response to pressure from both HOAs and lenders, states have attempted to find an acceptable solution to balance the competing interests and manage the conflict. These solutions have arguably sometimes fallen short in both fairness and practicality—metrics critical to this Comment's evaluation of the lien priority debate.

Nevada's controversial statute and its judicial interpretation are the result of a nation-wide trend cultivated by the lobbying efforts of HOA interest groups to increase the priority of association liens in response to the financial crisis of 2008.<sup>18</sup> That

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<sup>12</sup> *Id.*

<sup>13</sup> *See infra* Part I.

<sup>14</sup> *See infra id.*

<sup>15</sup> *See infra id.*

<sup>16</sup> *See infra id.*

<sup>17</sup> *See State Advocacy*, CMTY. ASS'NS. INST., <https://www.caionline.org/Advocacy/StateAdvocacy/Pages/default.aspx> [<http://perma.cc/8DZZ-KRGG>] (last visited Apr. 17, 2017). State governments are urged to consider and give favorable treatment to one or more of the uniform acts, such as the Uniform Common Interest Ownership Act ("UCIOA"), which contains favorable provisions for community association lien priority. *Id.*

<sup>18</sup> *See* Robert Aalberts, *Super Liens Help Fix Homeowners Associations But Will They Survive Politically?*, 44 REAL EST. L.J. 327, 327–29 (2015); *see also* Casey Perkins, Note, *Privatopia in Distress: The Impact of the Foreclosures Crisis on Homeowners' Associations*, 10 NEV. L.J. 561, 566–68, 580–81 (2010) (summarizing the recession caused by the 2008 foreclosure crisis).

trend is now being met with pushback from lenders across the United States.<sup>19</sup> Experts claim that while common interest communities (“CICs”) have formidable allies in state legislatures, lending institutions and real estate brokers have just as much or more influence to counter this shift in transactional power.<sup>20</sup> In Nevada, home of the *SFR Investments* decision and the epicenter of the debate, lenders and real estate brokers with “considerable resources and political experience” are currently building pressure for change.<sup>21</sup>

The law is far from uniform on how each state approaches the issue of HOA lien priority (in terms of both statute and case law), and states take different approaches when addressing the issue of what priority an HOA lien should take in relation to other instruments.<sup>22</sup> For ease of analysis, this Comment has grouped the many variations in state law into three distinct categories based on the priority given to an association’s assessment lien. These three categories include: the first-in-time approach, the super lien priority approach, and the purchaser liability approach.

This Comment examines how three different jurisdictions, each representing one of the approaches mentioned above, address the issue. It then discusses which approach, or combination thereof, most adequately and fairly balances the competing policy interests. In this evaluation, this Comment focuses its analysis on which methodology (1) better assists an HOA in collecting delinquent assessments without treating the lender’s interest unfairly, and (2) most adequately balances the competing public policy concerns. To better understand the different approaches each jurisdiction takes and frame the issue presented, we will first need an understanding of the general law that governs lien priority and the basic history of the development of super lien priority statutes. The next Part discusses that background and history.

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<sup>19</sup> See Aalberts, *supra* note 18, at 327–29.

<sup>20</sup> *Id.* (“But now super lien laws are under attack by more powerful forces than even homeowners associations might be able to withstand—lenders and real estate brokers.”).

<sup>21</sup> *Id.* However, HOA proponents dismiss this reaction as mere bluster since it would be impractical for lenders to stop doing business in all jurisdictions with super-lien priority statutes. *Id.*

<sup>22</sup> See Christian J. Bromley, *Encouraging Cooperation: Harmonizing the Battle of Association and Mortgage Lien Priority in America’s Common Interest Communities*, 43 REAL EST. L.J. 255, 257–59, 276–85 (2014). Recovery by an association is dependent on lien priority law in the state which has jurisdiction over the property. *Id.* A survey of these jurisdictions has revealed “inconsistent approaches to determining an association’s priority, or lack thereof, against the liens of any mortgages.” *Id.*

## I. BACKGROUND

To understand the issue of which approach most fairly balances competing policy interests, one must understand the basic mechanics of lien priority law. In order to provide a framework for analysis, this Part provides a brief overview of the general law governing HOA lien priority.

Covenants, which are created when an HOA is formed by recording a declaration of the community association's conditions, covenants, and restrictions ("CC&Rs"), often require homeowners to join an association and pay dues.<sup>23</sup> The governing documents of the association must provide for the collection of regular and special assessments from members to pay for community services and amenities, such as maintenance of common areas and facilities.<sup>24</sup> The members' obligation to pay assessments begins with the first conveyance of the subdivision, and this obligation is transferred to all subsequent purchasers of the property.<sup>25</sup>

Assessments accrued while a member owns the property are personal liabilities, which as a default rule, remain a personal liability to a debtor even after the property is transferred to another, whether voluntarily or involuntarily.<sup>26</sup> However, a member is not liable for dues that accrue either before or after their ownership of the HOA property.<sup>27</sup> Consequently, a purchaser at a foreclosure sale is usually not liable for a previous member's delinquent dues, while that previous member remains personally responsible for the debt to the HOA.<sup>28</sup>

The power an association has to impose assessments on its members can lead to the ability of the HOA to create a lien on the property that runs with the land.<sup>29</sup> Priority between an HOA lien and a lender's mortgage or deed of trust is usually determined by first-in-time principles unless modified by statute or agreement.<sup>30</sup> Generally, the HOA lien is perfected when the owner defaults on paying dues, and in some states like California, the recordation

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<sup>23</sup> RICHARD R. POWELL, *POWELL ON REAL PROPERTY* § 54.08 (Matthew Bender ed., 1995).

<sup>24</sup> *Id.* at 145–47.

<sup>25</sup> Tara C. Narayanan & Ella K. Gower, *Common Interest Developments*, in 8 MILLER & STARR CALIFORNIA REAL ESTATE § 28:93 (4th ed. 2017).

<sup>26</sup> *Id.* § 28:97.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> WAYNE S. HYATT, *CONDOMINIUM AND HOMEOWNER ASSOCIATION PRACTICE* 117–19 (3d ed. 2000).

<sup>30</sup> Karl E. Geier, *Recording and Priorities*, in 4 MILLER & STARR CALIFORNIA REAL ESTATE § 10.1 (4th ed. 2017).

of the delinquent assessment.<sup>31</sup> Since the lien is usually not perfected until the assessment becomes delinquent, a properly recorded first mortgage or deed of trust will normally be first in time in relation to an HOA lien as it generally occurs at the purchase of the property.<sup>32</sup>

Chief Justice John Marshall in *Rankin v. Scott* described the temporal priority relationship of liens under the first-in-time principle in the following terms:

The principle is believed to be universal, that a prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds, unless the lien be intrinsically defective, or be displaced by some act of the party holding it, which shall postpone him in a Court of law or equity to a subsequent claimant.<sup>33</sup>

Thus, the principle of first-in-time is universally recognized by every United States jurisdiction as a guiding principle for determining lien seniority that acts as a default rule absent modification by agreement or statute.

As a general rule, a purchaser at a foreclosure sale takes title to property free of all liens that are junior to the lien under which the property is sold.<sup>34</sup> However, a purchaser usually takes title subject to any liens that have seniority over the lien under which the property is sold.<sup>35</sup> Priority establishing seniority of liens is often modified by state statute.<sup>36</sup> In reference to the first-in-time principle discussed in *Rankin* above, the Supreme Court noted the default nature of the principle by explaining, “[t]his principle is widely accepted and applied, *in the absence of legislation to the contrary*.”<sup>37</sup> This modification by statute and judicial interpretation of such statute is what has precipitated the super lien priority statute controversy that Nevada faces today.

A brief explanation of the developmental history of super lien statutes will help to better explain the nature of this controversy. This Part proceeds with such a summary explanation by starting with an analysis of an example of a common law first-in-time regime and moving forward in time to the creation of HOA true super lien priority regimes in certain jurisdictions.

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<sup>31</sup> See NARAYANAN & GOWER, *supra* note 25, § 28:97; see also POWELL, *supra* note 23, § 37.41.

<sup>32</sup> POWELL, *supra* note 23, § 37.41.

<sup>33</sup> *Rankin v. Scott*, 25 U.S. 177, 179 (1827).

<sup>34</sup> Geier, *supra* note 30, § 10:1.

<sup>35</sup> *Id.*

<sup>36</sup> See R. Wilson Fryermuth & Dale A. Whitman, *Can Associations Have Priority Over Fannie or Freddie?*, 29 PROB. & PROP., July/August 2015, at 27, 27–28.

<sup>37</sup> *U.S. v. City of New Britain, Conn.*, 347 U.S. 81, 85 (1954) (emphasis added).

Currently, the laws of twenty-two states alter the general first-in-time rule of priority by giving HOA liens a “super priority” status.<sup>38</sup> This priority status gives association liens superior priority to first mortgages and deeds of trust in some form or another, accomplishing those goals through differing mechanisms between jurisdictions.<sup>39</sup> The degree of priority varies substantially, with some states adopting different generations of model and uniform laws (such as the Uniform Common Interest Ownership Act (“UCIOA”)) promulgated by organizations like the Uniform Law Commission.<sup>40</sup>

The law of community association lien priority has developed and diverged from the nearly universal common law principle of first-in-time through the adoption or rejection of different uniform laws by state legislatures. Over the past fifty years, state laws on CICs have developed from legislative incorporation of one of several (model or uniform) so-called “foundational” statutes that can be said to include: the 1958 Puerto Rican Horizontal Property Act or Horizontal Property Regime Act (“HPRA”), the 1962 Federal Housing Administration’s (“FHA”) Model Statute for the Creation of Apartment Ownership, the 1980 Uniform Condominium Act (“UCA”), and both the 1982 UCIOA and 1982 Uniform Planned Community Act (“UPCA”).<sup>41</sup>

Of the twenty-two states that have adopted super lien priority statutes, eight have adopted versions of the UCIOA,<sup>42</sup> five the UCA,<sup>43</sup> two the HPRA,<sup>44</sup> and seven have “stand-alone” statutes,<sup>45</sup> giving some type of priority to association liens.<sup>45</sup> One

<sup>38</sup> Hugh Lewis, *National Matrix of Association “Super-priority” Lien Legislation*, UNIF. LAW COMM’N 1 (Oct. 14, 2016, 4:36 PM), <http://www.uniformlaws.org/shared/docs/jeburpa/CAlienprioritymatrix2013.pdf> [<http://perma.cc/7R3B-SP43>].

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* at 1–3.

<sup>41</sup> *Id.*; *Acts*, UNIF. LAW COMM’N, <http://www.uniformlaws.org/Acts.aspx> [<http://perma.cc/X9YH-UQ82>] (last visited April 4, 2017). While a detailed analysis of the logistical workings of these uniform statutes is beyond the scope of this Comment, it is sufficient to understand that the states’ incorporation of all or part of these varied foundational schemes is largely the basis for the wide variety of approaches taken by different jurisdictions in regard to association lien priority. For a detailed discussion of the history and the mechanics of these statutory schemes, see Andrea J. Boyack & William E. Foster, *Muddying the Waterfall: How Ambiguous Liability Statutes Distort Creditor Priority in Condominium Foreclosures*, 67 ARK. L. REV. 225, 244–45 (2014).

<sup>42</sup> Lewis, *supra* note 38, at 2. States that have adopted versions of the UCIOA with HOA lien priority include: Alaska, Colorado, Connecticut, Delaware, Minnesota, Nevada, Vermont, and West Virginia. *Id.*

<sup>43</sup> *Id.* UCA states with HOA lien priority include: Alabama, Pennsylvania, Rhode Island, Tennessee, and Washington. Other states adopting portions of the UCA without the priority provision are omitted from this list. *Id.*

<sup>44</sup> *Id.* at 2 n.3. HPRA states with HOA lien priority include: Hawaii and Massachusetts. *Id.*

<sup>45</sup> *Id.* “Stand-alone” jurisdictions with HOA lien priority include: District of Columbia, Florida, Illinois, Maryland, New Hampshire, New Jersey, and Oregon. *Id.*

state has also adopted the UPCA that similarly includes a super lien priority statute.<sup>46</sup> Certain states that adopted an increased HOA lien priority under these uniform laws came to question the priority's sufficiency during the foreclosure crisis of 2008.<sup>47</sup>

During the foreclosure crisis, homeowners were defaulting on both their HOA assessments and mortgages.<sup>48</sup> This “snowball effect” began when the housing market dropped and subprime loans ballooned causing homeowners, many of whom were speculating, to walk away from their underwater homes that were worth a fraction of what was owed on the mortgages.<sup>49</sup> When these homeowners stopped paying their mortgages, many also stopped paying their assessment dues causing the associations' reserve funds to run dry.<sup>50</sup> The unmitigated volume of owners delinquent in paying their assessments—that in some cases were ten times higher than before the recession—was causing associations to become insolvent and incapable of providing the services they were obligated to perform.<sup>51</sup> In response, HOAs in many states were able to successfully lobby their state legislatures and courts through association interest groups to increase their liens' priority.<sup>52</sup>

One such HOA lobbying organization, CAI, seeks to influence state legislatures and courts to increase priority of HOA liens “equal to the amount of the assessments that are due over the term of the lien of a mortgage or first deed of trust.”<sup>53</sup> The CAI and other similar organizations were able to convince legislators and courts to increase association lien priority above what was afforded under previous common law and statute,

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<sup>46</sup> *Id.* In addition to the UCA, Pennsylvania is the only state thus far to adopt the UPCA that also provides for increased HOA lien priority. *Id.*

<sup>47</sup> See Aalberts, *supra* note 18, at 327–28.

<sup>48</sup> Kylee Gloeckner, Note, *Nevada's Foreclosure Epidemic: Homeowner Associations' Super-Priority Liens Not So "Super" for Some*, 15 NEV. L.J. 326, 326–27 (2014).

<sup>49</sup> Dennis Wagner, *Skipped dues crunch home associations*, USA TODAY (May 26, 2008, 3:00 PM), [http://www.usatoday.com/money/2008-05-26-condo-fees\\_N.htm](http://www.usatoday.com/money/2008-05-26-condo-fees_N.htm) [<http://perma.cc/C3RL-BUY6>].

<sup>50</sup> *Id.*

<sup>51</sup> See Andrea J. Boyack, *Community Collateral Damage: A Question of Priorities*, 43 LOY. U. CHI. L.J. 53, 58–61 (2011) (stating that on a national level at the time the article was written, mortgage delinquency rates were between ten percent and thirteen percent; and explaining that “this precipitous rise in mortgage delinquency corresponds with an even steeper increase in association assessment delinquency ‘which will continue until solvent owners replace delinquent owners’”).

<sup>52</sup> See Aalberts, *supra* note 18, at 327 (“[T]he managers of the CIC’s, are often able to harness significant political allies during times of need. This occurred during the depths of the Great Recession of 2007-2010 when HOA’s successfully lobbied state legislatures in 22 states and the District of Columbia to pass super lien laws.”).

<sup>53</sup> See *Lien Priority for Community Association Assessments*, COMMUNITY ASS’NS INST., <https://www.caionline.org/Advocacy/PublicPolicies/Pages/Lien-Priority-for-Community-Association-Assessments.aspx> [<http://perma.cc/WRE8-YCVN>] (last visited Mar. 1, 2018).

including subordinating the senior liens of other lienholders such as lenders.<sup>54</sup> As the real estate market gradually recovered, lenders in states that adopted super priority statutes began to respond by putting pressure on state legislatures and courts to rebalance lien priority.<sup>55</sup> In a typical association response to this lender pressure, CAI has called upon its “State Legislative Action Committees” to combat the lender attacks on association’s increased lien priorities.<sup>56</sup>

This battle has generated a pro-HOA legislative position and a pro-lender legislative position, each seeking to advance particular interests rather than accomplishing a true balance of the competing interests. This Comment seeks to evaluate existing models to craft a framework from which a blueprint for a better balanced approach might be created.

To facilitate analysis of the issue, this Comment has categorized the various statutory schemes into three basic approaches in regards to HOA lien priority.<sup>57</sup> First, most states still follow a first-in-time approach and have not adopted super lien statutes.<sup>58</sup> Second, there are states that have adopted super lien statutes where an HOA foreclosure extinguishes a lien made junior by the super priority status.<sup>59</sup> Finally, some states have adopted super lien statutes, but first mortgages and deeds of trust are not extinguished.<sup>60</sup> The next Part takes each in turn, analyzing one jurisdiction representing each approach.

## II. THE THREE APPROACHES TO HOA LIEN PRIORITY

This Comment’s comparative analysis will begin by examining how different jurisdictions have attempted to strike a balance between community association and lender interests.

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<sup>54</sup> See Aalberts, *supra* note 18, at 327–29 (“In response to these factors, some states’ lawmakers sought to help HOA’s by passing super lien laws.”).

<sup>55</sup> *Id.* at 328–29.

<sup>56</sup> See *State Advocacy*, *supra* note 17.

<sup>57</sup> See Lewis *supra* note 38, at 1–2. The legislatures of twenty-two states have adopted lien priority statutes that give priority to community association liens making these liens superior to other liens, including mortgages, to some degree. The remainder of the states, which are still the majority, follow a first-in-time approach to determine association lien priority. Florida has adopted a novel approach that deserves further study, and so will be included in the analysis of this Comment. *Id.*

<sup>58</sup> See Boyack & Foster, *supra* note 41, at 244–45. Boyack and Foster explain that most states provide that “a first-mortgage lien on a unit is completely superior in priority to association liens.” *Id.*

<sup>59</sup> See *SFR Investments Pool 1, LLC v. U.S. Bank*, 334 P.3d 408, 419 (Nev. 2014).

<sup>60</sup> See Christian J. Bromley, *Supremacy and Superiority: The Constitution’s Effect on State Lien Priority Statutes*, 44 REAL EST. L.J. 442, 453–55 (2016). Unlike the Nevada regime, the Florida HOA priority does not threaten the mortgagee’s lien with extinguishment and instead “the priority functions as a liability on purchasers, not as a lien competing with mortgages.” *Id.*

California will be examined first as a prototypical first-in-time jurisdiction. Next, Nevada's super lien statute will be analyzed as a representation of a jurisdiction where HOA foreclosure extinguishes a first deed of trust. Finally, this Comment will examine Florida's regime shifting liability for delinquent dues to purchasers as an alternative to both the first-in-time and super lien priority approaches.

### A. First-in-Time Approach to HOA Lien Priority

The original type of regime governing lien priority—first-in-time—will act as our control for evaluating shifts in lien priority. Only after understanding this common law priority system will one understand how and why super lien statutes have shifted the balance in favor of HOAs. Under the common law, the priority of liens was determined by a “first in time, first in right principle.”<sup>61</sup> Today, all United States jurisdictions still follow this rule as a general default, but application of the principle is often modified by a state's recording statute and sometimes a specific law granting priority to certain types of interests.<sup>62</sup> While recording can affect the priority of a mortgage or HOA lien, this Comment focuses on when the general principal of first-in-time, assuming proper recording, is still further modified by statute.<sup>63</sup>

Under a first-in-time regime, a first mortgage or deed of trust usually remains superior to an HOA lien.<sup>64</sup> The reason a first deed of trust is commonly senior to an association's lien is that such instruments are generally prioritized in the order in which they are perfected.<sup>65</sup> Since mortgage loans are usually executed prior to an HOA delinquency being assessed, a mortgage lien in a first-in-time jurisdiction will normally be prior, and thus superior, to an association lien.<sup>66</sup> This temporal principle governs unless there is a statutory exception.<sup>67</sup>

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<sup>61</sup> See JOSEPH WILLIAM SINGER, INTRODUCTION TO PROPERTY 516 (Aspen Law & Business 2001); see also ROBERT G. NATELSON, LAW OF PROPERTY OWNERS ASSOCIATIONS 234–38 (1989).

<sup>62</sup> SINGER, *supra* note 61, at 516–20 (“Recording acts focus on protecting buyers who record first and/or purchase without notice of prior recorded claims. The major types of recording acts are: (1) race, (2) notice, and (3) race-notice. About half the states have notice statutes, and about half the states have race-notice statutes.”).

<sup>63</sup> Geier, *supra* note 30, § 10:1 (“Priority may depend upon which instrument was created executed or recorded first, or it may be affected by other factors, such as . . . specific legal priority accorded to particular interests by law[.]”) This Comment focuses on specific legal priority accorded to the particular interest of an HOA lien in relation to a first deed of trust.

<sup>64</sup> NATELSON, *supra* note 61, at 239.

<sup>65</sup> See Boyack, *supra* note 51, at 93; see also Geier, *supra* note 30, § 10:1.

<sup>66</sup> Geier, *supra* note 30, § 10:1.

<sup>67</sup> *Id.*

Such exceptions are provided for under state law and usually consist of notice under a recording act, agreement of the parties, “the doctrine of equitable subrogation, or specific legal priority accorded to particular interests by law, such as tax liens or other governmental lien interests.”<sup>68</sup> HOA super lien priority statutes fall within the last category. However, unless state law provides a shift in priority, the general principal of first-in-time continues to govern.<sup>69</sup> First-in-time jurisdictions do not have statutes that specifically modify association lien priority, and therefore do not create an HOA exception to the general rule.<sup>70</sup> Most of the jurisdictions in the United States use this type of unmodified first-in-time approach in regards to HOA lien priority.<sup>71</sup>

In most cases, the first-in-time principle is applied in two different ways. Some first-in-time states, including California, have a notice requirement that provides an association must file a notice of delinquency on assessment dues before an HOA lien is perfected.<sup>72</sup> Other states hold that lien perfection relates back to the time the community is formed.<sup>73</sup> The relating back of a lien to community formation would normally make it prior in time to a first mortgage or deed of trust.<sup>74</sup>

However, the superior priority of a first mortgage or deed of trust is usually expressly stated in a relating back jurisdiction’s statute.<sup>75</sup> When a statute does not give direction on the issue, courts in relating back jurisdictions have uniformly held first mortgages and deeds of trusts to be superior to HOA liens in order to support the opportunity for borrowers to obtain credit.<sup>76</sup>

<sup>68</sup> Geier, *supra* note 30, § 10:1; *see also* Boyack, *supra* note 51, at 93.

<sup>69</sup> Boyack, *supra* note 51, at 94 (“In the absence of a statutory directive to the contrary, assessment liens follow the general first-in-time priority rule, and because mortgage loans are typically funded prior to assessment delinquencies, such first mortgage liens are senior to assessment liens.”).

<sup>70</sup> *Id.*

<sup>71</sup> *See* Boyack & Foster, *supra* note 41, at 244–45; *see also* NATELSON, *supra* note 61, at 239.

<sup>72</sup> *See* Boyack & Foster, *supra* note 41, at 245 (“Some states require an association to file a notice of delinquent assessment—which occurs after one perfects the first-mortgage lien—as a prerequisite step to perfecting an association lien.”) (footnote omitted).

<sup>73</sup> *See* Boyack & Foster, *supra* note 41, at 245 n.120. For example, Colorado’s law grants “granting priority over an association lien to ‘[a] security interest on the unit which has priority over all other security interests on the unit and which was recorded before the date on which the assessment sought to be enforced became delinquent.’” *Id.* (quoting COLO. REV. STAT. ANN. § 38-33.3-316 (West 2014)).

<sup>74</sup> Boyack & Foster, *supra* note 41, at 245. Boyack notes that in these jurisdictions “an association’s lien perfects at the time of the CIC’s formation; thus, recording the CIC declaration is the act of perfection.” *Id.*

<sup>75</sup> *Id.* (“Such states’ statutes specifically provide that first-mortgage liens on individual units in a common-interest community take priority over the association lien, even though the association lien relates back to the date of the CIC declaration.”).

<sup>76</sup> *Id.* (“[I]n the few states where statutes are less clear or do not address this point at all, courts have uniformly acknowledged the superior priority of first

Although there are two types of first-in-time approaches, the remainder of this Comment will use California as an exemplar sufficient to understand the larger first-in-time grouping of states for comparative purposes with those that deviate from a first-in-time standard.

California's statute follows the first-in-time principle stating that an association's lien "shall be prior to all other liens recorded subsequent to the notice of delinquent assessment[.]"<sup>77</sup> Such association liens may be secured and foreclosed upon if the assessments are not paid, but only after giving the required period of notice and subsequent recordation of the delinquent assessment.<sup>78</sup> Once the assessment has been recorded, the lien is imposed on the property and has priority from and after that date as against other interests in the property, such as a deed of trust.<sup>79</sup> Even when the association's recorded declaration provides for a present lien relating back to the beginning of the community, the lien is only imposed upon the recordation of the delinquent assessment.<sup>80</sup>

Under California law, the first-in-time principle puts associations at a disadvantage in their ability to collect delinquent member dues. Upon foreclosure of the lien by the association, deeds of trust that were recorded prior to the recording of the delinquent assessment "remain unaffected with their priority intact."<sup>81</sup> Conversely, when a first deed of trust is foreclosed on, it extinguishes all other junior liens which will usually include the association's assessment lien.<sup>82</sup> The buyer of the property at a mortgage foreclosure sale is not personally liable for any delinquent dues owed to the association by the homeowner.<sup>83</sup> Instead, the former homeowner remains personally liable for his unpaid assessments, but this debt is unsecured.<sup>84</sup> This structure creates problems regarding an association's ability to collect, because often a foreclosure sale on the first mortgage will leave no residual to satisfy the association's lien which is extinguished by the sale.<sup>85</sup>

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mortgagees—consistent with the desire to promote the availability of mortgage capital.") (footnote omitted).

<sup>77</sup> CAL. CIV. CODE § 5680 (West 2014).

<sup>78</sup> CAL. CIV. CODE § 5675 (West 2014).

<sup>79</sup> Narayanan & Gower, *supra* note 25, § 28:97.

<sup>80</sup> Thaler v. Household Fin. Corp., 95 Cal. Rptr. 2d 779, 783–85 (Ct. App. 2000).

<sup>81</sup> Narayanan & Gower, *supra* note 25, § 28:96.

<sup>82</sup> *Id.* § 10:1.

<sup>83</sup> CAL. CIV. CODE § 1466 (West 2017).

<sup>84</sup> *Id.*

<sup>85</sup> HYATT, *supra* note 29, at 121.

The dilemma an association faces in a first-in-time regime is illustrated by the result in *Thaler v. Household Finance Corp.* Thaler was a purchaser of a condo at a foreclosure sale pursuant to an HOA lien.<sup>86</sup> A second deed of trust had been recorded prior to the association's lien under which the property was foreclosed.<sup>87</sup> Thaler claimed that his interest was not subject to the second deed of trust even when the association lien was recorded after the deed of trust because the condominium's declaration of CC&Rs provided for a "present lien" (at formation of the community) with a power of sale to secure assessments.<sup>88</sup> While the CC&Rs provided the association lien would be subordinate to a first mortgage or deed of trust, they were silent on the HOA lien's priority in relation to other instruments, including a second deed of trust.<sup>89</sup>

The court in *Thaler* held that, despite the CC&Rs, the second mortgage had priority over the assessment lien which was recorded after the mortgage when the homeowner defaulted on monthly assessments.<sup>90</sup> The court reasoned that though the CC&Rs purported to create a present lien for the collection of assessments, the clear language of the relevant statute provided for a "first in time, first in right" lien priority system.<sup>91</sup> The assessment lien was not perfected until the delinquent assessment was recorded.<sup>92</sup> Therefore, because the second deed of trust was recorded prior to the delinquent assessment, it took priority over the assessment lien.<sup>93</sup> As a matter of law, Thaler bought the property at the association's foreclosure sale subject to the second deed of trust.<sup>94</sup>

As demonstrated in *Thaler*, a mortgage often takes priority over an association lien under California law because the association lien is not perfected until a member defaults on association dues and the delinquent assessment is recorded. Because a mortgage lien is typically placed on a property at the

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<sup>86</sup> *Thaler v. Household Finance Corp.*, 95 Cal. Rptr. 2d 779, 780–81 (Ct. App. 2000).

<sup>87</sup> *Id.*

<sup>88</sup> *Id.* ("Thaler seems to argue that, as a result, the lien for the enforcement of the Homeowners' assessment either sprang from the lien created by the CC & R's (rather than the Assessment Lien), or the Assessment Lien related back to (and derived priority from) the CC & R's. Thaler thus claims that [the second mortgagee] took its interest subject to, and therefore subordinate to, the lien by which Thaler ultimately purchased the property.") *Id.*

<sup>89</sup> *Id.* at 781–82.

<sup>90</sup> *Id.* at 780–81.

<sup>91</sup> *Id.* at 783 ("Such lien shall be prior to all other liens recorded subsequent to the recordation of said notice of assessment.") (emphasis removed).

<sup>92</sup> *Id.* at 783–85.

<sup>93</sup> *Id.*

<sup>94</sup> *Id.* at 784–85.

time of purchase, this will usually be before that purchaser stops paying their HOA dues. This puts associations at a temporal disadvantage in relation to first mortgages that translates into a disadvantage in priority due to the first-in-time principle.

In order to illustrate how the rules of a first-in-time regime determine the possible outcomes for each party, this Part will use two hypothetical situations. The first hypothetical will show what happens when a lender forecloses on the first mortgage lien or deed of trust. The second will reverse the situation with the association initiating foreclosure. We will return to these hypotheticals in Sections II(B) and II(C) to illustrate how each regime shapes the rational decisions of the parties and the logical outcome of those decisions.

Assume the property in question is located in an HOA neighborhood and was purchased just prior to the 2008 recession through a first deed of trust with the lender in the amount of \$885,000. During the recession, the homeowner becomes unemployed and is unable to keep up with both the mortgage payments and association assessments. The homeowner owes \$4500 in association dues. The balance on the mortgage is \$800,000, but the fair market value of the property has plummeted to \$400,000. The homeowner makes a decision to walk away from the underwater property and pay neither the mortgage nor the association assessments.

In our first scenario, the lender chooses to institute foreclosure proceedings before the association. The lender's first deed of trust has seniority over the association lien since the HOA lien is not perfected until the delinquency is recorded. This makes the first deed of trust prior in time and superior to the association lien. The lender is unable to find a buyer to pay more than market value, and the price at the foreclosure sale is \$400,000. The lender's senior lien is satisfied from the proceeds first, and there is nothing left for the association whose junior lien is extinguished during the sale.

Assume for the second hypothetical that instead of promptly initiating foreclosure, the lender delays initiation in order to see if the market makes a recovery and to avoid paying HOA dues if it decides to purchase the property. During this period of delay, no one is paying association dues on the property. The association waits for the lender to act for months, but finally decides they can wait no more. The association initiates foreclosure before the lender. Because the lender's lien is senior to the association's, the buyer at the foreclosure sale must take title subject to the lender's \$800,000 mortgage lien on the property. This makes it extremely difficult to find a buyer when

the market value of the property is worth half of the mortgage lien on the property. Unable to find a buyer, the association is forced to internalize the debt and passes the cost along to its remaining members with higher dues and special assessments.

Between an association and a lender, the first-in-time approach appears to heavily favor the lender's interests. As long as the loan is made prior to a homeowner ceasing to pay association assessments, a lender's lien will usually be senior to an HOA lien.<sup>95</sup> This seniority provides a lender with security in its interest. When a lender forecloses, its lien will be satisfied by the proceeds first, and the association will only be paid if there is a surplus. Furthermore, the lender need not fear that an HOA foreclosure will extinguish its interest because a lender's senior lien will survive an association's foreclosure.<sup>96</sup>

In contrast, the first-in-time approach puts community associations at a significant disadvantage. When a homeowner is in substantial debt for delinquent assessments, foreclosure is the more secure of the methods of recovery for an HOA.<sup>97</sup> However, since both associations and lender-mortgagees hold liens on specific properties, these two groups are inherently in competition with one another when the sale proceeds cannot satisfy payment on both obligations.<sup>98</sup> Under the California first-in-time approach, a lender's first deed of trust will almost always have priority over an association's lien because the statute bases the priority assessment of the HOA's lien off of the time the delinquent assessment is recorded.<sup>99</sup>

A California-type regime will continue to have the same kinds of problems identified during the Great Recession that motivated adoption of HOA super lien priority statutes. Associations under these first-in-time statutes will continue to struggle to collect deficient assessments during dips in the real estate market when association liens are extinguished by lender foreclosure with few viable alternative remedies for collection available.<sup>100</sup> The issue of collection is compounded when lenders

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<sup>95</sup> CAL. CIV. CODE § 5680 (West 2014).

<sup>96</sup> *Thaler*, 95 Cal. Rptr. 2d at 780–81. While a lender may not need to fear extinguishment of their lien under these circumstances, they do have a concern that association foreclosure will affect the market value of the property. This may have an adverse effect on their ability to maximize their return upon a foreclosure sale on the mortgage lien. See Courtney Newsom, Note, *No Free Ride: An Equitable Remedy to Protect Homeowners' Associations from Delayed Foreclosures*, 46 LOY. L.A. L. REV. 361, 363–64 (2012).

<sup>97</sup> See Bromley, *supra* note 22, at 257.

<sup>98</sup> *Id.*

<sup>99</sup> CAL. CIV. CODE § 5680 (West 2014).

<sup>100</sup> See Bromley, *supra* note 22, at 258; see also Boyack, *supra* note 51, at 78.

become reluctant to expedite foreclosure for financial reasons.<sup>101</sup> Without foreclosure sales being completed, new owners who could pay dues and provide income to the association are not taking title to the zombie property.<sup>102</sup>

Lenders operating inside the rules of a first-in-time jurisdiction have little motivation to expedite foreclosure proceedings<sup>103</sup> because lenders' liens have almost guaranteed priority under this approach.<sup>104</sup> A lender's senior interest is not substantially threatened—such as when the interest could be extinguished—by HOA foreclosure, so a lender is not under sufficient pressure from the association to quickly foreclose on a property.<sup>105</sup> Furthermore, a lender has little internal incentive to foreclose quickly in a declining real estate market. Under such conditions, the market value of the property is likely to be much less than the value of the mortgage loan.<sup>106</sup> To maximize the return on their lien, lenders often prefer to wait and see if the market makes a recovery before foreclosing on a property.<sup>107</sup> In addition, if the lender plans to be the purchaser at the foreclosure sale, taking title to the property would lead to the lender having to pay regular HOA assessments.<sup>108</sup> Most lenders would prefer to avoid this additional cost if they are able, and a

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<sup>101</sup> Newsom, *supra* note 96, at 367. Newsom explains that “[b]anks are able to take a free ride—and cause additional hardship for homeowners in an HOA—because of the combination of laws governing California HOAs and lien prioritization.” *Id.* The “free ride” she refers to is the ability of a lender to delay foreclosure in hopes the housing market will recover, allow maximization of the return on their lien during foreclosure, and avoid paying the additional cost of association dues.

<sup>102</sup> *Id.*

<sup>103</sup> *Id.* at 361 (“[A] bank will often delay foreclosure, sometimes months or even years, when the property is part of a homeowner’s association since the association must continue to insure and maintain the property regardless of whether the bank or the homeowner makes any contribution to the association.”).

<sup>104</sup> *Id.* at 373–78. Newsom explains that in California, a lien is not perfected until recorded after meeting the notice requirements of the statute. This will almost always make an association lien subsequent and junior to a first mortgage since the first mortgage is perfected at the purchase of the property. *Id.*

<sup>105</sup> *Id.* at 378 (“Without laws to the contrary, the lender is free to take advantage of the HOA because there is no incentive for the bank to foreclose or pay its fair share of HOA expenses.”) (footnote omitted).

<sup>106</sup> Joint Editorial Board for Uniform Real Property Acts, *Distribution of JEB Report on Common Interest Assessment Lien Priority*, UNIFORM LAW COMMISSION (Aug. 22, 2013), [http://www.uniformlaws.org/shared/docs/jeburpa/2013aug22\\_JEBURPA\\_UCIOA%20Lien%20Priority\\_Request%20for%20Comments.pdf](http://www.uniformlaws.org/shared/docs/jeburpa/2013aug22_JEBURPA_UCIOA%20Lien%20Priority_Request%20for%20Comments.pdf) [<http://perma.cc/M3LB-5FB5>] [hereinafter *JEB Report*].

<sup>107</sup> See Newsom, *supra* note 96, at 377 (“Delaying foreclosures allows lenders to control the number of homes on the market and potentially prevent continued drops in value marketwide, keep the loan on the performing side of the balance sheet, and avoid ownership costs.”) (footnotes omitted).

<sup>108</sup> *Id.*

first-in-time regime offers lenders such an opportunity by allowing them to simply forestall foreclosure on their lien.<sup>109</sup>

During economic recessions, ineffective collection methods and lack of paying members lead to HOAs not being able to fulfill their core functions of neighborhood maintenance.<sup>110</sup> The lack of neighborhood care and upkeep then contributes to the continued drop in the market value of member properties.<sup>111</sup> If HOAs are unable to collect dues by foreclosure or other means of collection, they are often forced to increase their dues to other members in order to continue operating.<sup>112</sup> As noted in the Miller and Starr treatise, “[t]here is a strong public policy in favor of the levying and enforcement of assessments in a common interest development as an economic necessity for the proper functioning of the development.”<sup>113</sup> This public policy interest is so strong that the California legislature granted regular assessments of housing associations an exemption from the claims of creditors to the extent necessary for the association to perform its obligation to provide essential services.<sup>114</sup>

However, as illustrated by the above discussion, the California legislature seems to have overlooked the obstacles associations must contend with when collecting assessments if their liens must compete with other senior liens such as a first deed of trust. Exemption from creditor claims for assessments is not a significant advantage when the association cannot collect sufficient assessments.

The difficulties associations face in the collection of assessments under the constraints of a first-in-time regime are the catalyst of UCIOA-type super lien priority statutes, which endeavor to resolve the problem. The next Section will discuss Nevada’s attempt to address this issue by its super lien priority statute and judicial interpretation that an HOA lien has true priority over a first mortgage.

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<sup>109</sup> *Id.*

<sup>110</sup> *JEB Report*, *supra* note 106. The report explains that during delays in foreclosure, “neither the defaulting unit owners nor the first mortgagee typically pay the assessments on the unit” because under a first-in-time regime, “the mortgagee does not become legally liable to pay assessments on the unit unless and until the mortgagee acquires title to the unit via a foreclosure sale or deed in lieu of foreclosure.” *Id.* at 2.

<sup>111</sup> *See* Collins, *supra* note 4.

<sup>112</sup> Newsom, *supra* note 96, at 361. An HOA in a first-in-time jurisdiction often has little recourse other than to increase dues of paying members because “[t]he bank is able to shed its financial obligation at the expense of the property’s innocent neighbors.” *Id.*

<sup>113</sup> Narayanan & Gower, *supra* note 25, § 28:93 (footnote omitted).

<sup>114</sup> *Id.* (“Regular assessments imposed on or collected from unit owners are exempt from execution by the association’s judgment creditors to the extent necessary for the association to perform its obligations under the governing documents as required by law.”).

## B. True Priority Super Lien Priority Statutes

In order to address the issues encountered by HOAs in collecting delinquent dues in a first-in-time jurisdiction, a minority of states, including Nevada, have taken the position that an HOA foreclosure on its lien extinguishes the interests of “all other liens and encumbrances,” including a first mortgage or deed of trust.<sup>115</sup> As previously mentioned, the laws of twenty-two states alter the general first-in-time rule of priority by giving HOA liens a “super priority” status.<sup>116</sup> The specific priority differs by state, with legislatures having adopted different generations of uniform codes and model statutes.<sup>117</sup> While several jurisdictions have held that a first deed of trust may be extinguished under its super lien priority statute,<sup>118</sup> this Comment uses only Nevada’s statute and case law as its focal point of discussion and as an example to understand generally the direction chosen by states that fit into the super lien category.<sup>119</sup>

To understand the nature of the issues, it is helpful to begin with a brief summary of the history of Nevada’s super lien statute. Super lien priority statutes arose in response to the issue of HOA inability to collect delinquent assessments under a traditional first-in-time type regime.<sup>120</sup> The Uniform Law Commission promulgated uniform model community association

<sup>115</sup> NEV. REV. STAT. § 116.3116(2) (West 2015).

<sup>116</sup> See Lewis, *supra* note 38, at 1 (“The laws of twenty-two (22) jurisdictions contain provisions that afford a so-called ‘super-priority’ to the liens available to condominium associations and/or community associations, making such liens superior to the liens of mortgage loans and other types of liens, to some varying extent.”).

<sup>117</sup> See Boyack & Foster, *supra* note 41, at 244–45. Boyack and Foster explain that “[t]hese acts vary widely in how they address buyers’ liability and association-lien priority” and “[t]he statutory divide among states is traceable largely to the historical development of their condominium regimes.” *Id.* at 246. This historical development is mainly from “four foundational condominium-ownership statutes: (a) the Puerto Rican Horizontal Property Act; (b) the Federal Housing Administration’s (FHA) Model Statute for the Creation of Apartment Ownership; (c) the Uniform Condominium Act (UCA); and (d) the Uniform Common Interest Ownership Act (UCIOA).” *Id.* at 246–47.

<sup>118</sup> See Chase Plaza Condo. Ass’n, Inc. v. JPMorgan Chase Bank, 98 A.3d 166, 178 (D.C. 2014); see also Summerhill Village Homeowners Ass’n v. Roughley, 289 P.3d 645, 646 (Wash. Ct. App. 2012).

<sup>119</sup> *HOA Foreclosures Leave Banks Empty Handed*, *supra* note 3. Nevada’s statute and case law are both at the forefront of the debate and may have “implications nationwide.” *Id.*

<sup>120</sup> Vaughn, *supra* note 3, at 10. Vaughn explains:

In response to an increase in HOAs, and a desire to help HOAs collect debt more efficiently, the Uniform Law Commission (“ULC”) developed the Uniform Condominium Act (“UCA”) . . . . Under the UCA, HOAs were granted some measure of lien priority against mortgages. . . . Subsequent acts, the Uniform Common Interest Ownership Act (“UCIOA”) and the Uniform Planned Community Act (“UPCA”), were passed in 1982 and all contained language granting HOAs super-priority status.

*Id.*

statutes such as the UCA, the UCIOA, and the UPCA, all of which included an HOA lien priority (for six months of delinquent assessments) over a first mortgage or deed of trust.<sup>121</sup> The original comments to the UCIOA stated the purpose of the HOA super lien priority as follows:

[T]he six months' priority for the assessment lien strikes an equitable balance between the need to enforce collection of unpaid assessments and the obvious necessity for protecting the priority of the security interests of lenders. As a practical matter, secured lenders will most likely pay the six months' assessments demanded by the association rather than having the association foreclose on the unit.<sup>122</sup>

The comments underscore the Uniform Law Commission's intent that the burden of paying for a delinquent homeowner's assessment be shifted to the lender who has substantially more assets, and therefore, may bear the burden more easily than an HOA.<sup>123</sup> However, most courts have interpreted the original language of UCIOA section 3-116 to suggest that an HOA lien should not have a true lien priority (which would extinguish a first mortgage), but rather a "limited priority lien" affording only a payment priority.<sup>124</sup> Such a scheme provides the priority position of the HOA lien is split with six months of unpaid assessments taking priority over a first mortgage, and the remaining assessment deficit staying subordinate to the first mortgage.<sup>125</sup> This "six-month capped 'super priority' portion" of an HOA lien is not accorded true priority in the original UCIOA because this portion cannot be foreclosed on by the association as senior to a first mortgage or deed of trust.<sup>126</sup> Instead, such a limited priority lien offers priority in payment upon foreclosure by the lender.<sup>127</sup>

In 1991, the Nevada state legislature adopted a modified version of the UCIOA.<sup>128</sup> The Nevada Uniform Common Interest

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<sup>121</sup> *See id.*

<sup>122</sup> UNIFORM COMMON INTEREST OWNERSHIP ACT § 3-116 cmt. 2 (2008) (amended 2014) (note that this language has since been removed) [hereinafter UCIOA § 3-116].

<sup>123</sup> *See Vaughn, supra* note 3, at 10–11. ("The Comments essentially suggests [sic] that because mortgage lenders have more money than HOAs, they should be responsible for the delinquent dues that stem from a common debtor.")

<sup>124</sup> *See Boyack, supra* note 51, at 98–99. Boyack explains the position of most states with super lien priority statutes is "[t]he six-month capped 'super priority' portion of the association lien does not have a true priority status under UCIOA since this six-month assessment lien cannot be foreclosed as senior to a mortgage lien." *Id.*

<sup>125</sup> *Id.* at 99 n.216.

<sup>126</sup> *Id.* at 99.

<sup>127</sup> *Id.* ("Rather, it either creates a *payment* priority for some portion of unpaid assessments, which would take the first position in the foreclosure repayment 'waterfall,' or grants *durability* to some portion of unpaid assessments, allowing the security for such debt to survive foreclosure.") (footnotes omitted).

<sup>128</sup> Gloeckner, *supra* note 48, at 329.

Ownership Act was enacted as NRS Chapter 116, and it included an HOA super lien priority statute.<sup>129</sup> In Nevada, NRS section 116.3116 governs HOA liens and is substantially similar to section 3-116 of the UCIOA.<sup>130</sup> The relevant parts of NRS section 116.3116 state the following:

A lien under this section is prior to all other liens and encumbrances on a unit except: . . . (b) A first security interest on the unit recorded before the date on which the assessment sought to be enforced became delinquent or, in a cooperative, the first security interest encumbering only the unit's owner's interest and perfected before the date on which the assessment sought to be enforced became delinquent, except that a lien under this section is prior to a security interest described in this paragraph to the extent set forth in subsection 3.<sup>131</sup>

This section of the statute provides that an association lien is superior to all other liens on a property with the exception of a first mortgage or deed of trust recorded prior to the recordation of the delinquent assessment. The priority provided to the HOA lien up to this point in the statute is the same as in a common law first-in-time jurisdiction. However, the following section alters the priority of the association lien:

A lien under this section is prior to all security interests described in paragraph (b) of subsection 2 to the extent of: (a) Any charges incurred by the association on a unit pursuant to NRS 116.310312; (b) The unpaid amount of assessments, not to exceed an amount equal to assessments for common expenses based on the periodic budget adopted by the association pursuant to NRS 116.3115 which would have become due in the absence of acceleration during the 9 months immediately preceding the date on which the notice of default and election to sell is recorded.<sup>132</sup>

According to the plain language of the statute, as drafted by the Nevada legislature, this section provides that nine months of the HOA lien's assessments will take priority over a first mortgage or deed of trust.<sup>133</sup> In the event of a foreclosure sale by the lender, the amount for nine month's assessments will be considered senior to a first deed of trust, and the association may collect this amount from the proceeds of the sale before the lender receives their portion.<sup>134</sup> However, there remained an

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<sup>129</sup> *Id.* ("The section of the statute relevant to the HOA foreclosure issue is NRS 116.3116, which is almost identical to section 3-116 of the UCIOA; this section governs liens against units for assessments.")

<sup>130</sup> *Id.*

<sup>131</sup> NEV. REV. STAT. ANN. § 116.3116(2) (West 2015).

<sup>132</sup> *Id.* § 116.3116(3).

<sup>133</sup> Gloeckner, *supra* note 48, at 330 ("Thus, a portion of the HOA's lien—limited to nine months of unpaid assessments preceding the lien—is given priority over the bank's first mortgage, creating a 'super-priority' status.")

<sup>134</sup> *Id.* ("In this case, the HOA's lien is considered 'senior' to the bank's first deed of

ambiguity in the statute regarding whether an HOA's foreclosure on its lien automatically extinguishes all prior liens on the property made junior by this super priority status.<sup>135</sup> In 2014, the Nevada Supreme Court resolved this ambiguity.<sup>136</sup>

In *SFR Investments*, the Nevada Supreme Court interpreted the NRS section 116.3116 priority to be a true lien priority, rather than just a limited payment priority as previously discussed.<sup>137</sup> Relying on the statute's plain language that an association lien is "prior to all other liens and encumbrances," the court held that an association lien held absolute priority to a first mortgage or deed of trust recorded before the delinquent assessment.<sup>138</sup> The court reasoned that the statute splits an association's lien into a "superpriority piece" of nine months of assessments senior to a first deed of trust and a "subpriority piece" remaining subordinate to the first deed of trust.<sup>139</sup> The court interpreted the language of the statute to mean that the HOA super priority piece was prior to, and therefore senior to, first security interests.<sup>140</sup>

The court used the comments to UCIOA section 3-116 to interpret the statute's ambiguity.<sup>141</sup> The comments stated "lenders will most likely pay the . . . assessments demanded by the association rather than having the association [foreclose] on the unit."<sup>142</sup> The court reasoned that if the super priority piece only established payment priority, this reference to the lender paying off the super priority piece to avoid foreclosure "would make no sense."<sup>143</sup> The court's interpretation in *SFR Investments* means that with both the statutory priority of an HOA lien being higher than a first mortgage and an association's ability to invoke non-judicial foreclosure, an HOA lien can completely extinguish a mortgage or first deed of trust on the foreclosed property.<sup>144</sup>

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trust, which is often referred to as a 'junior' security interest, even though the HOA lien was asserted subsequently in time.").

<sup>135</sup> *Id.* at 332 ("The ambiguity pertains to whether a foreclosure sale, properly conducted pursuant to NRS Chapter 116, automatically extinguishes all prior encumbrances on the property, thereby allowing a bona fide purchaser at an HOA foreclosure sale to obtain the property free and clear of all prior encumbrances.").

<sup>136</sup> *See SFR Invs. Pool 1, LLC v. U.S. Bank*, 334 P.3d 408 (Nev. 2014).

<sup>137</sup> *See Bromley*, *supra* note 60, at 453; *see also SFR Invs.*, 334 P.3d at 409.

<sup>138</sup> *SFR Invs.*, 334 P.3d at 409 (quoting NEV. REV. STAT. § 116.3116(2) (West 2015)).

<sup>139</sup> *Id.* at 411.

<sup>140</sup> *Id.* at 412.

<sup>141</sup> *Id.*

<sup>142</sup> *Id.* at 413 (quoting UNIFORM COMMON INTEREST OWNERSHIP ACT § 3-116 cmt. 1 (1982); UNIFORM COMMON INTEREST OWNERSHIP ACT § 3-116 cmt. 2 (1994); UCIOA § 3-116 cmt. 2 (emphasis omitted)).

<sup>143</sup> *Id.*

<sup>144</sup> *See Bromley*, *supra* note 60, at 453; *see also SFR Invs.*, 334 P.3d at 409.

To illustrate how a Nevada type regime works in contrast to a first-in-time jurisdiction, let us return to the hypothetical found in Section II(A) and apply the Nevada rules to the situation. Recall that the property in question is located in an HOA neighborhood and was purchased just before the Great Recession through a first deed of trust for \$885,000. The homeowner is unable to keep up with both the mortgage payments and association assessments, which accrue to \$4500. The balance on the mortgage is \$800,000, but the fair market value of the property has plummeted to \$400,000. The homeowner makes a decision to walk away from the underwater property and pay neither the mortgage nor the association assessments.

Assume for our first scenario that the lender initiates foreclosure first. The association's super priority amount for nine months of assessments is afforded super priority status under the statute. Assume that assessments for nine months in the community equal \$1800, which is the super priority amount under the statute. The lender sells the property for \$400,000, and the senior super priority amount of \$1800 must be paid before the first mortgage is satisfied. The HOA receives \$1800 from the proceeds while the lender gets \$398,200 from the foreclosure sale.

For the second scenario, assume that the lender decides not to foreclose in hopes of market recovery and to avoid paying HOA dues if it decides to purchase the property. During this period of delay, no one is paying association dues on the property. However, unlike in a first-in-time jurisdiction, the association has an ace up their sleeve under a Nevada type regime. The association can initiate foreclosure under their lien and the super priority amount of the lien is made senior to the first mortgage by statute. Because this portion is senior and given true lien priority, a foreclosure upon this senior portion of the lien will extinguish the first mortgage. As required by statute, the association provides notice to the lender of the impending foreclosure. The lender is allowed to pay off the \$1800 super priority amount and save its interest on the property from extinguishment. But if the lender does not pay this amount before the association forecloses, the lender's lien for \$800,000 will be extinguished. Furthermore, because the amount of the assessments is only \$4500 and the \$800,000 mortgage is extinguished, it is very likely that the association will find a buyer. Since the association can only satisfy \$4500 worth of dues, it is likely the association would sell the property for an amount around \$5000. It would then send a check for the surplus of the proceeds to the lender for \$500.

Essentially, the court took what was supposed to be a limited payment priority under the UCIOA and instead held that it was a true lien priority capable of extinguishing other junior interests in the property.<sup>145</sup> Under the original UCIOA as adopted by Nevada, the association's lien was given limited protection during a lender's foreclosure sale by allowing the HOA to collect six months' worth of assessments from the proceeds before the lender could satisfy its own lien. But the limited priority given to association liens upon lender foreclosure did not solve the problem of lender delay in initiating foreclosure found in first-in-time jurisdictions. Lender delay continued to be a problem because the lender did not have adequate motivation to foreclose. A lender's lien retained true priority over an HOA lien and certainly was not in danger of being extinguished.

The Nevada Supreme Court tackled this issue with the nuclear solution of giving the super priority piece of the association lien true priority over other liens made junior by the statutory priority.<sup>146</sup> Because the super priority piece of nine months of assessments held true priority over a first mortgage, an association can now foreclose on the super priority piece and extinguish a first mortgage. Under such a scheme, lenders must act to either initiate foreclosure or pay off the association lien if they wish to preserve their substantial interest in the property.

The result of this interpretation of Nevada's super lien priority statute is that it essentially takes away the lender's advantage afforded in a first-in-time jurisdiction and gives it to the HOA.<sup>147</sup> Under the Nevada-style regime, associations are almost guaranteed to be able to collect their unpaid dues.<sup>148</sup> This can be done either: (1) from the proceeds of a foreclosure action by the lender since the HOA lien is senior to a mortgagee's, (2) direct foreclosure by the HOA on its lien because it has priority, or (3) a buyout of the association lien by the lender who is forced to pay the assessment to avoid extinguishment of the mortgage lien by an HOA initiated foreclosure.

While this scheme essentially solves association problems found in a first-in-time jurisdiction, the result appears to be significantly unfair to the lender whose substantial interest in

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<sup>145</sup> *SFR Inv.*, 334 P.3d at 409.

<sup>146</sup> *Id.*

<sup>147</sup> See Bromley, *supra* note 60, at 453.

<sup>148</sup> See Aalberts, *supra* note 18, at 328 ("With super liens an association can actually collect even if the property's value is greatly underwater to the amount owed on the mortgage; this is in contrast to states without super lien laws where the lack of equity makes it generally impossible to collect.").

the property can be extinguished.<sup>149</sup> The result is unfair because a lender's security interest on a property will generally be for an amount far greater than a few months of delinquent assessments.<sup>150</sup> The ability of an HOA to wipe out a security interest on a million dollar loan for a few thousand dollars worth of dues is disproportionate and does not give the impression of being fair and equitable.<sup>151</sup> This interpretation is arguably not in accordance with the equity originally intended by the UCIOA drafters, and grants far too much of the balance of power to associations.<sup>152</sup>

Despite the perceived failings at achieving a true balance, super lien priority statutes do not appear to be in danger of disappearing in the near future absent lenders' successful lobbying of state legislatures. In 2014, the Uniform Law Commission updated the UCIOA to reflect the recent court holdings granting the super priority lien true priority status.<sup>153</sup> In fact, against prior judicial interpretation of UCIOA section 3-116 holding that the section merely provides a payment priority, the Commissioners state that the original UCIOA intended a true lien priority capable of extinguishing junior interests.<sup>154</sup> However, the UCIOA comments to section 3-116 also state that the equitable balance between associations and lenders contemplated by the uniform code was premised on the assumptions that lenders would foreclose quickly, and a sufficient return existed on the foreclosure sale to satisfy both liens.<sup>155</sup> The comments go on to explain that this situation did not exist during the foreclosure crisis, and the language of the statute created an interpretive dispute as to

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<sup>149</sup> *Lenders' Mortgage Liens at Risk of Being Extinguished by Condo and Homeowners' Association "Super-Priority" Liens*, GOODWIN PROCTOR LLP (Sept. 27, 2014), <https://www.goodwinlaw.com/publications/2014/09/lenders-mortgage-liens-at-risk-of-being-extinguish> [hereinafter *Goodwin Mortgage Liens*].

<sup>150</sup> *HOA Foreclosures Leave Banks Empty Handed*, *supra* note 3.

<sup>151</sup> See Gardberg, *supra* note 3, at 13.

<sup>152</sup> Bromley, *supra* note 60, at 453 ("This result lacks any of the equitable balance intended by the UCIOA drafters and alternately affords the association exactly what the UCIOA and the Nevada statute intended to avoid: absolute priority status of a mortgagee at the expense of unpaid associations.").

<sup>153</sup> UCIOA § 3-116 cmt. 2 ("First, subsection (a) affirms the result in *Summerhill Village Homeowners Ass'n v. Roughley*, . . . and makes clear that the association's lien has true priority over the lien of an otherwise first mortgage lender to the extent of the amount specified in subsection (c). Thus, if the association conducts a foreclosure sale of its association lien and the otherwise first mortgagee does not act to redeem its interest by satisfying the association's limited priority lien, the mortgagee's lien would be extinguished.").

<sup>154</sup> *Id.* ("As originally promulgated in 1982, subsection (c) provided that the association's lien did have priority to the extent of six months of unpaid common expense assessments, based on the association's periodic budget.").

<sup>155</sup> *Id.*

whether the super priority lien should be a true lien priority or a payment priority.<sup>156</sup>

The Uniform Law Commission resolved this ambiguity in the UCIOA by changing the language of section 3-116(b)(3) to include: “[a]ny priority accorded to the association’s lien under this section is a priority in right and not merely a priority to payment from the proceeds of the sale of the unit by a competing lienholder or encumbrancer.”<sup>157</sup> With this amendment to the UCIOA, it is now clear that the Uniform Law Commission intends that the priority provided to an association lien under section 3-116 is intended to be a true priority. What is left to be seen is whether the remaining states that adopted section 3-116 will agree with the Commissioners’ intent and adopt true lien priority for their super priority statutes.

Though Nevada and the Uniform Law Commission have essentially solved the problems encountered by associations in first-in-time jurisdictions, serious issues remain with true priority super lien priority statutes. While a first-in-time jurisdiction gives lenders a significant advantage, super lien priority statutes holding foreclosure on an HOA lien extinguishes a first deed of trust shift the balance completely to community associations.

Both approaches result in significant disadvantages to whichever party is not favored under the law. Each approach grants priority to parties on opposite ends of the association-lender spectrum. Either may be considered a valid approach if it is determined that either the lender or the association should hold priority in a competitive zero-sum game. However, it may be more fair to the parties involved to aspire to achieve a more balanced lien priority scheme. The next Section will examine an approach that falls somewhere in between these two polar extremes.

### C. The Purchaser Liability Approach

Some jurisdictions have sought to craft a solution to the perceived imbalances created in the groups described in Sections II(A) and II(B) above. While the first-in-time approach greatly favors the lender, super lien priority jurisdictions with true lien priority provisions shift the advantage to associations. Florida takes an approach somewhere between the two. This Section begins with an overview of the Florida scheme and the context in

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<sup>156</sup> *Id.* at 189–90.

<sup>157</sup> UCIOA § 3-116.

which it developed, followed by an analysis of the legal structure set forth in Florida's approach to balancing competing lien interests.

Florida was one of the states hit hardest during the Great Recession, which began with the foreclosure crisis in 2008.<sup>158</sup> By March 2010, sixty percent of Florida CICs were reporting that at least half of their units or parcels were two months or more behind in paying their assessments.<sup>159</sup> Homeowners that did pay their dues were paying for the upkeep of sometimes dozens of empty homes in the process of foreclosure in their neighborhoods.<sup>160</sup> One community association attorney likened the situation to "getting stuck with the bar tab of a roomful of people you have never met."<sup>161</sup> As a result, CICs had to increase assessments and were sometimes unable to provide the maintenance and services they were obligated to perform, which further depreciated the neighborhood's property values.<sup>162</sup> Florida required an innovative solution to its foreclosure problem.

Under Florida common law, the general rule governing lien priority is unsurprisingly "first in time is first in right," absent statutory regulation otherwise.<sup>163</sup> Florida's recording statute makes it a notice jurisdiction, and the holder of a lien must record in order to preserve his lien's priority against subsequent purchasers, creditors, and other lien holders.<sup>164</sup> Under Florida's statute, both condominium and homeowners association liens are

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<sup>158</sup> See Daniel Goldmintz, Note, *Lien Priorities: The Defects of Limiting the "Super Priority" for Common Interest Communities*, 33 CARDOZO L. REV. 267, 282–83 (2011).

<sup>159</sup> Rachael Lee Coleman, *Desperate condo, homeowner associations thrown a lifeline*, MIAMI HERALD (Mar. 7, 2010), [https://www.miamiforeclosurelawyerblog.com/files/2015/07/Desperate-condo-homeowner-associations-thrown-a-lifeline-03\\_07\\_2010-MiamiHerald.com\\_.pdf](https://www.miamiforeclosurelawyerblog.com/files/2015/07/Desperate-condo-homeowner-associations-thrown-a-lifeline-03_07_2010-MiamiHerald.com_.pdf) [<http://perma.cc/H8WN-VN8M>].

<sup>160</sup> Rich McKay, *Empty Homes Mean Others Pick Up Tab*, ORLANDO SENTINEL (Jan. 24, 2010), [http://articles.orlandosentinel.com/2010-01-24/news/1001230144\\_1\\_dues-town-homes-housing-market](http://articles.orlandosentinel.com/2010-01-24/news/1001230144_1_dues-town-homes-housing-market) [<http://perma.cc/ED8L-KHRT>].

<sup>161</sup> *Id.*

<sup>162</sup> Boyack, *supra* note 51, at 78. Boyack provides the following example:

Parkview Point Condominium in Miami Beach suffered a large enough loss of assessment revenue that it was unable to pay water bills for the building, and the unit owners nearly had their water cut off before solvent owners were able to raise funds to pay the arrearage. The lobby ceiling repairs, however, were stopped mid-repair, leaving wiring and ducts exposed.

*Id.*

<sup>163</sup> 34 FLA. JUR. 2D § 34 (2017). In other words, "the general rule is thus that liens shall take precedence in the order of their creation unless the one prior in time is extrinsically defective or is destroyed by some act of the holder." *Id.*

<sup>164</sup> THOMAS E. BAYNES, JR., FLORIDA MORTGAGES § 9-1 (2016).

effective from, and relate back to the recording of the original declaration establishing the CIC.<sup>165</sup>

In accordance with Florida's recording statute, the original declaration of the community is said to provide notice to other potential interest holders so long as the declaration provides that the CIC lien will have a higher priority than other liens.<sup>166</sup> However, the Florida statutory scheme makes an exception for first mortgages, which are given an expressly prescribed priority higher than an association lien.<sup>167</sup> Therefore, in relation to a first mortgage, the association lien becomes effective once the claim of lien is recorded in the county public records.<sup>168</sup> Because only junior liens are extinguished in a foreclosure action, this means that a foreclosure action by a CIC, on its lien, will usually not extinguish a first mortgage since a first mortgage will normally be senior to a CIC lien.<sup>169</sup>

In 1992, Florida altered association lien priority by its partial adoption of the UCIOA super lien priority statute which grants association liens a six-month limited payment priority.<sup>170</sup> However, the priority granted under this statute does not work in the traditional sense prescribed by the UCIOA which required an association lien to compete with other liens, including a first mortgage.<sup>171</sup> Instead, the Florida statute allows an association's lien to bypass direct competition with a first mortgage because the foreclosure sale purchaser is held jointly and severally liable with the former homeowner for unpaid association assessments.<sup>172</sup> At an HOA foreclosure sale, a purchaser is often the lender because a lender will usually prefer to purchase the property itself rather than dealing with an unknown third party. But regardless of whether the purchaser is the lender or a third party, the association recovers directly from that purchaser

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<sup>165</sup> See THE FLA. BAR, FLORIDA REAL PROPERTY LITIGATION § 5.40 (8th ed. 2016); Homeowner's Association Act, FLA. STAT. § 720.3085 (2017); Condominium Act, FLA. STAT. § 718.116 (2017).

<sup>166</sup> THE FLA. BAR, *supra* note 165, § 5.272; see also Coral Lakes Cmty. Ass'n, Inc. v. Busey Bank, 30 So. 3d 579, 584–85 (Fla. Dist. Ct. App. 2010).

<sup>167</sup> THE FLA. BAR, *supra* note 165, § 5.628; FLA. STAT. § 720.3085; FLA. STAT. § 718.116.

<sup>168</sup> FLA. STAT. § 720.3085; FLA. STAT. § 718.116.

<sup>169</sup> POWELL, *supra* note 23, § 37.41.

<sup>170</sup> See Bromley, *supra* note 22, at 284–85; see also 1992 Fla. Laws. ch. 92-49, at 444.

<sup>171</sup> UCIOA § 3-116 cmt. 2.

<sup>172</sup> See Boyack & Foster, *supra* note 41, at 258–59. Boyack and Foster note that Florida's approach is unique because it “impos[es] joint and several liability on any foreclosure purchaser for past-due assessments of the previous owner but limit[s] such liability in the case of a first-priority lender to the amount of the CIC super-priority lien.” *Id.*

rather than collecting their super priority against the foreclosing mortgagee's sale proceeds.<sup>173</sup>

Both Florida and some other states have taken a purchaser liability approach, but only Florida applies it to a holder of a first mortgage's purchase of the property at an association's foreclosure sale.<sup>174</sup> However, the Florida statute still limits a lender-purchaser's liability.<sup>175</sup> While the lender is liable for the previous owner's past due assessments upon purchase at the foreclosure sale, the Florida statute imposes a statutory cap on the lender's liability.<sup>176</sup> This statutory cap is restricted to the amount of the CIC's super priority lien.<sup>177</sup> Originally, the maximum under the Florida super priority lien statute was six months of delinquent assessments prior to the foreclosure purchase.<sup>178</sup>

During the housing crisis beginning in 2008, foreclosure timelines became longer as more and more property foreclosures inundated the judiciary.<sup>179</sup> These timelines were especially a problem in states such as Florida that required judicial foreclosure, since judicial foreclosure typically involves longer wait times due to required judicial oversight of the foreclosure process.<sup>180</sup> In 2010, the Florida legislature passed an amendment to their super lien priority statute increasing associations' super priority from the six months of delinquent assessments to twelve months or one percent of the amount of the foreclosing mortgage.<sup>181</sup> Therefore, the lender-purchaser's super lien liability is now currently restricted to the lesser of either (1) twelve months of delinquent assessments proceeding the purchase, or (2) one percent of the original mortgage debt on the property.<sup>182</sup>

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<sup>173</sup> Bromley, *supra* note 60, at 454–55 (“Florida’s limited priority is provided through the statutory liability of a foreclosure sale purchaser. The statute allows a mortgagee to foreclose its interest and imposes liability for the priority amount on that mortgagee as a foreclosure sale purchaser.”).

<sup>174</sup> Boyack & Foster, *supra* note 41, at 257–59 (“Florida is the only state that imposes assessment liability on a lender who acquires title at a foreclosure sale, although it caps the amount of liability imposed on such lender.”).

<sup>175</sup> *Id.* at 255.

<sup>176</sup> *Id.* at 258–59.

<sup>177</sup> *Id.*

<sup>178</sup> THE FL. BAR, *supra* note 165, § 5.628.

<sup>179</sup> Boyack, *supra* note 51, at 107–08. Boyack notes, “[t]he lengthy foreclosure timeline is caused in part by the sheer magnitude of the increase in foreclosure volume over the past few years—in 2010, there were more foreclosures commenced each month than were typically commenced in an entire year prior to 2005.” *Id.*

<sup>180</sup> Bromley, *supra* note 60, at 454. Bromley argues that “[t]he challenges of the foreclosure crisis, especially with protracted timeframes in judicial foreclosure states like Florida, necessitate increased priority rights for associations.” *Id.*

<sup>181</sup> Fla. S. 1196, Gen. Assemb., Reg. Sess. (Fla. 2010).

<sup>182</sup> FLA. STAT. ANN. § 720.3085 (West 2017); FLA. STAT. ANN. § 718.116 (West 2017).

Let us revisit the earlier hypos of Sections II(A) and II(B) to apply the Florida regime to those facts. Again, assume the property in question is located in an HOA neighborhood and was purchased just prior to the 2008 recession through a deed of trust for \$885,000. The homeowner is unable to keep up with both the mortgage payments and association assessments, owing \$4500 on the latter. The balance on the mortgage is \$800,000 while the fair market value of the property is \$400,000. The homeowner makes a decision to walk away from the underwater property and pay neither the mortgage nor the association assessments.

In our first scenario the lender forecloses on their mortgage lien. Under the Florida approach, the lender's lien is not in competition with the association's lien. Instead, the Florida statute shifts responsibility for the delinquent assessments to the purchaser at the foreclosure sale.<sup>183</sup> Whether this is the lender or a third party, the purchaser must pay the cost of the assessments. If the lender decides to purchase the property, then as a purchaser, the lender would be required to pay up to twelve months of the assessments or one percent of the overall mortgage value. In this case let us assume that regular assessments are \$200 a month. Twelve months of assessments would be \$2400 while one percent of the mortgage would be \$8000. The lender would be responsible for the lesser of these amounts and would have to pay \$2400 included in the purchase price. If the purchaser is a third party, then they would have to pay the entire amount of \$4500 in delinquent dues included in the purchase price of the property. This is because the statute only limits the liability of lender-purchasers, not when a purchaser is a third party.

For the second scenario, assume that the lender delays foreclosure in hopes the market recovers or to avoid paying HOA assessments in the event the lender decides to purchase the property. During this period of delay, no one is paying association assessments on the property. The lender is under some pressure during this period to institute foreclosure because they know the priority amount is building up to twelve months' assessments. But assume they wait the full year period and there is no longer additional motivation for the lender to initiate foreclosure. The HOA waits as long as it can and then initiates foreclosure itself. A lender will often have motivation to purchase the property in this situation to avoid having to deal with a third-party purchaser with whom it is not familiar.

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<sup>183</sup> See FLA. STAT. ANN. § 720.3085 (West 2017); FLA. STAT. ANN. § 718.116 (West 2017).

Regardless of whether the lender or a third party purchases the property, the cost of the delinquent assessments will be included in the purchase price: \$2400 for the lender, or the entire \$4500 for a third-party purchaser.

The Florida approach differs significantly from the previously discussed approaches in two distinct ways: (1) the 2010 amendment doubled the priority amount from six months under the UCIOA to twelve months or one percent of the mortgage under the Florida statute, and (2) the super priority of the lien bypasses competition with the first mortgage and instead acts as a statutory liability on the purchaser.<sup>184</sup> Some Florida lawyers have interpreted the plain language of the statute to mean that a non-lender foreclosure purchaser would be liable for the entire amount of delinquent assessments, though this has not yet been decided by a court.<sup>185</sup> This regime is very similar in effect to the limited priority of an HOA lien offered under the UCIOA, but differs by virtually guaranteeing the eventual recovery of delinquent assessments via the liability imposed on the purchaser by the statute.<sup>186</sup>

Some have criticized this approach on the basis that, while it increases the overall delinquent assessment amount an association may recover, it does not solve the underlying problem that remains in both first-in-time jurisdictions and super lien priority statutes that act only as a payment priority.<sup>187</sup> The underlying problem manifests because lenders have no incentive to expedite foreclosure on their lien once assessments have accrued to the maximum allowable super priority level.<sup>188</sup> As discussed in first-in-time jurisdictions, a

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<sup>184</sup> Bromley, *supra* note 60, at 454 (explaining that the lien priority of the Florida statute “functions as a liability on purchasers, not as a lien competing with mortgages”).

<sup>185</sup> See Boyack, *supra* note 51, at 109. Boyack notes that “[a]ccording to some Florida lawyers, the new law permits unlimited recovery of unpaid assessments from third-party buyers at mortgage foreclosure (unlimited durability of the association lien) and caps recovery only from lenders.” *Id.* at 109 n.281.

<sup>186</sup> See FLA. STAT. ANN. § 720.3085; see also FLA. STAT. ANN. § 718.116. Boyack explains that “[t]he six-month capped ‘super-priority’ portion of the association lien does not have true priority status under UCIOA since this six-month assessment lien cannot be foreclosed as senior to a mortgage lien. Rather, it creates a payment priority for some portion of unpaid assessments.” Boyack, *supra* note 51, at 99 (emphasis removed).

<sup>187</sup> See Boyack, *supra* note 51, at 108.

<sup>188</sup> *Id.* Boyack explained the underlying problem of first-in-time jurisdictions in the following text:

Although . . . these enhanced lien priority measures increased ultimate recovery by an association, they failed to solve the underlying problem that still plagues the six-month capped priority laws: once the designated period has elapsed (be it six or nine or twelve months), lenders have no further incentive to contribute to property upkeep or to expeditiously foreclose so that someone new can take title.

*Id.*

lender has little incentive to foreclose on an underwater property in a stagnant market when doing so would require it to pay HOA assessments.<sup>189</sup>

Under the Florida-type alternative, the lender has some incentive to move forward with foreclosure during the twelve-month period while assessments are building up to the statutory cap.<sup>190</sup> However, once this period is over, the lender may continue to delay foreclosure and is still not obligated to pay the assessments since it has not yet taken title.<sup>191</sup> Therefore, the Florida approach somewhat addresses the problem of lender delay in foreclosure by the increase in the statutory cap of assessments for which a lender-purchaser can be held responsible. However, the increased statutory cap does not have the force of extinguishment of the lender's lien that unreservedly forces lender compliance under the Nevada regime.

Others have praised this Florida-style approach as greatly expanding an association's potential recovery of delinquent assessments.<sup>192</sup> Bromley, for example, has posited: "This extension contemplates what the UCIOA drafters could not have foreseen decades prior."<sup>193</sup> Bromley believed that this expansion of the statutory cap under the super priority statute would effectively counter the financial difficulties of HOAs caused by the expanded foreclosure timelines in judicial foreclosure states such as Florida.<sup>194</sup> Furthermore, he noted that the procedure of imposing statutory liability on the purchaser (often the mortgagee) at the foreclosure sale would probably prevent the inequitable results found in decisions like *SFR Investments*.<sup>195</sup> Notably, these assessments of up to twelve months' payments or one percent of the original mortgage debts are generally more generous than the recovery available even in states such as Nevada.<sup>196</sup> Under Nevada law, though the regime grants absolute

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<sup>189</sup> See *supra* Section II(A).

<sup>190</sup> A lender has increased incentive to foreclose during this period simply because the amount they can be liable for as a purchaser is increasing during the twelve-month period. The more quickly they foreclose on the property, the less of the super priority amount they will owe upon purchase of the property.

<sup>191</sup> See *supra* Section II(A).

<sup>192</sup> Bromley, *supra* note 60, at 453–54 (arguing that "Florida separates condominium and homeowners' association liens into separate statutes that greatly expand an association's potential recovery") (footnote omitted).

<sup>193</sup> *Id.* at 454 (explaining that what UCIOA drafters could not have foreseen decades prior were "[t]he challenges of the foreclosure crisis, especially with protracted timeframes in judicial foreclosure states like Florida, necessitate increased priority rights for associations.").

<sup>194</sup> See *id.*

<sup>195</sup> See *id.* at 453–54.

<sup>196</sup> FLA. STAT. ANN. § 720.3085; FLA. STAT. ANN. § 718.116.

priority to an HOA lien, the statutory super priority cap is set at nine months' worth of delinquent assessments.<sup>197</sup>

At first glance, the Florida statutes appear to better balance the interests of the HOAs and lenders. In effect, the Florida regime is “effectively identical to limited priority over a mortgagee,” but also ensures the CIC will recover delinquent assessments through the imposition of liability for these unpaid fees on the purchaser of the property.<sup>198</sup> While providing for the highest recovery for an HOA of any state discussed in this Comment, the method of collection of these dues is unlikely to reproduce the risk of unfairness to lenders imposed by a true priority regime with a super lien priority statute.<sup>199</sup> Despite these attractive characteristics, further analysis of the positive and negative aspects of each approach in regards to their ability to fairly balance competing policy interests is still required before fully evaluating which system works best. Part III broadens the comparative assessment to consider overall fairness and furtherance of other policy objectives across the alternatives.

### III. A COMPARISON OF THE APPROACHES IN RELATION TO FAIRNESS AND POLICY<sup>200</sup>

The preceding Section of this Comment have provided an analysis of the mechanics and consequences to the parties of each jurisdiction's lien priority approach. The following Sections will discuss how each jurisdiction balances issues of fairness and achieves desired policy results. This Part will begin with a discussion of each jurisdiction's effectiveness at achieving fairness and equity for the relevant parties. It will then proceed to examine each type of approach in relation to the policy concerns regarding (1) the disproportionate value of the liens, (2) the value of encouraging HOAs as a means of private governance, (3) the availability of credit to buyers in association communities, and (4) the party in the best position to internalize the externality of delinquent dues.

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<sup>197</sup> NEV. REV. STAT. ANN. § 116.3116.

<sup>198</sup> Bromley, *supra* note 60, at 454.

<sup>199</sup> *Id.*

<sup>200</sup> While this Comment recognizes the ongoing constitutional challenges to super lien priority statutes, this Comment will instead focus on other infirmities of these statutes in terms of fairness and public policy. See *generally* Bourne Valley Court Tr. v. Wells Fargo Bank, 832 F.3d 1154 (9th Cir. 2016); Saticoy Bay LLC v. Wells Fargo Home Mortg., 388 P.3d 970, 971 (Nev. 2017).

## A. Fairness and Equity to the Parties

An attempt to determine a superior approach to HOA lien priority rightly begins with a discussion of fairness and equity. One of the paramount concerns of property law is that an individual's reasonable expectations of his or her interests in property will be respected and protected.<sup>201</sup> Therefore, it is important that the law be settled and predictable in order to offer owners and potential owners of property greater certainty in their property rights.<sup>202</sup> With greater certainty comes greater confidence in investment.<sup>203</sup> This confidence drives our economy, which in turn, distributes the benefits of increased wealth to our society as a whole.<sup>204</sup> This principle was summarized in the seminal case, *State v. Shack*, in which the court recognized that “[p]roperty rights serve human values. They are recognized to that end, and are limited by it.”<sup>205</sup> Both fairness and equity are uniquely human values, and any attempted determination of a system of property rights must include a discussion of these principles.

For reasons discussed previously in Part II, lenders do not have sufficient motivation in a bad housing market to expedite foreclosure proceedings. One reason for this is the lender's hope of maximization on the return on their mortgage lien by waiting to see if the market improves. Another reason is the avoidance of the responsibility of paying HOA dues should the lender purchase the property. Regardless of the reasons for delay, this deliberate and calculated inaction is crippling to associations who have to reduce services they are obligated to provide or increase assessments on paying members.<sup>206</sup> With paying members fitting the bill, lenders receive the benefit of the value of their collateral being preserved without having to pay for this advantage.<sup>207</sup>

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<sup>201</sup> See Donald J. Kochan, *Dealing with Dirty Deeds: Matching Nemo dat Preferences with Property Law Pragmatism*, 64 U. KAN. L. REV., Nov. 2015, at 1, 5–7.

<sup>202</sup> *Id.* at 29–35 (explaining the importance of recording acts as one area of property law that provides “confidence in the transfer of property in a very real way because buyers and sellers have greater predictability in the enforcement of their conveyances”).

<sup>203</sup> See Donald J. Kochan, *Certainty of Title: Perspectives after the Mortgage Foreclosure Crisis on the Essential Role of Effective Recording Systems*, 66 ARK. L. REV. 267, 298–311 (2013).

<sup>204</sup> *Id.* at 310 (“Delineation of ownership facilitates exchange. Contracting would be impossible if parties were unable to trade rights. Likewise, property ownership must be protected from aggression in order for a civil society to flourish. At a minimum, therefore, government must have the power to protect these institutions of property and free exchange.”).

<sup>205</sup> *State v. Shack*, 277 A.2d 369, 372 (N.J. 1971).

<sup>206</sup> See Newsom, *supra* note 96, at 361. Newsom explains that while a “bank is able to shed its financial obligation at the expense [of] the property's innocent neighbors,” an “association must continue to insure and maintain the property regardless of whether the bank or homeowner makes any contribution to the association.” *Id.*

<sup>207</sup> *Id.*

Thus, the lenders were being unjustly enriched by not acting expeditiously in initiating foreclosure proceedings.<sup>208</sup> They were receiving the benefit of preservation of their collateral's value through the dues paid by other members of the community.<sup>209</sup> The payment of these additional costs by the remaining members kept up the property values of the abandoned homes by maintaining attractive characteristics such as exterior upkeep and lawn care despite the lack of a steward-owner to perform these routine tasks. The dues also contributed towards the upkeep of common areas in the neighborhood that increased the abandoned properties' values.

HOA payment for these absconded member shares presented an inherently unfair situation to both community associations and to their remaining members who had to shoulder the cost. Lenders were receiving the value from the preservation of their mortgaged property without a requirement to contribute towards that upkeep. Both the inability of HOAs to remain financially solvent and unjust enrichment of lenders led to the Nevada Supreme Court decision affording true priority to their state's UCIOA-type super lien priority statute.

In contrast to the above examples, super lien priority statutes have resolved many of the problems facing community associations in first-in-time jurisdictions and limited priority UCIOA jurisdictions.<sup>210</sup> Goldmintz argued in favor of a Nevada-type regime that eliminates the limited priority of the UCIOA in lieu of true priority for association liens.<sup>211</sup> His student comment advocated that "giving associations a full priority over all mortgages will insure that associations recover all back-maintenance fees and will put their budgets back on track."<sup>212</sup> He also notes that the burden will be placed "squarely onto lenders," and argues this is equitable because "lenders are better situated to protect against the risks of default, are better

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<sup>208</sup> *Id.*

<sup>209</sup> *Id.* at 363 ("The banks get a premium price for each home because the homes are located in a well-maintained development with a well-run HOA, even though the banks did not pay a dime toward the expenses of the HOA.").

<sup>210</sup> CMTY. ASS'N INST., MORTGAGE BANKERS VS. LOCAL COMMUNITIES: PROTECTING HOMEOWNERS AND AMERICA'S NEIGHBORHOODS (2014), [https://www.caionline.org/Advocacy/StateAdvocacy/PriorityIssues/PriorityLien/Documents/2014\\_NV\\_Response.pdf](https://www.caionline.org/Advocacy/StateAdvocacy/PriorityIssues/PriorityLien/Documents/2014_NV_Response.pdf) [<http://perma.cc/FN7F-VSC8>] (noting that after the *SFR Investments* decision in Nevada, mortgage lenders are moving more quickly to effectuate foreclosures and pay community associations).

<sup>211</sup> Goldmintz, *supra* note 158, at 289–90. Goldmintz proposed that "[t]he limited super-priority should be abolished and associations should be given full priority over mortgagees in order to reverse the downward fiscal spiral of associations and the lenders that finance them." *Id.* (footnote omitted).

<sup>212</sup> *Id.* at 289.

able to bear the burden, and have the tools and sophistication to maximize the value of the sale at foreclosure proceedings.”<sup>213</sup>

However, the fix to HOA issues through such a system does so in an arguably unfair manner at the expense of the lender, whose interest may be extinguished without adequate justification. Lenders and their supporters have stated that “[t]hese initiatives run contrary to the very heart and nature of secured lending.”<sup>214</sup> A Nevada-style regime effectively coerces a lender to pay association dues by using the threat of extinguishing his interest (sometimes worth hundreds of thousands of dollars) for the act of omission of not instituting its own foreclosure proceedings in a timely manner.<sup>215</sup>

However, proponents of super lien priority statutes have argued that because notice to the lender is required to be given of an HOA foreclosure, the lender has adequate time and opportunity to ensure the security of its interest.<sup>216</sup> In October of 2015, in response to constitutional challenges relating to adequate notice, the Nevada Legislature amended its statute to ensure a lender with an interest in a property being foreclosed on by an HOA would receive adequate notice to protect its interest.<sup>217</sup> NRS section 116.31163 provides that:

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 certified mail to: . . . Each holder of a recorded security interest encumbering the unit’s owner’s interest which was recorded before the recordation of the notice of default, at the address of the holder that is provided pursuant to NRS 657.110 on the Internet website maintained by the Division of Financial Institutions of the Department of Business and Industry.<sup>218</sup>

This statute requires that notice be delivered to a holder of a recorded security interest that was recorded prior to the HOA

<sup>213</sup> *Id.*

<sup>214</sup> Aušra Gaigalaite, *Priority of Condominium Associations’ Assessment Liens vis-à-vis Mortgages: Navigating in the Super-Priority Lien Jurisdictions*, 40 SEATTLE U. L. REV. 841, 866 (quoting AM. BANKERS ASS’N ET AL., STATEMENT OF PRINCIPLES ON HOA SUPER PRIORITY LIENS 1 (2015)).

<sup>215</sup> *See supra* Section III(B).

<sup>216</sup> Gloeckner, *supra* note 48, at 343–44. Gloeckner explains the notice argument for true lien priority:

For example, proponents of HOAs have argued that because NRS Chapter 116 requires multiple notices be provided to lenders, there is sufficient time to secure their interest. A lender does not lose its interest until the property is sold at an HOA foreclosure sale; therefore, lenders have ample time to cure delinquent assessments on the home.

*Id.* at 343 (footnotes omitted).

<sup>217</sup> *See* Gardberg, *supra* note 3, at 17.

<sup>218</sup> NEV. REV. STAT. ANN. § 116.31163 (West 2015).

assessment under which an association forecloses. Because first mortgage or deed of trust holders fall squarely within the category of parties who must be afforded notice, extinguishment of the lender's interest is arguably equitable if they fail to act to protect their interest by paying the assessment. However, the argument that a lender has adequate notice to pay off an association lien and save its interest in the property ignores the basic principle that the lender is not responsible for the assessment debt in the first place.

It is important to remember that the original homeowner who defaulted on payments is the party who is ultimately responsible for the assessment debt. The most equitable solution would be for the debtor to pay his own debts. However, often times this is not a practical solution because the debtor may not have the necessary funds to pay their debt. While placing the burden on another party that has the resources to pay is obviously more practical, it brings up issues of fairness and equity that cannot be ignored.

One of the strongest fairness arguments for a Nevada-type regime is that it is fair for a lender to shoulder the responsibility of HOA dues because the lender acts wrongfully by delaying foreclosure proceedings and is thereby unjustly enriched.<sup>219</sup> However, in order for a party to fairly be held accountable for a wrongful omission or inaction, they must fail to perform a legal duty the party is obligated to perform. *Black's Law Dictionary* defines a duty as “[a] legal obligation that is owed or due to another and that needs to be satisfied; that which one is bound to do, and for which somebody else has a corresponding right.”<sup>220</sup>

A lender is in privity with a homeowner mortgagor who has been granted a mortgage loan to purchase property located within a neighborhood governed by an HOA. An association is in privity with such a homeowner through the covenants attached to the purchased property. However, a lender and association have no direct connection with each other through these relationships with the homeowner. Until a lender takes title to the property by foreclosure sale or deed in lieu of foreclosure, a

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<sup>219</sup> See Goldmintz, *supra* note 158, at 289. Goldmintz states that a full priority scheme “incentivizes . . . the quick execution of foreclosure proceedings, since, the longer the bank waits, the more money they’ll have to pay to associations. This, in turn, is therefore more equitable, more efficient, and more beneficial to all the parties involved.” *Id.* (footnote omitted). See also Newsom, *supra* note 96, at 363 (arguing that banks are unjustly enriched by receiving the benefit of the higher value of a property in a well-run HOA by delaying foreclosure, and therefore, their obligation to pay assessments).

<sup>220</sup> *Duty*, BLACK’S LAW DICTIONARY (10th ed. 2014).

lender has no legal duty to pay association assessments.<sup>221</sup> Therefore, a lender has no legal duty to pay an HOA when the homeowner mortgagor defaults on association assessments, just as the HOA has no legal duty to pay the homeowner's mortgage when he or she defaults on mortgage payments.

Even if it is determined that it is equitable for a lender to pay the mortgagor's delinquent assessments, extinguishment and threat of extinguishment of the lender's mortgage lien does not correspond proportionally to the wrong the lender committed. As to the wrong the lender commits, there is a good argument that the lender is unjustly enriched by not paying dues the non-defaulting HOA members must pay.<sup>222</sup> *Black's Law Dictionary* defines unjust enrichment as "[a] benefit obtained from another, not intended as a gift and not legally justifiable, for which the beneficiary must make restitution or recompense."<sup>223</sup> As previously discussed in this Part, a lender obtains the benefit of protection the value of his interest in the property without having to pay for that benefit.

However, the normal remedy for unjust enrichment is restitution which does not involve extinguishment of a lien far more valuable than the benefit conferred.<sup>224</sup> The remedy of restitution definition provides that "the measure of recovery is usually based not on the plaintiff's loss, but on the defendant's gain."<sup>225</sup> The unjust benefit conferred to lenders was protection of their interests' value through the payment of assessments by other association members. Restitution of this benefit would mean that the lender would have to disgorge the benefit conferred: the payment of the assessments.

A Nevada-style regime does require payment of assessments by the unjustly enriched lender and is in accordance with the principle of restitution. However, it does so by giving a power of extinguishment of the lender's lien to the HOA through its ability to foreclose on the property. Because a lender's lien will usually be much more substantial than the relatively minor benefit of protection of the mortgaged property's value, even inadvertent extinguishment would produce an extremely harsh and unjust result.

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<sup>221</sup> *JEB Report*, *supra* note 106.

<sup>222</sup> See Newsom, *supra* note 96, at 361, 363–64 ("[A] bank that purposely delays foreclosure on a property located in a homeowner's association is unjustly enriched by the association when the bank knows the homeowner has also defaulted on its homeowner's association dues.").

<sup>223</sup> See *Unjust Enrichment*, BLACK'S LAW DICTIONARY (10th ed. 2014).

<sup>224</sup> *Id.*

<sup>225</sup> *Restitution*, BLACK'S LAW DICTIONARY (10th ed. 2014).

The Florida approach of joint and several liability for the purchaser and seller likely strikes a fairer balance between these divergent extremes of first-in-time jurisdictions and true priority super lien priority statutes. As previously discussed, both first-in-time and true priority super lien priority statutes completely place the cost of delinquent dues either on the association or lender respectively. Under the Florida method, the burden of paying delinquent HOA dues shifts to the purchaser.<sup>226</sup>

After the homeowner who originally defaulted on the debt, the purchaser is arguably the party upon which it is most fair to impose this cost. The negative externalities of delinquent assessments must be borne by a party other than the original debtor if the debtor cannot be made to pay. Pursuit of a judgment against that debtor may be impractical because they are insolvent or judgment proof. If the association internalizes the cost of the debt, the cost is distributed to its other members.<sup>227</sup> This is an unjust result because the other members are not responsible for the debts of the defaulting members, and those other members are likely under similar financial burdens which caused the non-paying members' defaults.<sup>228</sup> As previously discussed, while a lender may be better able to bear the cost, forcing him or her to pay for an externality he or she did not cause also produces an unjust result.

In contrast to the association and lender, a purchaser of the property has the ability to either accept the added liability of paying the delinquent dues, or to walk away from the foreclosure sale. In addition, the association lien is taken out of competition with the first mortgage because the assessment amount is statutorily required to be paid by the foreclosure purchaser.<sup>229</sup> Rather than having a zero sum game between the association and lender, liability for the externality is simply placed upon the shoulders of the one party who can make the choice to accept it.<sup>230</sup> The added factor of choice arguably makes the Florida approach the most fair and equitable of the different

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<sup>226</sup> See FLA. STAT. ANN. § 720.3085 (West 2017); see also FLA. STAT. ANN. § 718.116 (West 2017).

<sup>227</sup> Christine Haughney, *Collateral Foreclosure Damage for Condo Owners*, N.Y. TIMES (May 15, 2008), <http://www.nytimes.com/2008/05/15/business/15condo.html>.

<sup>228</sup> See CMTY ASS'N LEADERSHIP LOBBY, COMMUNITY ASSOCIATIONS FACE A PERFECT STORM: FORECLOSURES, BUDGET SHORTFALLS, AND STATE MANDATES (Dec. 1, 2009).

<sup>229</sup> Bromley, *supra* note 60, at 454–55.

<sup>230</sup> Under a first-in-time regime, a first mortgage or deed of trust will usually take priority and extinguish an association lien upon the lender's foreclosure. On the other hand, a true priority super lien priority statute completely shifts this advantage to the HOA lien that will extinguish a first mortgage if foreclosed upon by the association. This situation presents a zero sum game where it is all or nothing for either side. See *supra* Sections II(A) and II(B).

lien priority schemes discussed. The next Sections examine whether it remains in that favored position after considering other policy concerns.

## B. The Disproportionate Value of the Liens

One of the most compelling policy arguments against the Nevada super lien statute and its interpretation by the Nevada Supreme Court relates to the differential value between competing lien interests. The value of an association lien compared to a first mortgage is usually extremely disproportionate. An association lien will typically only be for a few thousand dollars of delinquent dues,<sup>231</sup> whereas a first mortgage will usually be an amount closer to the entire value of the home at the time it was bought.<sup>232</sup> To allow an HOA foreclosure on a lien worth a few thousand dollars to extinguish a million dollar mortgage does not appear to be fair and just. Consider the following examples of the inequities that can result in some true super lien priority jurisdictions.

In *SFR Investments*, U.S. Bank approved a mortgage loan for \$885,000 in 2007, just before the housing bubble imploded the following year.<sup>233</sup> During the recession, the homeowner fell behind on payments and then quit paying altogether because the value of the home was underwater.<sup>234</sup> In addition to their mortgage, the homeowners also owed about \$4500 in association dues.<sup>235</sup> The HOA began a non-judicial foreclosure proceeding without notice to the bank and sold the home at an auction for \$6000 to SFR, a speculation company that was taking advantage of the legal/economic situation.<sup>236</sup> SFR initiated a quiet title action, and the court held U.S. Bank's security interest on the remaining \$800,000 of the loan was extinguished.<sup>237</sup> The

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<sup>231</sup> Melissa Waite, *The HOA Foreclosure and Priority: Who is in First?*, CLARK COUNTY B. ASS'N COMMUNIQUÉ, Nov. 2013, at 26, 26–28. Waite describes HOA foreclosure sales in Nevada at the time of this article as being “very low in relation to the fair market value of the property being sold” with the typical sales price being between \$3000 and \$12,000. *Id.*

<sup>232</sup> Timm Herdt, *Foreclosure crisis not driven by luxury home purchases*, VENTURA COUNTY STAR (Aug. 17, 2010), <http://archive.vcstar.com/business/foreclosure-crisis-not-driven-by-luxury-home-purchases-ep-367899884-348388001.html/?page=1> [<http://perma.cc/L2EW-4FTA>] (stating an analysis by the nonprofit Center for Responsible Lending showed that the average value at the time of loan origination was \$396,351).

<sup>233</sup> *SFR Investments Pool 1, LLC v. U.S. Bank*, 334 P.3d 408, 409 (Nev. 2014).

<sup>234</sup> *Id.*

<sup>235</sup> *Id.* at 418.

<sup>236</sup> *Id.* at 409. Note that under subsequent Nevada laws, notice would be required. The Nevada Legislature addressed the issue of notice by requiring adequate notice to other interest holders in a property that is the subject of an HOA foreclosure. *See supra* Section III(A).

<sup>237</sup> *Id.* at 418–19.

loan became unsecured and eventually resulted in losses to the bank.<sup>238</sup>

In *Chase Plaza Condominium Association, Inc. v. JPMorgan Chase Bank*, the original buyer of a condo bought the property with a loan from JPMorgan Chase Bank for \$280,000.<sup>239</sup> The owner fell behind on payments for the loan, and also owed payments to their condominium association amounting to \$9415.<sup>240</sup> The association foreclosed without notifying the bank and sold the condo for \$10,000.<sup>241</sup> The bank was alerted to the sale when the association sent a check to the bank for the surplus of \$478.<sup>242</sup> The court upheld this action as valid because the Washington D.C. super lien priority statute gave the CIC lien priority over the mortgage, and the foreclosure by the HOA extinguished the bank's interest in the condo.<sup>243</sup>

In *Saticoy Bay*, the original purchaser took out a mortgage loan for \$81,370 from Wells Fargo Bank.<sup>244</sup> The homeowner fell behind on their association dues, and the HOA foreclosed on their lien.<sup>245</sup> The property was sold for only \$6900 to another speculation LLC intending to cash in on the situation.<sup>246</sup> The Court upheld the Nevada super lien priority statute as constitutional, holding, inter alia, that the HOA's exercise of its new statutory rights did not constitute state action for purposes of the Due Process Clause and the Takings Clause.<sup>247</sup>

As these cases demonstrate, because an HOA can only collect the small amount it is owed on its lien from the profits of its foreclosure sale, it has little incentive to sell the home at a price which exceeds the amount they are owed.<sup>248</sup> One Nevada attorney stated that a typical sales price at an association foreclosure in Nevada during 2013 was between \$3000 and

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<sup>238</sup> Vaughn, *supra* note 3, at 4.

<sup>239</sup> *Chase Plaza Condo. Ass'n, Inc. v. JPMorgan Chase Bank*, 98 A.3d 166, 168 (D.C. Cir. 2014).

<sup>240</sup> *Id.*

<sup>241</sup> *Id.* The court hinted that the failure of the lien priority statute to require notice be sent to other lienholders may be facially unconstitutional, but was unable to reach the issue because JPMorgan did not raise it as an issue. See *Goodwin Mortgage Liens*, *supra* note 149.

<sup>242</sup> *Chase Plaza Condo. Ass'n*, 98 A.3d at 168–69.

<sup>243</sup> *Id.* at 178.

<sup>244</sup> *Saticoy Bay LLC v. Wells Fargo Home Mortg.*, 388 P.3d 970, 971 (Nev. 2017).

<sup>245</sup> *Id.*

<sup>246</sup> *Id.*

<sup>247</sup> *Id.* at 975.

<sup>248</sup> See 6A PATRICK J. ROHAN, REAL ESTATE TRANSACTIONS: HOME OWNER ASSOCIATIONS AND PLANNED UNIT DEVELOPMENTS – LAW AND PRACTICE § 9.15 (Matthew Bender ed., 2013) (“The purpose of foreclosure of an association's lien is to have the property applied to the payment of the outstanding assessment liability.”).

\$12,000.<sup>249</sup> This amount is not even close to what would usually be required to satisfy a first mortgage, which can often run in the hundreds of thousands, if not millions, of dollars. Savvy real estate investment companies have taken advantage of the situation and often make a profit of twenty to fifty times the amount in which they paid at the HOA foreclosure.<sup>250</sup> It is obvious that equity to the lender demands this wrinkle in the law be addressed, and addressed quickly.

One route for challenging an association's foreclosure sale that has been met with limited success is a claim the UCIOA incorporates a duty of good faith on the part of HOAs conducting foreclosure sales to expend efforts to get the fair market price for the property.<sup>251</sup> The UCIOA states: "Every contract or duty governed by this [act] imposes an obligation of good faith in its performance or enforcement."<sup>252</sup> The Vermont Supreme Court recently held that enforcement of an HOA lien via foreclosure must be executed in good faith as defined by section 1-113 of the UCIOA, which requires a standard of commercial reasonableness.<sup>253</sup> In doing so, the court set aside a foreclosure sale of a parcel just over \$33,500 when that parcel had a fair market value of at least \$70,000.<sup>254</sup> The court reasoned that the sale was not commercially reasonable, so the sale must be void under the good faith standard of the UCIOA.<sup>255</sup>

This application of the law by the Vermont Supreme Court demonstrates a possible solution to prevent this unjust result under Nevada-type lien priority regimes.<sup>256</sup> It is possible that had the good faith issue been raised in *SFR Investments, Chase Plaza*, and *Saticoy Bay*, these courts could have found that the associations failed to meet the good faith standard because the sales prices were for just a fraction of the likely fair market

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<sup>249</sup> See Waite, *supra* note 231, at 26.

<sup>250</sup> See Robin E. Perkins, *Can an HOA "Super-Priority" Lien Extinguish a Lender's Deed?*, A.B.A. SEC. LITIG. (Mar. 18, 2014), <https://www.americanbar.org/groups/litigation/committees/corporate-counsel/articles/2014/winter2014-can-an-hoa-super-priority-lien-extinguish-a-lenders-deed.html> [<http://perma.cc/KP6J-SV4R>]. Perkins states a home costing anywhere from \$200,000 to \$500,000 would be sold at an HOA foreclosure sale for an amount between \$3000 and \$10,000 because "properties are auctioned for little more than the amount of the HOA lien." *Id.*

<sup>251</sup> See Gaigalaité, *supra* note 214, at 868.

<sup>252</sup> UCIOA § 1-113.

<sup>253</sup> *Will v. Mill Condo. Owners' Ass'n*, 848 A.2d 336, 341 (Vt. 2004).

<sup>254</sup> *Id.* at 342-43.

<sup>255</sup> *Id.*

<sup>256</sup> Although beyond the scope of this Comment, which focuses on three approaches to HOA lien priority as they currently exist, incorporation of the duty of good faith into the UCIOA may be a possible solution to the inequitable result to lenders of homes being sold by HOAs at foreclosure for a fraction of their value. It will be interesting to see if this proposition is adopted by the true super lien priority states in the near future.

values of the properties. Such sales of properties would probably not fall within the definition of commercial reasonableness required by the UCIOA good faith standard. Therefore, the good faith standard may have played an important role in these cases because the UCIOA was incorporated by the lien priority statutes of both the District of Columbia and Nevada.

While super lien priority statutes have solved many of the problems that associations have encountered in first-in-time jurisdictions, the cost of this benefit should not be a disaster to lenders and a windfall to third-party purchasers taking advantage of the situation. When an association's small value lien is able to extinguish a large first mortgage, there is possibly a commercially unreasonable transaction if the HOA forecloses and sells the property. The other possible end result is the lender is coerced into paying another's bill to prevent such a transaction. It is difficult to invent an argument where either of these results could be considered fair to the lender. Nonetheless, any proposed solution must balance fairness to the lender with the ability of an association to collect dues and remain financially solvent, a goal that we have seen is not easy to reach. The next Section focuses again on some of the special values of HOAs implicated by the competing liens.

### C. The Value of HOAs as an Efficient Means of Private Governance

Another major policy consideration related to lien priority lies in preserving the financial security of CICs so that they may serve to reduce the burdens on local governments. Many argue that typically, HOA's are a more efficient and better vehicle for neighborhood maintenance, upkeep, and community relations than public government.<sup>257</sup> HOA's are usually run by members of the community who are closely attached to the situation in their neighborhood and have a personal stake in the betterment of their community.<sup>258</sup> In contrast, elected officials in public government may be detached from specific needs and requirements of a particular neighborhood.<sup>259</sup> Allowing semi-autonomous governance of a community by private associations reduces the responsibilities of municipal government and places

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<sup>257</sup> See Bromley, *supra* note 22, at 261–65.

<sup>258</sup> See HYATT, *supra* note 29, at 21 (“An association of the property owners in the community (the ‘community association’) manages the common property with funds obtained by levying assessments against the property.”).

<sup>259</sup> See Bromley, *supra* note 22, at 262–63.

them in the hands of the community members themselves.<sup>260</sup> This often equates to a well maintained community with corresponding higher property values.<sup>261</sup>

Beginning in the 1960s, CICs developed from an experiment in suburban housing into one of the most common forms of residential neighborhoods in America today.<sup>262</sup> In 1970, there were about 10,000 CICs with an estimated 2.1 million residents living in approximately 700,000 housing units.<sup>263</sup> By 2015, the number had exponentially increased to an estimated 338,000 communities with sixty-eight million residents living in 26.2 million housing units, and twenty-one percent of the total United States population living in CICs.<sup>264</sup> CIC housing was estimated, in aggregate, to be valued at \$5.287 trillion in 2015.<sup>265</sup>

The Foundation for Community Association Research attributes this rapid growth of community association to four factors: (1) the value of collective management at the neighborhood level, (2) the privatization of public functions reducing financial pressure on local municipalities, (3) the expansion of affordable homeownership with condominiums as lower cost entry housing, and (4) the minimization of social costs and fostering of market efficiencies by reducing government oversight of routine community maintenance.<sup>266</sup> In fact, local governments often require new subdivisions to form HOAs as a condition of land use approval as a “load shedding” function of services and tasks which are usually carried out by local government.<sup>267</sup>

The ability of an HOA to collect the dues necessary to maintain the community through a secure mechanism afforded by law is essential to encouraging the continued growth of HOAs.<sup>268</sup> If associations are underfunded because members are not paying their dues, both lower property values and higher

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<sup>260</sup> See FOUND. FOR COMMUNITY ASS'N RES., STATISTICAL REVIEW FOR U.S. HOMEOWNERS ASSOCIATIONS, CONDOMINIUM COMMUNITIES AND HOUSING COOPERATIVES (2012).

<sup>261</sup> Daniel S. Scheller, *Neighborhood Governments and their Role in Property Values*, URBAN AFFAIRS REV. 1, 24–25 (2010).

<sup>262</sup> See Bromley, *supra* note 22, at 261–62.

<sup>263</sup> COMMUNITY ASS'N INST., NATIONAL AND STATE STATISTICAL REVIEW FOR 2015: COMMUNITY ASSOCIATION DATA (2015).

<sup>264</sup> *Id.*

<sup>265</sup> *Id.*

<sup>266</sup> FOUND. FOR COMMUNITY ASS'N RES., *supra* note 260.

<sup>267</sup> Bromley, *supra*, at 262.

<sup>268</sup> *Id.* at 264–65. Bromley notes there is an “inherent interdependency” between associations and their members. *Id.* at 264. “The association provides vital necessities to the community that will be dramatically affected, should some or all be eliminated if the association is unable to sufficiently fund them. The association is simultaneously dependent on the property owners’ payment of dues in order to maintain these necessities.” *Id.*

dues for members who are continuing to pay assessments result.<sup>269</sup> The impact on association services, in turn, can actually have a negative effect on the economy on a large scale by the corresponding decline in property values.<sup>270</sup> Therefore, it is in the interest of public policy to both encourage the growth of HOAs and ensure they have the means to fund themselves.

While encouragement of community associations remains a high public policy goal, such support should not undermine issues of fairness under the law and other public policy goals. These issues are at the center of the controversy over the Nevada statutes.<sup>271</sup> Although these regimes have largely solved first-in-time HOA lien priority issues, they have also lead to negative fairness and policy consequences. In contrast, the original difficulties of HOA collection on delinquent dues remain in the first-in-time and limited priority UCIOA jurisdictions.<sup>272</sup> A more balanced approach is required to address the issue of protecting HOA solvency because negative policy consequences result from the application of both super lien priority statutes and traditional first-in-time regimes.

A better solution may be one similar to the more balanced Florida approach. Unlike the preferential treatment to either lender or association afforded under the other approaches through lien priority, this method passes the cost of the unpaid assessments to the purchaser of the property by statute.<sup>273</sup> The purchaser is free to make the decision to either assume or reject the debt imposed by the statute on the purchase price because they may decide whether or not to purchase the property. While some may argue that this approach would damage HOAs by chilling possible sales due to the additional cost, this will usually only amount to a few thousand dollars on top of the purchase

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<sup>269</sup> Haughney, *supra* note 227. Even “[b]argain hunters say they are reluctant to buy” when “they might have to pay unexpected fees as distressed neighbors default on their mortgages or just stop paying the association fees that cover everything from taxes to pool maintenance to air-conditioning repair.” *Id.*

<sup>270</sup> See Goldmintz, *supra* note 158, at 286–87. Goldmintz argues that “when associations buckle under the pressure of multiple, simultaneous delinquencies, property values suffer. This hinders the mortgagee’s ability to maximize its recovery at a foreclosure sale.” *Id.* at 286. Therefore, “the lender’s pecuniary interests are intimately wrapped up in the long-term viability and short term liquidity of associations. As lenders work to undermine the extension of super-liens beyond the current six-months, they work contrary to their own financial interests.” *Id.*

<sup>271</sup> See Aalberts, *supra* note 18, at 327–29.

<sup>272</sup> See *supra* Section II(A).

<sup>273</sup> See FLA. STAT. ANN. § 720.3085 (West 2014); see also FLA. STAT. ANN. § 718.116 (West 2014).

price.<sup>274</sup> Because a buyer is probably already getting a reduced price in a foreclosure sale, it is likely that this small amount in relation to overall cost will not have a large effect on finding buyers at foreclosure sales.

The Florida statute also addresses the first-in-time jurisdiction problem of lenders delaying foreclosure proceedings. As discussed previously, one of the major problems of a first-in-time jurisdiction is that a lender's superior priority allows them to delay foreclosure to wait for market recovery and avoid paying the additional cost of association assessments. Lender foreclosure delay places a large burden on associations and their remaining members because it causes the property to remain without a custodian and no one paying dues.

Both the Florida HOA and condo association lien priority statutes allow for up to twelve months of assessments or one percent of the mortgage in regards to a purchase by the lender.<sup>275</sup> This is double the amount which is provided for under the UCIOA and currently greater than any super priority lien statute jurisdiction allows.<sup>276</sup> This provides incentive to a lender who will be motivated to expedite foreclosure proceedings because the assessments it is liable for upon purchase will be accruing for twice the period provided for by most states with super lien priority statutes.

However, the large Florida super priority amount does not address the issue of lender foreclosure delay in two situations: (1) when the lender is not considering purchase of the property if the HOA forecloses, and (2) when the lender has already waited twelve months to foreclose and the super priority amount it would have to pay upon purchase is already capped. One possible solution to the second issue is for Florida to adopt a provision similar to the 2014 UCIOA section 3-316(c)(1) amendment allowing for rolling liens.<sup>277</sup> The rolling lien authorized under the UCIOA allows for a six month super priority amount for each budget year for the HOA.<sup>278</sup> Therefore, an HOA is entitled to the super priority amount available under the statute for each budgeted year.

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<sup>274</sup> Waite, *supra* note 231, at 26–28. Waite states that a typical sales price of a Nevada home in an HOA foreclosure sale would be in between \$3000 and \$12,000, which is “slightly more than the amount owed to the HOA.” *Id.* at 26.

<sup>275</sup> FLA. STAT. ANN. § 720.3085 (West 2014); FLA. STAT. ANN. § 718.116 (West 2014).

<sup>276</sup> See Lewis *supra* note 38, at 1. The UCIOA offers six months of assessments for its super priority amount. Nevada statute provides for up to nine months of assessments which is the second largest amount provided for by any state. *Id.*

<sup>277</sup> UCIOA § 3-116(c)(1).

<sup>278</sup> *Id.*

While not a perfect solution, the Florida regime balances the interests of both parties by providing a better mechanism for collection of association dues without threatening or otherwise jeopardizing the lender's substantial interest in the property. As will be shown in the next Section, security in a lender's interest in a property may have more importance than solely on the question of what is equitable and fair.

#### D. Lender Willingness and Buyer Opportunity to Obtain Financing

Lenders have been watching carefully (and with anxiety and unease) the decisions affording true priority to HOA liens. There is inherent risk in implementing unrestricted HOA super lien priority statutes because it may have a chilling effect on the housing market.<sup>279</sup> Lenders will be taking on a great amount of additional risk by lending to borrowers purchasing in HOA communities.<sup>280</sup> When their liens can be subordinated by statute and extinguished if they fail to pay a homeowner's delinquent assessment, they will be reluctant to take on this substantial risk.<sup>281</sup>

Proponents of HOA super lien priority statutes have argued that this risk can be almost completely mitigated by adequate notice to the lender of the association's intent to foreclose.<sup>282</sup>

In 2015, the Nevada Legislature amended its super lien priority statute to require the HOA to send foreclosure notices to any lienholders who have a recorded interest in the property.<sup>283</sup>

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<sup>279</sup> Deborah Goonan, *Is the HOA priority lien necessary and beneficial?*, INDEP. AMERICAN COMMUNITIES (June 9, 2016), <https://independentamericancommunities.com/2016/06/09/is-the-hoa-priority-lien-necessary-and-beneficial/> [<http://perma.cc/FKB3-ZDZT>] (“Essentially, wiping out the first mortgage lien ultimately forces other borrowers to pay more for a mortgage, makes it more difficult to obtain a mortgage, and makes homeownership more elusive.”).

<sup>280</sup> Kenneth R. Harney, *Homeowner association liens pose perils for condo buyers*, L.A. TIMES (May 17, 2015, 5:00 AM), <http://www.latimes.com/business/la-fi-harney-20150513-story.html> [<http://perma.cc/J9K4-KG6N>] (“For example, if the amount of back assessments owed is \$6,000 but the first mortgage on the property is in the hundreds of thousands of dollars, the house might be sold at foreclosure to a bargain-hunting buyer for the assessment amount plus fees, leaving the lender with huge losses.”).

<sup>281</sup> *Realtor Magazine* noted the lending industry has warned that “[h]ome buyers may soon face more stringent underwriting standards and even higher interest rates when applying for a mortgage to purchase a home that falls within a homeowner association.” *Buyers Face Barriers in HOA Neighborhoods*, REALTOR MAG. (May 17, 2015), <http://realtormag.realtor.org/daily-news/2015/05/18/buyers-face-barriers-in-hoa-neighborhoods> [<http://perma.cc/KM7G-7ZF8>].

<sup>282</sup> See *SFR Investments Pool 1, LLC v. U.S. Bank*, 334 P.3d 408, 414, 418 (Nev. 2014) (“[A]s a junior lienholder, U.S. Bank could have paid off the SHHOA lien to avert loss of its security.”).

<sup>283</sup> Gardberg, *supra* note 3, at 17 (“The lienholder then has a specific period of time—until five days before the foreclosure sale—to pay off the superpriority lien. Upon

However, it is not yet clear if this notice process will reduce the risk of inadvertent extinguishment of lender interests. Large lending institutions have mortgages on a large amount of properties, and verifying which properties are located in some sort of community association is not as easy as one would assume.<sup>284</sup> Lenders continue to deal with the uncertainty of inadvertent extinguishment because the reliability of the notice regime to correct information deficiencies has yet to be fully tested.

This higher risk in super lien priority statute jurisdictions, whether real or merely perceived, could trigger both higher rates on financing and an overall reluctance of creditors to extend credit to certain buyers.<sup>285</sup> The Mortgage Bankers Association reports that currently:

Over 1,000 Nevada cases continue to be litigated to determine whether clear title existed for property purchasers at HOA foreclosure sales, and subsequently whether proper notice was given by HOAs to first lien mortgagees before these sales were executed. If the courts determine notice was proper and clear title exists, these mortgagees could lose hundreds of millions of dollars from this change in interpretation.<sup>286</sup>

This additional risk and possible loss of a substantial amount of lender investment has a high probability of affecting availability and interest rates on credit. Though it has not yet played out, lending industry representatives have already indicated that “[w]here any HOA super lien authority exists, lenders may be forced to price risk through higher interest rates, mitigate it through larger downpayment [sic] requirements, or exit risky jurisdictions altogether. Property owners may even be unable to sell or refinance their homes.”<sup>287</sup> This effect, in turn, could lead to certain buyers being effectively shut out of the market.

While lenders will most likely not make good on their threat to exit super lien priority statute jurisdictions since almost half of the United States has some form of these statutes, other effects such as higher interest rates and limited availability of

doing so, the HOA may still foreclose (on the portion of its lien, if any, not having superpriority status), but the lender’s lien will not be extinguished.”)

<sup>284</sup> Goonan, *supra* note 279 (“According to Equifax . . . private industry has taken the lead in creating a national database of HOAs,” but the “database is missing a minimum of 125,000 HOAs, based upon CAI’s estimated total of 350,000 HOAs.”)

<sup>285</sup> Harney, *supra* note 280. In a statement before the Nevada Legislature, general counsel for the Federal Housing Finance Agency, Alfred Pollard, stated that if lenders’ rights can be extinguished by community associations, purchasers “may face challenges in securing a loan to buy a unit or refinance.” *Id.*

<sup>286</sup> *Homeowners and Condominium Associations Should Not Be Granted “Super Lien” Priority*, MORTGAGE BANKERS ASS’N, <https://www.mba.org/issues/residential-issues/hoa-super-lien-priority> [<http://perma.cc/48LC-8MX4>] (last visited March 19, 2018).

<sup>287</sup> *Id.*

credit to certain borrowers are very real possible consequences.<sup>288</sup> Proponents of super lien priority statutes argue that lenders are in the best position to absorb the externality of delinquent assessments by directly assuming those debts when the original debtor cannot be compelled to pay.<sup>289</sup> However, it is likely that these costs will ultimately be passed on to consumers causing further negative economic consequences.

#### E. Which Party is in the Best Position to Internalize the Cost?

One of the major questions in determining which of the three discussed approaches is better, both in fairness and policy, is money. Who should bear the cost of the delinquent HOA dues when the original debtor walks away from the property and refuses to pay both the mortgage and association assessments? There appear to be four different options of those whom could potentially bear the cost: (1) the original homeowner, (2) the association, (3) the lender, or (4) the purchaser at the foreclosure sale.

One student comment suggests that the optimal method would be for the HOA to seek a money judgment against the original homeowner who is in default.<sup>290</sup> While this approach seems to be the most equitable because it would force the person who incurred the debt to internalize their own costs, it does not have a realistic likelihood of resulting in successful collection. A person who is underwater and walking away from their home, including the debt associated with it, likely does not have enough assets to make legal action against them worthwhile.<sup>291</sup> This type of judgment is also difficult to enforce both because it is against an individual rather than a business, and the personal debt against the individual is unsecured.<sup>292</sup> A court order could provide for garnishment of wages, but pursuing a judicial remedy against the owner costs the association money and time.<sup>293</sup>

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<sup>288</sup> See Lewis, *supra* note 38, at 1. Lewis notes that twenty-two states currently have super lien priority statutes. *Id.* It will be interesting to see if loan statistics confirm the lender threat of higher interest rates and less availability of credit.

<sup>289</sup> Vaughn, *supra* note 3, at 11.

<sup>290</sup> *Id.* at 28–30.

<sup>291</sup> JAMES J. BROWN, JUDGMENT ENFORCEMENT § 2.11 (3d ed. 2017) (“The client may decide that the hourly fees have reached the limit of economically achieving the judgment enforcement objectives. There is a point in postjudgment litigation when the client rightfully cuts his losses, sits on the judgment, and waits for other enforcement opportunities to come along.”).

<sup>292</sup> ALAN M. AHART, *Lawyer’s Role in Debt Collection Process*, in ENFORCING JUDGMENTS AND DEBTS (2017). Judge Ahart explains that enforcing unsecured judgments on consumer claims are difficult to collect because of liberal exemptions under the law, difficulty in locating the debtor, insufficient assets and income, and a consumer is more likely than a business to file a Chapter 7 bankruptcy petition. *Id.*

<sup>293</sup> BROWN, *supra* note 291, § 2.11 (“Counsel engaged in enforcing judgments must consider the size of the judgment and collection prospects vis-à-vis a reasonable budget for

The problems associated with HOAs collecting money judgments against debtors are compounded when there are multiple owners within the community who have walked away from their debt. In such situations legal costs for pursuing and collecting the individual judgments will be multiplied since they must be pursued against multiple debtors. Because the debt is secured by lien, foreclosing on the property is a safer and more cost efficient option for an association to collect the deficiency when an owner is likely not to have sufficient personal assets to pay a judgment.<sup>294</sup>

Making the HOA bear the cost of the delinquent assessments is another option. The first-in-time approach gives priority to the lender's mortgage when it is first-in-time.<sup>295</sup> In the foreclosure context, the HOA cannot recoup the cost of the delinquent dues unless: (1) there is a surplus from the lender's foreclosure, or (2) the HOA forecloses and is able to sell the property for an amount in excess of the lender's mortgage.<sup>296</sup> Either are highly unlikely in a recession, and the law should be prepared for the worst of situations.<sup>297</sup> Therefore, in a first-in-time jurisdiction, the burden remains with the association, which will have to internalize the cost by passing it on to its members through higher regular and special assessments.<sup>298</sup> These new costs may prove too expensive for other innocent association members. Therefore, these costs may cause additional harm by forcing even more homeowners to default on assessment dues and walk away from their underwater properties.<sup>299</sup>

Another option would be to make the mortgagee lender bear the cost of delinquent assessments. The Nevada super lien priority approach shifts the cost to the lender who must "buy out" the HOA lien or have its own interest extinguished.<sup>300</sup> There is a good argument that this is an efficient and secure approach for associations to recoup their costs because the lender has a

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accomplishing postjudgment objectives, whether his fees are paid on an hourly or percentage basis.").

<sup>294</sup> Roger Chase, *HOA Collection Options: Lien Foreclosures vs. Money Judgments*, CONDO ASS'N (May 25, 2009, 9:56 AM), <http://www.condoassociation.com/blog/tabid/19257/bid/8954/HOA-Collection-Options-Lien-Foreclosures-vs-Money-Judgments.aspx> [<http://perma.cc/QX34-53WF>]. Chase explains that "[m]any attorneys specializing in homeowner association law recommend the lien foreclosure route because it is less expensive and typically more successful than a money judgment." *Id.*

<sup>295</sup> See *supra* Section II(A).

<sup>296</sup> Boyack, *supra* note 51, at 95.

<sup>297</sup> See Bromley, *supra* note 22, at 258; Boyack, *supra* note 51, at 78.

<sup>298</sup> See Collins, *supra* note 4.

<sup>299</sup> See CMTY. ASS'N LEADERSHIP LOBBY, *supra* note 228. One HOA board member recognizes the issue that raising assessments can drive other members into foreclosure. *Id.*

<sup>300</sup> See *SFR Investments Pool 1, LLC v. U.S. Bank*, 334 P.3d 408, 409–10 (Nev. 2014).

substantial motivation to pay this relatively small amount to protect its interest.<sup>301</sup> Proponents of the method state it is also fair, provided the lender has notice and the opportunity to protect its interest.<sup>302</sup> Institutional lenders typically have much greater resources than HOAs, and can internalize the external cost of paying their borrowers' delinquent dues much easier than a community association.<sup>303</sup> But as previously mentioned, this policy forces the lender to pay the debt of another when the lender has not committed any kind of wrongful act.<sup>304</sup>

Instead, the law could be structured so that the purchaser at the foreclosure sale bears the cost of the delinquent assessments. The Florida approach shifts the cost from the HOA to the purchaser by a statutory mechanism.<sup>305</sup> This method is likely superior to a money judgment on the original debtor, the HOA internalizing the debt, or cost shifting to the lender, because shifting the cost to the purchaser is both fair and financially practical.

Presumably, the purchaser has the resources to pay this relatively small additional cost, either through their own funds or through financing, since they are making an offer on the property. Therefore, this approach is more financially realistic than collecting the delinquent assessment directly from the original debtor. Also, the association's lien is taken out of competition with the lender's lien by the statutory imposition on the purchaser.<sup>306</sup> This bypassing of lien priority provides the HOA with a better chance of recouping its costs than in a first-in-time regime where its lien will usually be junior to a first mortgage.<sup>307</sup> Lastly, a lender's first mortgage or deed of trust survives extinguishment by an HOA foreclosure.<sup>308</sup> Therefore, this approach does not have the unjust result of forcing the lender to pay to maintain their interest, nor the negative economic consequences to borrowers of that approach.

## CONCLUSION

This Comment has analyzed three different jurisdictions with respect to HOA lien priority and whether the interest of a first mortgage or deed of trust may be extinguished under each.

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<sup>301</sup> See UNIF. COMMON INT. OWNERSHIP ACT § 3-116.

<sup>302</sup> See *SFR Investments*, 334 P.3d at 409–10.

<sup>303</sup> Vaughn, *supra* note 3, at 11.

<sup>304</sup> See *supra* Section II(B).

<sup>305</sup> FLA. STAT. ANN. § 720.3085 (West 2014); FLA. STAT. ANN. § 718.116 (West 2014).

<sup>306</sup> FLA. STAT. ANN. § 718.116 (West 2014).

<sup>307</sup> See *supra* Section II(C).

<sup>308</sup> FLA. STAT. ANN. § 720.3085 (West 2014); FLA. STAT. ANN. § 718.116 (West 2014).

Traditional first-in-time jurisdictions favor a lender's interest to the detriment of HOAs. Under a first-in-time regime, a lender's first mortgage usually takes priority over an association's lien, and therefore, is not extinguished by an HOA's foreclosure on the property in question. While this falls in line with the lender's interest, this means that an HOA's junior interest will usually be extinguished by a foreclosure sale by the lender because such a sale will not usually generate enough profits to satisfy both liens, especially in a troubled economy.

A similar situation arises if the HOA tries to foreclose on its lien because the first mortgage still has priority. This leaves associations with the less reliable option of seeking a money judgment against delinquent homeowners. Furthermore, lenders have no incentive to expedite foreclosure proceedings in such a jurisdiction, and may intentionally postpone initiating foreclosure in order to avoid paying HOA assessments.

Nevada's super lien priority statute and case law flips the balance of power completely in the HOA's favor. Under this regime, an association lien's super priority portion is afforded true priority. This allows an association to foreclose on the super priority portion and extinguish a first mortgage or deed of trust as a junior lien. This puts lenders at an HOA's mercy, and requires them to pay off the super lien portion of the HOA lien, or suffer the consequences of lien extinguishment.

Proponents of this approach argue that this has solved the financial problems for associations inherent in first-in-time type regimes, because it encourages the lender to expedite foreclosure proceedings and almost guarantees an association's ability to collect delinquent dues. However, it does so by arguably violating principles of fairness while generating negative policy consequences that could adversely affect borrowers' access to credit.

While not a perfect solution, the purchaser liability approach taken by Florida is a more balanced method, improving the chances of collection for an HOA while avoiding the drastic measure of extinguishment of a first mortgage. This regime is more equitable to both lenders and associations because it bypasses priority competition between the liens and instead attaches liability to the purchaser of the property at the foreclosure sale. Of the parties involved, only the purchaser has both the financial assets to accept the burden of the delinquent assessments and the freedom of choice to accept it.

This regime also addresses the problem of lender recalcitrance to institute foreclosure by doubling the super priority amount currently provided for under the UCIOA. When

such an increase occurs, a lender has more motivation to foreclose since the super priority is capped at the greater amount of twelve months or one percent of the mortgage debt.

However, the Florida approach to lender delay of foreclosure does not address when a lender is not considering buying the property if the HOA forecloses, or when the super priority period is already maxed out. One possible solution to lender delay of foreclosure under these circumstances is partial adoption of the 2014 UCIOA amendment providing for rolling liens. Under this amendment, an association is entitled to the super priority amount for each budget year for the association. Adoption of such an amendment would mean the statutory cap would continue to accrue, and a lender purchaser would be motivated to initiate foreclosure because its liability for assessments would continue to grow. However, this solution still does not address the situation of when a lender has decided it will not purchase the property in question.

Given the negative consequences discussed in affording lien priority to either the association or the lender by Nevada-type regimes and first-in-time jurisdictions respectively, states should give the search for a balanced approach to lien priority greater future consideration as they attempt to find an optimal solution to the HOA lien priority issue. Only by bringing transparency to the existence of the stacked deck can we determine how to make the system work for all involved. Only then, by finding the right balance, can we achieve the objectives of real estate law to provide an equitable and predictable system of lien priority.

