STATEMENT OF PRINCIPLES

HOA SUPER PRIORITY LIENS

Within state legislatures and the courts, a debate has been taking place over whether priority lien status should be granted to one private party over another private lienholder that has followed proper procedures to record a first lien. In some jurisdictions, the debate over "super priority" liens has even extended to whether or not the subordinately filed lien should be granted the ability to extinguish liens recorded first in time.

The trade association signatories to this statement affirm the following as their joint public policy position on super priority liens for common interest communities, including condominiums, planned communities, and real estate cooperatives (referred to here, collectively, as HOAs):

- We support the bedrock principle in real estate finance of "first in time, first in right," that any private lien secured after origination of a property's first lien mortgage or deed of trust should not take priority over that mortgage or deed of trust in foreclosure (i.e. "payment priority"), or have the ability to extinguish the mortgagee's interests (i.e. "true priority").

- We are opposed to policy initiatives that seek to give priority lien status to one private party ahead of another private lienholder that has followed proper procedures to record their lien. These initiatives run contrary to the very heart and nature of secured lending, and can destabilize the entire real estate finance system by undermining the value of the collateral securing a loan — resulting in higher costs that will ultimately be borne by consumers.

- If state policymakers decide to proceed contrary to this core principle and allow for an HOA super priority lien within their jurisdiction, this lien should exist as a payment priority that is satisfied from the proceeds of a foreclosure sale conducted by a superior lienholder or encumbrancer. At no time should this lien hold true priority status with the capacity to extinguish a mortgagee's superior interests in a property. Additionally, if a payment priority HOA super lien exists:

  - What is included within this lien must be expressly defined.

  - The associated costs must be reasonably limited. Included in the HOA super priority lien should only be the following:

    - Six months of delinquent regular assessments owed to the HOA by the homeowner, based on the HOA's current periodic budget year, and excluding special assessments;

    - An interest rate based on the lien amount that is commercially reasonable and based on interest rates for other collection actions; and

- Reasonable collection costs for the aforementioned six months of delinquent assessments, which should be defined by prescribed limits. The costs should be similar to amounts incurred in other collection actions, and must not be framed within generic statements of law — examples of generic statements of law include "attorney's fees" or "necessary costs."

- The maximum amount of an HOA super priority lien should be capped at one percent of the mortgage amount.

▪ An HOA's super lien should lose its payment priority status if the HOA sells its lien interest to a third party.

American Bankers Association
American Financial Services Association
Association of Mortgage Investors
Housing Policy Council of the Financial Services Roundtable
Mortgage Bankers Association
Securities Industry and Financial Markets Association Structured Finance Industry Group

APPENDIX

HOA SUPER PRIORITY LIENS

July 23, 2015

Issue History:

In 1982, the Uniform Law Commission (ULC) developed the *Uniform Common Interest Ownership Act* (UCIOA)[1] as model law. UCIOA contained language for the formation, management, and termination of common interest communities, including condominiums, planned communities, and real estate cooperatives (referred to here, collectively, as HOAs). Prior to UCIOA, the ULC developed related models in the late 1970s: the *Uniform Condominium Act* (UCA)[2] and the *Uniform Planned Community Act* (UPCA).[3] Since their creation, more than 20 jurisdictions have adopted variations of these acts or their amended versions — in whole or in part.[4]

Notably, the ULC suggested in each model that HOAs should hold a "super priority" lien on a property for several months of delinquent assessments. Typically, adopting jurisdictions have quantified the super priority lien as between six and nine months of unpaid amounts and related collection costs.

For decades, HOA super priority liens have been enforced as a "payment priority" from the proceeds of a foreclosure sale conducted by a superior lienholder or encumbrancer. However, in 2014 the Nevada Supreme Court[5] and the District of Columbia Court of Appeals[6] ruled that HOA super priority liens are "true priority" liens — meaning an HOA may conduct a foreclosure sale on this lien and if an otherwise superior lienholder or encumbrancer does not act to satisfy it, their otherwise advanced lien interest will be extinguished.

Existing Dangers:

These rulings[7] — shifting HOA super liens from a payment priority to a true priority — have created profound, unintended consequences for mortgage lenders, the servicers of their loans, and the housing industry at large:

- In a true priority jurisdiction, a relatively diminutive HOA super priority lien amount — likely totaling in the thousands of dollars — now has the capacity to wipe out a mortgage or deed of trust worth hundreds of thousands of dollars. In the prior noted Nevada Supreme Court case, an HOA foreclosure sale was executed for $6,000, in order to satisfy a delinquent $4,500 HOA super priority lien amount.[8] This resulted in a loss of $885,000 for the otherwise superior first lien mortgagee through lien extinguishment.

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[1] http://www.uniformlaws.org/Act.aspx?title=Common%20Interest%20Ownership%20Act%20(1982).

[2] http://www.uniformlaws.org/Act.aspx?title=Condominium%20Act.

[3] http://www.uniformlaws.org/Act.aspx?title=Planned%20Community%20Act.

[4] According to the ULC's website, as of July 23, 2015 nine states have adopted UCIOA: AK, CO, CT, MN, NV and WV (1982 version); and CT, DE and VT (2008 version). Additionally, 14 states have adopted UCA: AL, AZ, KY, ME, MN, MO, NE, NM, PA, RI, TX, VA, WA and WV. Pennsylvania has also adopted UPCA. However, it is likely that the ULC's aforementioned list is not definitive, given that Tennessee's existing condominium law and the District of Columbia's existing condominium law are both similarly structured to the UCA model and are not listed on the ULC's website.

[5] *SFR Investments Pool 1, LLC v. U.S. Bank, N.A.*

[6] *Chase Plaza Condominium Assoc. Inc. v. JPMorgan Chase Bank, N.A.*

[7] In 2012, a Washington State case — *Summerhill Village Homeowners Assoc. v. Roughley* — also established true priority for that State's HOA super liens. Note that these are state interpretations of their laws, and these decisions are only controlling in states where and when they are made.

[8] *See supra* note 5 (the specific lien amount owed ranged from $1,149.24 when the notice of delinquency was recorded to $4,542.06 when the notice of sale was sent).

- HOAs do not always provide appropriate notice to a superior lienholder or encumbrancer that a super priority lien amount is delinquent — resulting in mortgage servicers being unaware of lien concerns until well after the HOA foreclosure sale has been conducted. Inadequate state notice requirements exacerbate this problem.

- Even if a servicer does determine that a property is subject to an HOA super priority lien, communication with HOAs is often difficult. Most HOAs do not have current registered agent information on file with their secretary of state and less than 20 percent are managed by a professional company.

- Numerous "payoff" issues have also arisen, including HOAs improperly rejecting servicers' tender to satisfy the statutorily mandated super priority lien amount — in order to instead collect their full delinquent costs in foreclosure. In certain instances, some HOAs have even affirmatively refused to disclose to servicers the amount owed.

- Further, there is no mechanism to dispute the super priority lien amount purportedly owed by the homeowner, which essentially represents a private dispute with no judicial finding of the validity of the HOA's claim.

- Moreover, speculative investors have begun capitalizing on HOA foreclosure sales in order to experience windfall profits upon resale.

- Over 1,000 Nevada cases are being litigated to determine whether clear title existed for 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 under Nevada law and clear title exists, holders of first lien deeds of trust will lose hundreds of millions of dollars.

If other jurisdictions begin adopting a true priority standard, many of the aforementioned consequences will inevitably result there as well, leading to serious financial impacts that will directly harm consumers:

- Lenders in true priority jurisdictions will need to financially account for the risks related to possible extinguishment in order to continue originating mortgage loans. The impact this might have on a consumer's loan will depend on an individual lender's risk mitigation strategy. For example, a lender might price the related risk into higher interest rates, mitigate it through higher down payment requirements, or completely exit risky jurisdictions altogether. Inevitably, any option will have a negative impact on consumers seeking mortgage credit or refinance options in a time when the market is experiencing the lowest interest rates in decades. It may even impact homeowner property sales as consumers are offered less favorable loan terms for homes in HOA-managed areas.

- Aside from access to credit and property sale impacts, homeowners are also vulnerable to additional risks in a true priority jurisdiction. They could inadvertently lose their homes (and their hard-earned equity) in the course of an assessment dispute with their HOA. Added concerns arise when a homeowner is out of town, sick, etc. for an extended time period and inadvertently neglects to stay current on their HOA assessments. These concerns exist even if a homeowner is mortgage-free.

Notably, true priority HOA super liens significantly affect several public programs and federal government interests, including the Federal Housing Administration's (FHA) mortgage insurance program — which

helps create sustainable homeownership opportunities for first-time and low- to moderate-income homebuyers, and the Federal Housing Finance Agency's (FHFA) conservatorship of the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac). Given the magnitude of these concerns, numerous legal actions have been undertaken to challenge the appropriateness of true priority HOA super liens:

- In September 2014, the U.S. District Court for Nevada marginally limited the Nevada Supreme Court decision, barring HOA foreclosure sales on first lien deeds of trust in Nevada that are insured through FHA. The District Court held in *Washington and Sandhill Homeowners Association v. Bank of America N.A.* that the U.S. Constitution's Supremacy Clause bars foreclosure sales of this type and renders them invalid.

- Additionally, FHFA has directly intervened in several actions on this true priority issue. In June 2015, FHFA and Fannie Mae successfully challenged the ability of HOA super priority liens to extinguish federal government property interests in a case before the U.S. District Court for Nevada. In *Skylights LLC v. Byron et al*, FHFA and Fannie Mae did not dispute that recently upheld Nevada law allows an HOA's foreclosure of its super priority lien to extinguish an otherwise first position deed of trust if that lien is not properly satisfied by an otherwise superior lienholder or encumbrancer. However, FHFA and Fannie Mae counterclaimed that provisions of the federal *Housing and Economic Recovery Act of 2008* (HERA) prohibit an HOA from foreclosing on Fannie Mae's property interests without the consent of its conservator, FHFA. Given that FHFA did not consent to the extinguishment in question (and has publically stated it will not do so),[9] the District Court determined that the HOA's foreclosure sale did not extinguish Fannie Mae's property interests, nor allow the property to be conveyed free of this encumbrance.
  - Importantly, the District Court's decision included language indicating that the ruling could be limited to a scenario where Fannie Mae was the deed of trust's record beneficiary at the time of the HOA's foreclosure. However, three cases decided in July 2015 expanded the ruling to the more common scenario for Fannie Mae or Freddie Mac — where either own the debt but are not the recorded beneficiary of the deed of trust. These cases are *Elmer v. JPMorgan Chase Bank, N.A*; *Premiere One Holdings, Inc. v. Fed. Nat'l Mortg. Ass'n*; and *Williston Inv. Group, LLC v. JPMorgan Chase Bank, N.A.*

- While the aforementioned District Court decisions are not controlling in other jurisdictions, nor are other judges within the U.S. District Court for Nevada bound by these rulings, they do provide exceedingly favorable precedent for these arguments.

- Importantly, even if HOA super liens are eventually unable to extinguish FHFA and FHA property interests in any jurisdiction that adopts a true priority standard, loans made with private capital will remain vulnerable to extinguishment and investors will not have as much of an incentive to invest in homeownership, creating a major barrier to full housing market recovery and the ability of consumers to purchase homes in true priority states.

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[9] FHFA Statement on HOA Super-Priority Lien Foreclosures, *available at* http://www.fhfa.gov/Media/PublicAffairs/Pages/Statement-on-HOA-Super-Priority-Lien-Foreclosures.aspx (April 21, 2015).

Statement

Statement on HOA Super-Priority Lien Foreclosures

FOR IMMEDIATE RELEASE

4/21/2015

Title 12 United States Code Section 4617(j)(3) states that, while the Federal Housing Finance Agency acts as Conservator, "[no] property of the Agency shall be subject to levy, attachment, garnishment, foreclosure, or sale without the consent of the Agency." This law precludes involuntary extinguishment of Fannie Mae or Freddie Mac liens while they are operating in conservatorships and preempts any state law that purports to allow holders of homeownership association (HOA) liens to extinguish a Fannie Mae or Freddie Mac lien, security interest, or other property interest.

As noted in our December 22, 2014 statement on certain super-priority liens, FHFA has an obligation to protect Fannie Mae's and Freddie Mac's rights, and will aggressively do so by bringing or supporting actions to contest HOA foreclosures that purport to extinguish Enterprise property interests in a manner that contravenes federal law. Consequently, FHFA confirms that it has not consented, and will not consent in the future, to the foreclosure or other extinguishment of any Fannie Mae or Freddie Mac lien or other property interest in connection with HOA foreclosures of super-priority liens.

12/22/2014: **Statement of the Federal Housing Finance Agency on Certain Super-Priority Liens**

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The Federal Housing Finance Agency regulates Fannie Mae, Freddie Mac and the 12 Federal Home Loan Banks. These government-sponsored enterprises provide more than $5.6 trillion in funding for the U.S. mortgage markets and financial institutions. Additional information is available at **www.FHFA.gov**, on Twitter **@FHFA**, **YouTube** and **LinkedIn**.

Contacts:

Media: Corinne Russell (202) 649-3032 / Stefanie Johnson (202) 649-3030

Consumers: **Consumer Communications** or (202) 649-3811

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Statement

Statement of the Federal Housing Finance Agency on Certain Super-Priority Liens

FOR IMMEDIATE RELEASE

12/22/2014

Today, the Federal Housing Finance Agency (FHFA) is alerting homeowners, financial institutions, and state authorities of the agency's concerns with state-level actions that threaten the first-lien status of single-family loans owned or guaranteed by Fannie Mae and Freddie Mac. In particular, FHFA is concerned about state actions to create super-priority liens in two instances: 1) through certain energy retrofit financing programs structured as tax assessments and 2) through granting priority rights in foreclosure proceedings for homeowner associations. In issuing this statement, FHFA is acting in furtherance of its statutory obligations as regulator and conservator of Fannie Mae and Freddie Mac.

The existence of these super-priority liens increases the risk of losses to taxpayers. Fannie Mae and Freddie Mac, while operating in conservatorship, currently support the housing finance market by purchasing, guaranteeing, and securitizing single-family mortgages. One of the bedrock principles in this process is that the mortgages supported by Fannie Mae and Freddie Mac must remain in first-lien position, meaning that they have first priority in receiving the proceeds from selling a house in foreclosure. As a result, any lien from a loan added after origination should not be able to jump in line ahead of a Fannie Mae or Freddie Mac mortgage to collect the proceeds of the sale of a foreclosed property. However, as is detailed below, FHFA is concerned by some liens being advanced to "super-priority" status over Fannie Mae and Freddie Mac first-lien mortgages.

Energy Retrofit Financing Programs Structured as Tax Assessments

While FHFA fully supports energy retrofit financing programs to allow homeowners to improve energy efficiency, these programs must be structured to ensure protection of the core financing for the home and, therefore, cannot undermine the first-lien status of Fannie Mae and Freddie Mac mortgages. Some entities and localities are advancing the argument that single-family energy retrofit financing programs that are structured to make loans through the homeowner's property tax assessment and require that borrowers repay their loans as part of their property tax bill should have priority over all other loans, including pre-existing Fannie Mae and

Freddie Mac mortgages.1 One such program is known as the Property Assessed Clean Energy (PACE) program, which often provides loans as first-liens and is offered in California and in some other states. Localities offering these PACE loans threaten to move existing Fannie Mae and Freddie Mac mortgages to a second lien position and increase the risk of loss to the Enterprises and, by extension, to taxpayers.

In issuing this statement, FHFA wants to make clear to homeowners, lenders, other financial institutions, state officials, and the public that Fannie Mae and Freddie Mac's policies prohibit the purchase of a mortgage where the property has a first-lien PACE loan attached to it. This restriction has two potential implications for borrowers. First, a homeowner with a first-lien PACE loan cannot refinance their existing mortgage with a Fannie Mae or Freddie Mac mortgage. Second, anyone wanting to buy a home that already has a first-lien PACE loan cannot use a Fannie Mae or Freddie Mac loan for the purchase. These restrictions may reduce the marketability of the house or require the homeowner to pay off the PACE loan before selling the house.

FHFA believes it is important for states and municipalities to understand these restrictions before continuing to offer the programs. Additionally, FHFA believes that borrowers should fully understand these restrictions prior to taking out a first-lien PACE loan.

In addition to aggressive enforcement of these existing policies, FHFA is continuing to explore other possible remedies and legal actions to protect the Enterprises' lien position in response to first-lien PACE programs.

Homeowner Association Priority Status

FHFA is aware that, in certain jurisdictions, liens for unpaid homeowner association ("HOA") dues may be deemed to be senior to preexisting mortgage liens on a homeowner's property. As a result, on December 5, 2014, FHFA and Fannie Mae filed an action in federal court in Nevada, seeking a determination that a HOA's foreclosure sale is invalid and contrary to federal law to the extent that it purports to extinguish Fannie Mae's property rights. *Federal National Mortgage Association v. SFR Investments Pool 1, LLC*, No. 2:14-cv-02046 (D. Nev. December 5, 2014). FHFA has also intervened in *Saticoy Bay, LLC Series 1702 Empire Mine v. Federal National Mortgage Assoc.,* No. 2:14-cv-01975 (D. Nev.), seeking a declaration that a prior HOA foreclosure sale is invalid to the extent that it purports to extinguish Fannie Mae's property interests.

These FHFA actions are based on federal law which precludes involuntary extinguishment of liens held by Fannie Mae or Freddie Mac while they are operating in conservatorships and bars holders of other liens, including HOAs, from taking any action that would extinguish a Fannie Mae or Freddie Mac lien, security interest or other property interest. Specifically, Title 12 USC Section 4617(j)(3) states that "[no] property of the Agency shall be subject to levy, attachment, garnishment, foreclosure, or sale without the consent of the Agency, nor shall any involuntary lien attach to the property of the Agency." FHFA is authorized, as conservator, to bring this suit because Enterprise lien interests in collateral constitute property protected by this provision.

FHFA has an obligation to protect Fannie Mae's and Freddie Mac's rights, and will aggressively do so by bringing actions to void foreclosures that purport to extinguish Enterprise property interests in a manner that contravenes federal law.

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1 PACE financing programs can be structured as secondary liens that stand behind the original mortgage and do not threaten the priority status of Enterprise loans.

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Contacts:

Stefanie Johnson (202) 649-3030 / Corinne Russell (202) 649-3032

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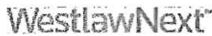

27-31-210. Lien for unpaid assessments; right of mortgagee or purchaser acquiring title at foreclosure sale.
de of Laws of South Carolina 1976 Annotated Title 27. Property and Conveyances *(Approx. 2 pages)*

NOTES OF DECISIONS (3)

In general
Regime fees

Code of Laws of South Carolina 1976 Annotated
Title 27. Property and Conveyances
Chapter 31. Horizontal Property Act
Article 1. General Provisions

Code 1976 § 27-31-210

§ 27-31-210. Lien for unpaid assessments; right of mortgagee or purchaser acquiring title at foreclosure sale.

Currentness

(a) All sums assessed by the administrator, or the board of administration, or other form of administration specified in the bylaws, but unpaid, for the share of common expenses chargeable to any apartment shall constitute a lien on such apartment prior to all other liens except only (i) tax liens on the apartment in favor of any assessing unit, and (ii) mortgage and other liens, duly recorded, encumbering the apartment. Such lien may be foreclosed by suit by the administrator, or the board of administration, or other form of administration specified in the bylaws, acting on behalf of the council of co-owners, in like manner as a mortgage of real property. In any such foreclosure the apartment owner shall be required to pay a reasonable rental for the apartment after the commencement of the foreclosure action and the plaintiff in such foreclosure shall be entitled to the appointment of a receiver to collect such rents. The administrator, or the board of administration, or other form of administration specified in the bylaws, acting on behalf of the council of co-owners, shall have the power to bid in the apartment at foreclosure sale and to acquire and hold, lease, mortgage and convey the same. Suit to recover a money judgment for unpaid common expenses may be maintainable without instituting foreclosure proceedings.

(b) Where the mortgagee of any mortgage of record or other purchaser of an apartment obtains title at the foreclosure sale of such a mortgage, such acquirer of title, his successors and assigns, shall not be liable for the share of the common expenses or assessments by the co-owners chargeable to such apartment accruing after the date of recording such mortgage but prior to the acquisition of title to such apartment by such acquirer. Such unpaid share of common expenses or assessments shall be deemed to be common expenses collectible from all of the apartment owners, including such acquirer, his successors and assigns.

Credits

HISTORY: 1962 Code § 57-514; 1967 (55) 449.

Notes of Decisions (3)

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Code 1976 § 27-31-210, SC ST § 27-31-210
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