

Contractor's Claim Trumps Lender
in Mechanic's Lien Lawsuit

by

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The Southern District of the Missouri Court of Appeals recently decided that a contractor's mechanic's lien had priority over a bank's construction loan. This is an important decision because contractors and lenders often find themselves fighting over a financial pie that is too small to serve both of them.

The case is *Grau Contracting, Inc. v. Captiva Lake Investments, LLC*, 2014 WL 911339, decided March 10.

The dispute involved the Majestic Pointe condominium development located on a multi-acre point that jutted into the Lake of the Ozarks. In 2005 the developer had nearly finished one condo building and planned to start the next. The project's lender, however, decided not to continue financing the additional construction.

National City Bank agreed to finance finish work on the existing building and construction of another high-rise, plus interior finish on three units in a separate condominium tower with a \$20,000,000 construction loan secured by a deed of trust.

The development was not successful. Various material suppliers and contractors filed mechanics' liens and actions to recover for work performed on the condominium tower after the bank had recorded its deed of trust. This included Missouri Builders Service, Inc., Questec Constructors, Inc., Butler Supply, Inc., House of Carpet, Inc. and Meyer Electric Company.

Thereafter, Captiva Lake Investments bought the bank's construction loan, foreclosed on the deed of trust, acquired the property and was substituted for the bank in the mechanic's lien litigation.

The question at trial and on appeal was whether the mechanics' liens filed by the various contractors had priority over the bank's construction loan.

The trial court decided that pursuant to Missouri's "first spade rule" the contractors had priority over the bank's deed of trust. The first spade rule is a court-created rule. It provides that all mechanics' liens are deemed to have

commenced on the date when the first contractor did the first work, be it the “first stroke of the axel or spade.”

The liens continue throughout the project but each separate lien claimant must file its own lien within six months of its last item of work. Priority is important because there often is not enough money to pay everyone. Those in the front of the line get paid first.

The Court of Appeals elaborated that the priority of the mechanic’s lien will vary based on the type of property. A mechanic’s lien on land is given relation-back priority under Missouri law, whereas a mechanic’s lien on a building is given complete priority. As to the land, a deed of trust recorded after the commencement of work on a project is inferior to any mechanic’s lien relating to that land.

Captiva argued on appeal that Section 443.055 of Missouri’s statutes, which covers future advance deeds of trust (rather than mechanic’s liens), forms a statutory exception to the first spade rule.

Captiva acknowledged before the appellate court that some recent Missouri cases seem to hold that construction liens are inferior to mechanics’ liens even when considering Section 443.055. In part, this section provides that the deed of trust is a priority lien that dates from the time the deed is recorded and has priority over others including by inference contractors.

Captiva argued on appeal that no Missouri case has directly considered whether Section 443.055 “trumps the first spade rule.” The appellate court noted that the bank knew at the time of its construction loan that a multi-building project already was in progress and that this loan was being used to finance the construction of a condominium tower and to complete unfinished units in a separate building.

The appellate court, agreeing with the trial court, found that Captiva could not divide the improvement into phases for the purpose of obtaining a priority.

The appellate court also affirmed the trial court’s decision to award several of the contractors 14% prejudgment interest pursuant to Section 431.180. This section allows a court to award in a construction case a prevailing party reasonable attorney fees and interest up to 18%, in the court’s discretion.

Missouri’s general statute on prejudgment interest sets the rate at 9%. The appellate court noted that it gives great deference to the decision of the trial court and did not find the award of the 14% interest to be unreasonable.

Missouri Builders argued on appeal that the trial court awarded only 9% post-judgment interest, which was inconsistent with the 14% for prejudgment

interest. The Southern District affirmed this result, stating it did not “shock our sense of justice.”

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