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The Weitz Company, LLC v. Heth

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SYNOPSIS: Subrogation can't overcome the statutory priority of a mechanics lien.

The Weitz Company, LLC v. Heth, 314 P3d 569 (Ariz. App. 2013)

Summit borrowed $54 million from Arizona National Bank on a construction loan to develop a 165-unit condo project. Summit hired Weitz as its general contractor, but failed to pay Weitz the full amount of the contract. After 92 of the units were sold, Weitz filed a mechanics lien claim, which under the applicable statute related back to the date construction began. The statute, Ariz. Rev. Stat. 33-992A, provides that:

> The liens provided for in this article ... are preferred to all liens, mortgages or other encumbrances upon the property attaching subsequent to the time the labor was commenced or the materials were commence to be furnished [except for construction loan deeds of trust].

The buyers of the units and the lenders that had made purchase-money loans thus found themselves subordinate to Weitz's mechanics lien claim. They argued that, since their payments had gone in part to pay the construction loan, they should be subrogated to its priority, and thus to have priority over Weitz's mechanics lien claim.

There were several problem with this argument that the court did not address. First, the construction loan had not been fully paid off from the proceeds of sale of the 92 units. Generally, subrogation will not be granted for a partial payoff of a preexisting lien, since doing so has the result of bifurcating the lien. This is like a court creating a sort of involuntary loan participation among parties who have no participation agreement and no unity of interest, and it is apt to result in serious conflicts among those parties. The courts generally are simply unwilling to foist such a situation upon them.

Second (and also not addressed by the court), there were multiple purchasers of the condo units. If they were granted subrogation, would they all have equal priority? Should subrogation ever be granted where there are multiple payers of the prior lien? Once again, wouldn't this result in a sort of loan participation among them – perhaps not involuntary, since they all wanted this result, but still problematic? We don't know the answer to this, since the court doesn't discuss it.

The court bases its decision instead on the literal language of the mechanics lien statute, quoted above. Since the statute gives the lien claimant priority over "all liens,

mortgages or other encumbrances upon the property attaching subsequent to the time the labor was commenced," that's the end of the matter. The principle of subrogation can't override the statutory language, no matter how equitable it might be to do so. Two previous Arizona cases had recognized subrogation in a similar context, but the court disagrees with them: *Lamb Excavation, Inc. v. Chase Manhattan Mortgage Corp.*, 95 P.3d 542 (App.2004); and *Peterman–Donnelly Eng'rs & Contractors Corp. v. First Natl Bank of Ariz.*, 408 P.2d 841 (1965). The court notes that several other states have agreed with its approach, including Alabama, Nevada, Indiana, and Utah.

COMMENT: The court follows the statute literally, but its interpretation is by no means the only way of reading the statute. If the condo buyers' and lenders' interests are thought of as (by way of subrogation) "attaching" when the construction loan was made – that is, they "related back" by way of subrogation – then they would have priority over the mechanic's lien, since the construction deed of trust was recorded before work began. Under this view, there are two "relation backs" -- the mechanic lien (to the date construction commenced) and the condo buyers' and lenders' interests (to the date the construction deed of trust was recorded, which was earlier). But the court refused to stretch the meaning of the word "attach" in this manner.

In a sense, the underlying problem here is the "secret lien" aspect of mechanics liens. They can exist in an unrecorded and unfindable form from the date construction begins until they are filed in the public records, which in many states can be up to six months after completion of construction. I would argue that no civilized society would permit such liens. But I must admit that contractors, lumber yards, and others in the construction industry love 'em, and their political weight is sufficient that we are unlikely to see the "secret" aspect of mechanics liens disappear any time soon.

In Arizona, the "secrecy" of the lien isn't quite as secret as in many states, for the statute requires the lien claimant to have filed a preliminary twenty-day mechanic's lien notice at the time construction began. See A.R.S. § 33–992.01. Weitz had made such a filing. Thus, the condo buyers, if they had checked the public records, would at least have know that Weitz *might* be planning to file a mechanics lien. If they (or their title companies) had been more careful, perhaps when they purchased their units they would have sought lien waivers, a bond, or other assurance from Weitz that they were not going to be primed by a lien subsequently recorded by Weitz.