

The Intersection of Bankruptcy and Construction Law:

{ Liens, Discharge, and Other Considerations

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“Just as no plan of battle survives first contact with the enemy, it appears no plan of construction survives first contact with the elements.”

{ General Construction Company v. Public Utility District No. 2 of Grant County, 195 Wn. App. 698 (2016).

- ⌘ Automatic Stay
- ⌘ Property of the Estate
- ⌘ Claims
- ⌘ Executory Contracts
- ⌘ Discharge and Exceptions to Discharge
- ⌘ Preferences
- ⌘ Among other Possible Issues

Building Blocks: Bankruptcy Issues in the Construction Context

Deadlines

Federal & State Laws

Mechanics Liens and Bankruptcy:

RCW 60.04.021: Lien Authorized: "Except as provided in RCW 60.04.031, any person furnishing labor, professional services, materials, or equipment for the improvement of real property shall have a lien upon the improvement for the contract price of labor, professional services, materials, or equipment furnished at the instance of the owner, or the agent or construction agent of the owner."

Pre-claim Notice May be Required

RCW 60.04.031 (notice requirement, subject to exceptions)

Lien Authorized | State Law

Notice of Claim of Lien; RCW 60.04.091: "Every person claiming a lien under RCW 60.04.021 shall file for recording, in the county where the subject property is located, a notice of claim of lien not later than ninety days after the person has ceased to furnish labor, professional services, materials, or equipment"

Enforcement Action. RCW 60.04.141: "No lien created by this chapter binds the property subject to the lien for a longer period than eight calendar months after the claim of lien has been recorded unless an action is filed by the lien claimant within that time in the superior court in the county where the subject property is located to enforce the lien, and service is made upon the owner of the subject property within ninety days of the date of filing the action"

. . . . and in case the action is not prosecuted to judgment within two years after the commencement thereof, the court, in its discretion, may dismiss the action for want of prosecution."

Notice of Claim & Enforcement Action

Owner Files Bankruptcy

Broadly Staying:

“any act to create, perfect or enforce any lien against property of the estate” 11 U.S.C. § 362(a)(4)

“any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title” 11 U.S.C. § 362(a)(5)

{ Automatic Stay |
11 U.S.C. § 362(a)(4),(5)

Subject to Narrow Exceptions:

*“The filing of a petition . . . does not operate as a stay . . . of any act to **perfect, or to maintain or continue the perfection of, an interest in property** to the extent that the trustee’s rights and powers are subject to such perfection under section 546(b) of this title or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title”*

{ 11 U.S.C. § 362(b)(3)

§ *“In other words, ‘act[s] to perfect an interest in property’ as defined by 11 U.S.C. § 546(b) are exempted from the automatic stay.”*

Miner Corporation v. Hunters Run Limited Partnership (In re Hunters Run Limited Partnership), 875 F.2d 1425, 1428 (9th Cir 1989).

The Automatic Stay | 11 U.S.C. § 362

- ↳ "This section allows creditors with certain types of liens to avoid the potential prejudice of section 362's automatic stay by allowing for post-bankruptcy petition perfection of these liens."

Miner Corporation v. Hunters Run Limited Partnership (In re Hunters Run Limited Partnership), 875 F.2 1425, 1428 (9th Cir. 1989).

The Automatic Stay | 11 U.S.C. § 362

- ↳ Turns on State Law.

- ↳ **Relation Back | RCW 60.04.061:** *"The claim of lien created by this chapter upon any . . . land shall be prior to any . . . encumbrance which attached to the land after or was unrecorded at the time of commencement of labor or professional services or first delivery of materials or equipment by the lien claimant."*

- ↳ Recording (in WA) | Perfection

- ↳ Must Comply with Statutory Time Requirement.

Creation v. Perfection: When Does the Lien Arise

- ↳ **Notice in Lieu of Commencement | 11 U.S.C. § 546(b)(2)**

- ↳ **Lien Duration, RCW 60.04.141:** *"This is a period of limitation, which shall be tolled by the filing of any petition seeking protection under Title Eleven, United States Code by an owner of any property subject to the lien established by this chapter."*

- ↳ Extension of Time | 11 U.S.C. § 108(c).

- ↳ Lift Stay

Perfection v. Enforcement: Preserving Lien

Issue: Whether a mechanics lien claim expired under Washington law.

Holding: No, “11 U.S.C. § 108(c) tolled the enforcement period.”

“[A] Washington lien is ‘perfected’ once the claim has been properly recorded Commencement of foreclosure proceedings . . . is not an element of ‘perfection’ exempted from section 362’s stay by section 546(b); rather, it is ‘enforcement’ which remains stayed by section 362. Consequently, section 108(c) applies to toll the enforcement period”

{ *Miner Corporation v. Hunters Run Limited Partnership* (In re Hunters Run Limited Partnership), 875 F.2d 1425 (9th Cir. 1989).

See, e.g., *O’Malley Lumber Co. v. Lockard (In re Lockard)*, 884 F.2d 1171 (9th Cir. 1989): concluding “that the surety bond at issue in th[e] case is not ‘property of the estate,’ within the meaning of 11 U.S.C. § 541” such that the “state court action” against the surety was not “subject to the automatic stay”

Payment Bond | Automatic Stay

- ⌚ **Discharge**
- ⌚ **Certain Exceptions Include:**
 - ⌚ False pretenses, false representation, or actual fraud | 11 U.S.C. § 523(a)(2)(A);
 - ⌚ Fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny | 11 U.S.C. 523(a)(4); and
 - ⌚ Willful and malicious injury | 11 U.S.C. § 523(a) (6).
- ⌚ **Construed Narrowly**
- ⌚ **Action Required; Attention to Deadline**

Discharge & Possible Exceptions in the Construction Context

⌚ **Issues may arise with:**

⌚ Pay applications, trust funds, certifications, diverting funds, and other facts

⌚ **Fact Specific Inquiry under Federal and State Law**

⌚ **Wickam v. Ivar (In re Werner)**, 817 Fed. Appx. 432 (9th Cir. July 23, 2020)

Exceptions to Discharge: Examples

{ THANK YOU