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Illinois Decision on Lien Priorities

November 16, 2011 by Jeffrey L. Hamera

The Illinois Supreme Court in *La Salle Bank N.A. v. Cypress Creek 1, LP* has issued an opinion clarifying the relative priorities of a lender and mechanic's lien claimants to the proceeds of a foreclosure sale where the lender's mortgage was recorded before the mechanic's liens attached. The only other pertinent fact is that the sale proceeds were insufficient to satisfy the mortgage and the mechanic's liens. The court held that a lender has priority to the value of the property at the time the construction contract was entered into, plus the value of the improvements that were paid for out of the construction loan secured by the mortgage. The state Supreme Court concluded a mechanic's lien holder has priority only to the value of the improvements for which it has not been paid. This case expressly overruled *Mitchell v. Robinovitz*, which allowed a lien claimant's priority claim to include the value of all improvements, including those provided by others. Despite the court's analysis of existing case law, the dissent criticized the majority opinion because it "does not apply the statute's plain language."

This case does not address projects encumbered by a mortgage recorded after the construction contract is executed. However, the state Supreme Court left the door open for a lender that records after the date of a construction contract to claim equitable subrogation rights arising from payments that it advances for the work of that contract, and thereby claim priority to that part of the value of the improvements. Despite stating that it avoided reaching the lender's claim of equitable subrogation based on the amounts that it paid for construction, the court's rationale is not at odds with an equitable subrogation claim.

Senate Bill 1564, referred to the Senate Assignments Committee, would modify Section 16 of the Mechanics Lien Act, to effectively parallel the reasoning in *Cypress Creek*. Therefore, the law of relative priorities of mechanic's liens and construction mortgages in Illinois remains unsettled and may undergo further changes and interpretations in the near future.