



*A Division of Ohio Bar Title Insurance Company
A First American Company*

TITLE ALERT

Title Alert 2012-09

May 21, 2012

Mechanics' Lien Risk for Construction Mortgages

Purpose: To disseminate new standards of review for issuance of title insurance policies providing mechanics' lien coverage resulting from a recent Superior Court decision.

Background: The Superior Court of Pennsylvania has held that an open-end mortgage recorded after commencement of construction on the mortgaged property does not have statutory priority over mechanics' liens unless all of the proceeds of the loan are used to pay the costs of completing erection, construction, alteration or repair of the mortgaged premises. In *Commerce Bank/Harrisburg, N.A. v. Kessler*, 2012 WL 1610139 (Pa.Super.), decided on May 9, 2012, the Superior Court held that a lien filed by a contractor had priority over an open-end construction mortgage when (a) work on the property commenced prior to the recording of the mortgage, and (b) some of the proceeds of the mortgage were used to pay off a mortgage, judgments, real estate taxes and closing costs.

Section 1508(c) of the Mechanics' Lien Law provides that a lien of a contractor or subcontractor is subordinate to "An open-end mortgage as defined in 42 Pa.C.S. §8143(f) . . . , the proceeds of which are used to pay all or part of the cost of completing erection, construction, alteration or repair of the mortgaged premises secured by the open-end mortgage." [49 Pa.C.S. §1508(c)(2)] The Superior Court in *Kessler* interpreted that provision to mean that a mechanics' lien would be subordinate to an open-end mortgage only if **all of the proceeds** from the open-end mortgage are used to pay the cost of completing erection, construction, alteration and repair of the mortgaged premises secured by the open-end mortgage.

Part of our current underwriting standard for providing mechanics' lien coverage was to treat an open-end mortgage that is used to pay the costs of construction as a "safe harbor". Due to the *Kessler* case, such standard is being revised as set out below.

Standard: Special underwriting will be required if you are requested to provide mechanics' lien coverage on a loan policy insuring an open-end construction mortgage, or it is determined that construction **has already commenced** or it is anticipated that construction **will commence prior to recording the mortgage**. Please contact us immediately and be sure to report this on your title application.

WARNING: this Underwriting Communication is intended solely for the employees of Penn Attorneys/Ohio Bar Title Insurance Company and its Approved Attorneys, and is not to be distributed to third parties, and any reliance by any other person or entity is unauthorized. This Underwriting Communication is intended solely for the purpose of underwriting policies of Ohio Bar Title Insurance Company.

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