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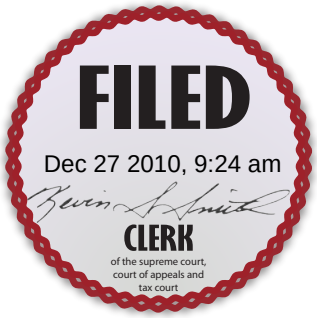

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IN THE
COURT OF APPEALS OF INDIANA

McINTYRE BROTHERS, INC.,	)	
Appellant,	)	
	)	
vs.	)	No. 47A01-1004-PL-172
	)	
KIM D. HENDERSON, MELINDA J. HENDERSON,	)	
SYDNEYCO, LLC, FIFTH THIRD BANK and	)	
LAWRENCE COUNTY TREASURER,	)	
Appellees.	)	

APPEAL FROM THE LAWRENCE SUPERIOR COURT
The Honorable William E. Vance, Special Judge
Cause No. 47D01-0402-PL-178

December 27, 2010

MEMORANDUM DECISION - NOT FOR PUBLICATION

BAILEY, Judge

Case Summary

Fifth Third Bank ("Fifth Third") loaned $945,000 to Kim and Michele Henderson ("the Hendersons"), paying off two prior mortgages at closing. Fifth Third failed to discover a mechanic's lien held by McIntyre Brothers, Inc. ("McIntyre"). In subsequent foreclosure proceedings, lien priority was disputed, with Fifth Third claiming that the doctrine of equitable subrogation granted priority to the $311,000 paid to satisfy a mortgage held by Stone City Bank ("Stone City") over McIntyre's mechanic's lien. In partial summary judgment proceedings, the trial court agreed. After a bench trial, the trial court denied McIntyre foreclosure of its mechanic's lien, granted McIntyre judgment against the Hendersons, and prioritized the entirety of the $945,000 Fifth Third mortgage lien over McIntyre's judgment lien. McIntyre appeals. We affirm in part, reverse in part, and remand.

Issues

McIntyre presents two issues for review, which we re-order and restate as follows:

I. Whether the trial court erroneously granted partial summary judgment to Fifth Third upon finding the doctrine of equitable subrogation applicable to Fifth Third's payoff of the Stone City mortgage; and

II. Whether the validity of McIntyre's mechanic's lien was an issue reserved for trial.

Facts and Procedural History

In 2001, the Hendersons purchased commercial property located in Bedford, Indiana, where a Dollar General Store and Subway Restaurant were operated. In April of 2002, the buildings were destroyed by fire and the Hendersons hired McIntyre to clean up debris. McIntyre eventually constructed a new building on the property. Around the time that

construction began, the Hendersons obtained a mortgage on the property from Stone City. The mortgage was recorded on September 23, 2002.

The Hendersons transferred ownership of the property to Sydneyco, a limited liability corporation, and McIntyre billed Sydneyco for construction work. McIntyre submitted invoices totaling $1,565,139.59, a portion of which was paid. On August 15, 2003, McIntyre recorded its Notice of Intention to Hold Mechanic's Lien for the unpaid balance of the invoices.

On August 22, 2003, Fifth Third loaned $945,000 to Sydneyco and $100,000 to another company owned by the Hendersons. At the real estate closing on that date, the Hendersons executed mortgage documents in their individual capacity but deeded the property to Sydneyco. Fifth Third paid off the two liens that had been discovered by their title company, specifically, $311,706.18 to Stone City and $187,275.48 to the Poling Trust. McIntyre's lien had not been discovered, and Fifth Third did not disburse funds to McIntyre.[1]

Fifth Third recorded two mortgages on August 25, 2003. In 2004, Fifth Third prepared a Corrective Mortgage and Security Agreement to reflect the fact that Sydneyco had owned the property as of the date of the August 22, 2003 closing. The corrective mortgage was recorded on September 1, 2004.

On February 16, 2004, McIntyre filed a complaint for breach of contract, unjust enrichment, and foreclosure of a mechanic's lien, naming as defendants the Hendersons,

[1] After receiving excess funds at closing, Melinda Henderson delivered a Sydneyco check for $492,000 to McIntyre.

Sydneyco, LLC, Fifth Third Bank, and the Lawrence County Treasurer. Fifth Third filed a counterclaim, cross-claim, and third-party claim, in part asserting that the Hendersons had committed fraud in the execution of a Mortgagor's Affidavit. The proceedings were stayed when, in March of 2006, Sydneyco filed for Chapter 11 bankruptcy protection. McIntyre filed a Proof of Claim indicating that it held a secured claim, a mechanic's lien, against Sydneyco. After litigation, the Bankruptcy Court determined that Sydneyco owed McIntyre $560,000 as opposed to the $807,842.27 claimed.

The case became active again in the Lawrence Superior Court on November 21, 2008, when Fifth Third filed a Motion for Scheduling Conference. Fifth Third subsequently filed a motion for partial summary judgment. Oral argument was heard on September 2, 2009, at which the Hendersons argued their lack of individual liability because of a novation, and Fifth Third requested a determination that equitable subrogation applied to prioritize its mortgage lien, to the extent that the funds had been used to pay off the Stone City mortgage.[2] McIntyre claimed that Fifth Third was not entitled to equitable subrogation, due to its culpable negligence in failing to discover the mechanic's lien and in lending to individuals rather than the corporate owner of the subject property.

On September 16, 2009, the trial court issued an order finding for Fifth Third and against the Hendersons on the issue of novation. With respect to McIntyre, the trial court entered partial summary judgment in Fifth Third's favor:

[2] Fifth Third conceded that factual issues precluded summary judgment as to whether equitable subrogation was applicable to The Poling Trust mortgage it had paid off. According to counsel for Fifth Third, "there is almost no good evidence as to how the proceeds of how that second mortgage, the Pulling [sic] Trust loan were applied. They're right about that because it's the summary judgment stage we don't have that evidence." (Tr. 15.)

> The Court finds for Fifth Third Bank and against McIntyre Brothers, Inc. on the question of priority as it relates to the funds expended to retire the Stone City Bank mortgage.
>
> Specific amounts are to be determined.

(App. 22.)

The matter proceeded to trial on September 23, 2009. By this time, Fifth Third had obtained dismissal of its fraud claim against the Hendersons but was pursuing a personal judgment against them and also a judgment of foreclosure. As for the equitable subrogation claim, counsel for McIntyre and Fifth Third jointly advised the trial court: "the bank is not proceeding today by agreement on any claim that the Poling Trust mortgage, which some of the documents relate to, has a priority over the McIntyre lien." (Tr. 35.) Fifth Third submitted its Exhibits 13 and 18, detailing interest that would correspond to a principal balance of $311,706.18 (attributable to the Stone City mortgage).

On January 21, 2010, the trial court issued a judgment of foreclosure inconsistent with its prior partial summary judgment order that had applied the doctrine of equitable subrogation. The trial court awarded McIntyre judgment against Sydneyco in the amount of $560,000 but determined that McIntyre had not perfected its mechanic's lien. Accordingly, Fifth Third was granted foreclosure of a mortgage lien equal to the $916,003.66 principal balance on the current Fifth Third mortgage, plus interest (superior to McIntyre's judgment lien). The trial court also decreed that Fifth Third's claim for repayment of real estate taxes was to be prioritized over McIntyre's judgment lien. This appeal ensued.

Discussion and Decision

I. Partial Summary Judgment – Equitable Subrogation

McIntyre argues that partial summary judgment was erroneously granted, having been premised upon the trial court's misapprehension of the law regarding equitable subrogation. Pursuant to Indiana Trial Rule 56(C), summary judgment is appropriate when there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. On review of a trial court's grant or denial of summary judgment, this Court applies the same standard as the trial court. Best Homes, Inc. v. Rainwater, 714 N.E.2d 702, 705 (Ind. Ct. App. 1999). Neither the trial court nor the reviewing court may look beyond the evidence specifically designated to the trial court. Id.

Fifth Third claimed only that it was entitled to partial summary judgment with regard to the amount of the Stone City mortgage satisfied by refinancing. The designated evidence and the arguments of counsel at the summary judgment hearing reveal that the parties asserted that they held competing liens and that their point of contention primarily distilled to conflicting interpretations of statutory and common law regarding equitable subrogation.

Indiana Code Section 32-28-3-1 provides that a contractor who has performed labor or furnished materials may have a lien to the extent of the value of any labor done or the material furnished. The historical origin and purpose of the mechanic's lien statutes was to make a property owner an involuntary guarantor of payments for the reasonable value of improvements made to real estate by the physical labor or materials furnished by laborers or materialmen. Ford v. Culp Custom Homes, Inc., 731 N.E.2d 468, 472 (Ind. Ct. App. 2000),

trans. denied. In order to acquire a lien upon the property, the party seeking the lien must timely file a sworn statement of his intention to hold a lien in the recorder's office of the county in which the relevant real estate is located. Id. To enforce a lien, the lienholder must timely file suit to foreclose the lien. Id.

Indiana Code Section 32-21-4-1, addressing the priority of recorded transactions, provides that "[a] conveyance, mortgage, or lease takes priority according to the time of its filing." A mechanic's lien is not rendered superior to the lien of a prior recorded mortgage by the fact that the security of the latter is increased by the improvement. See Thorpe Block Sav. & Loan Ass'n v. James, 13 Ind. App. 522, 522, 41 N.E. 978, 978 (1895). According to the time of recordation, the Stone City and Poling Trust mortgages were superior to McIntyre's mechanic's lien. Fifth Third has claimed that it is entitled to "step into the shoes" of the Stone City mortgage under the doctrine of equitable subrogation.

The doctrine of equitable subrogation has existed alongside the recordation statutes and is, consistent with its name, grounded in equity. Neu v. Gibson, 928 N.E.2d 556, 560 (Ind. 2010). "The doctrine substitutes one who fully performs the obligation of another, secured by a mortgage, for 'the owner of the obligation and the mortgage to the extent necessary to prevent unjust enrichment.'" Id. (quoting Restatement (Third) of Property § 7.6(a) (1997)). The substitution avoids an inequitable application of the general principle that priority in time gives a lien priority in right. Id.

The classic formulation of the doctrine would permit a purchaser of a note and mortgage to be accorded a right of subrogation to the mortgage discharged, including its

priority over junior liens, where the purchaser did not have actual knowledge and where he or she was not culpably negligent in failing to learn of the junior lien. Bank of New York v. Nally, 820 N.E.2d 644, 653 (Ind. 2005). However, the Nally Court (agreeing with the Restatement position "at least in the context of a conventional refinancing") revised this formulation, placing the focus not upon notice but rather upon whether or not the junior lienholder was prejudiced by subrogation:

> Precluding equitable subrogation when a mortgagee discovered or could have discovered a junior lien holder runs contrary to the purposes underlying the doctrine. Equitable subrogation is a remedy to avoid an unearned windfall. . . . Neither negligence nor constructive notice of an existing lien is relevant to whether the junior lien holder will be unjustly enriched or prejudiced.

Id. Application of the doctrine of equitable subrogation will depend on the "equities and attending facts and circumstances of each case." Id. at 654. Mere negligence that causes no harm will not result in an unexpected elevation of priority status; however, "culpable negligence," which is some action or inaction amounting to more than mere inadvertence, mistake or ignorance, may support the opposite result. Id. at 654-55.

McIntyre has also identified authority it deems persuasive for the proposition that a subsequent lender cannot invoke equitable subrogation to gain priority over a prior-recorded mechanic's lien. In Ex parte Lawson, 6 So.3d 7, 14 (Ala. 2008), the Alabama Supreme Court declared that "the constructive notice supplied by the materialman's lien statute defeats the lenders' equitable-subrogation claim" and "that to hold otherwise would violate the equitable maxim that equity follows the law." In Alabama, a recognized element of equitable subrogation is that the "lender must be ignorant of the intervening lien." Id. at 12. However,

as previously discussed, the Nally Court's adoption of the Restatement position removed the focus away from constructive notice, and the Court explained that constructive notice was irrelevant to the issue of unjust enrichment or whether a "junior lienholder" was prejudiced.[3] Nally, 820 N.E.2d at 623.

Finally, McIntyre points out that Nally involved competing mortgages, and argues that when a lien priority dispute includes a mechanic's lien, the trial court's discretion is circumscribed by Indiana Code Section 32-29-1-11(d). This statutory provision, enacted in 2003 (when the common law focus was upon actual or constructive notice) and amended in 2005,[4] now provides:

> Except for those instances involving liens defined in IC 32-28-3-1 [mechanic's lien], a mortgagee seeking equitable subrogation with respect to a lien may not be denied equitable subrogation solely because:
>
> (1) the mortgagee:
> (A) is engaged in the business of lending; and
> (B) had constructive notice of the intervening lien over which the mortgagee seeks to assert priority;
> (2) the lien for which the mortgagee seeks to be subrogated was released; or
> (3) the mortgagee obtained a title insurance policy.

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[3] The Lawson Court, in dicta, stated that a mechanic's lien falls within an exception as set out in the Restatement (Third) of the Law of Property § 7.6, cmt. f, Illustration 30. Lawson, 6 So.3d at 15. The referenced illustration concludes with the language "[a] court is warranted in finding that a grant of subrogation to Mortgagee-2 would be unjust to Mechanic, and upon such a finding may deny Mortgagee-2's subrogation claim." (emphasis added.) It does not, however, mandate a finding for a mechanic's lienholder irrespective of the equities.

[4] In 2003, the General Assembly enacted conflicting versions of subsections (d) and (e). P.L. 122-203 included (e) but omitted the phrase "except for those instances involving liens defined in IC 32-28-3-1" at the beginning of subsection (d), while P.L. 151-2003 conversely included the reference to IC 32-28-3-1 at the start of subsection (d) and omitted the reference to mechanic's liens in subsection (e). The General Assembly reconciled the conflicting versions by emergency legislation effective April 25, 2005. P.L. 2-2005 "corrected and amended" the statute to read as set forth herein.

Subsection (e) provides that "[s]ubsection (d) does not apply to a municipal sewer lien under IC 36-9-23 or a mechanic's lien under IC 32-28-3-1." According to McIntyre, the intent of the Legislature was to "allow courts to deny requests for equitable subrogation as to mechanic's liens based solely upon either one of these factors." Appellant's Brief at 20. McIntyre then argues that two circumstances present in this case, constructive notice and Fifth Third's purchase of title insurance, precluded a grant of summary judgment to Fifth Third.

The interpretation of a statute is a legal question that is reviewable de novo. Avemco Ins. Co. v. State ex rel. McCarty, 812 N.E.2d 108, 115 (Ind. Ct. App. 2004). The goal of statutory construction is to determine and implement legislative intent. Fort Wayne Patrolmen's Benev. Ass'n v. City of Fort Wayne, 903 N.E.2d 493, 497 (Ind. Ct. App. 2009), trans. denied. We read all sections of an act and strive to give effect to all provisions. Id. "We will not read into a statute that which is not the manifest intent of the legislature. For this reason, it is as important to recognize not only what a statute says, but also what a statute does not say." Cox v. Cantrell, 866 N.E.2d 798, 809 (Ind. Ct. App. 2007) (citation and quotation marks omitted), trans. denied. The statute here at issue provides that, as to liens that are neither municipal sewer or mechanic's liens, equitable subrogation "may not be denied" solely because of specified circumstances. It does not state the converse; it does not mandate the denial of equitable subrogation in one of the specified circumstances.

Regardless of the origin of the lien asserted, when an equitable remedy is pursued, it becomes the task of the trial court to examine the "equities and attending facts and

circumstances." See Nally, 820 N.E.2d at 653. This includes any evidence of culpable negligence by the party asserting that equitable intervention is necessary to prevent unjust enrichment. The refinancing mortgagee's actual or constructive knowledge of intervening liens is irrelevant and so does not automatically preclude a court from applying equitable subrogation. See id. at 654. The relevant inquiry is whether the holder of the intervening lien was prejudiced. See id.

At the time that McIntyre began to supply materials and perform work, Stone City held a recorded mortgage on the subject property, which McIntyre would have expected to be superior to its own mechanic's lien. McIntyre was placed in no worse position when Fifth Third paid off Stone City's mortgage and later asserted an equitable right to "step into the shoes" of the Stone City mortgage. At the summary judgment stage, McIntyre identified no genuine issue of material fact that would have precluded partial summary judgment for Fifth Third.

McIntyre now claims that there is a genuine issue as to Fifth Third's "culpable negligence." The facts and circumstances surrounding the Fifth Third mortgage transaction have not been disputed. McIntyre essentially claims that the totality of these undisputed facts rise to the level of culpable negligence. No designated evidence indicates that Fifth Third's conduct amounted to more than mere inadvertence, mistake, or ignorance. The trial court properly granted partial summary judgment to the effect that a portion of the Fifth Third mortgage lien, specifically that attributable to the Stone City mortgage payoff, is superior to McIntyre's mechanic's lien.

II. Validity of Mechanic's Lien

The decree of foreclosure made no specific reference to equitable subrogation, nor did the trial court determine what portion of Fifth Third's mortgage was entitled to priority under the doctrine. The trial court dissolved McIntyre's lien – absent a motion by any party – because of an ostensible failure of proof as to when the work was performed relative to the recordation. The foreclosure decree stated in relevant part:

> McIntyre Brothers failed to prove by a preponderance of the evidence that its Notice of Intention to Hold a Mechanics Lien was recorded against the Real Estate within the ninety-day period required by statute in order to perfect the mechanics lien which McIntyre Brothers has asserted in this case.

(App. 24.) McIntyre asserts that the validity of its mechanic's lien was not an issue reserved for resolution by the trial court at the bench trial, inasmuch as Fifth Third had not sought to dissolve the mechanic's lien and the parties had uniformly taken the position in bankruptcy and summary judgment proceedings that McIntyre held a lien and the dispute was with regard to priority of liens. The record supports McIntyre's contention. For example, at the summary judgment hearing Fifth Third's counsel advised the trial court:

> I'm here to talk about the issue of priority. We have competing liens against this building in Bedford. My client has a mortgage attached to that building. The Plaintiff McIntyre Brothers has a mechanic's lien attached to that building.

(Tr. 13.) (emphasis added.) Although "arguments of counsel are not evidence that trial courts may consider when making factual determinations," nevertheless "a clear and unequivocal admission of fact by an attorney is a judicial admission which is binding on the client." In re K.H., 838 N.E.2d 477, 480 (Ind. Ct. App. 2005).

In turn, the trial court's partial summary judgment order included its determination "on the question of priority." (App. 22.) (emphasis added.) The reference to priority presumes the existence of competing liens; the parties proceeded to bench trial under such an assumption. A sua sponte challenge to the validity of the mechanic's lien and the ensuing outcome is akin to trial by ambush. We therefore reverse the order of foreclosure which decreed that McIntyre had no mechanic's lien.

We remand for further proceedings consistent with the partial summary judgment order (which concluded that, under the doctrine of equitable subrogation, the amount of the Stone City mortgage has priority over the mechanic's lien) and with this opinion.

Affirmed in part, reversed in part, and remanded.

RILEY, J., and KIRSCH, J., concur.