



Step Carefully When Crossing a Texas Minefield

Mechanic's Lien and Bond Claims in Texas

The first mechanic's lien law in Texas was passed in 1839, when the Congress of the Republic of Texas enacted "An Act for the Relief of Master Builders and Mechanics of Texas."¹ The Texas Constitution of 1869 first created the constitutional mechanic's lien in Texas.² Today, Chapter 53 of the Texas Property Code sets forth harrowingly detailed procedures for asserting mechanic's lien claims.³ Given the many changes in the relevant constitutional and statutory provisions over the past 175 years, and the difficult objective of providing protection to all segments of the construction industry, the mechanic's lien laws in Texas are extraordinarily complex. The key to crossing this minefield is simple: one step at a time.

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The underlying premise of Texas lien law has always been to protect contractors, suppliers and subcontractors by giving them a claim or interest in the property to the extent of the value of the improvement to ensure that the property owner does not receive the added value without paying for it. For contractors and suppliers seeking protection against non-payment, there is an array of legal issues to consider. In order to protect their rights against private property owners, or sureties in the case of bonded public or private projects, contractors and suppliers must comply with extremely technical statutory requirements.

The applicable deadlines and other statutory requirements are set forth in: (1) the Texas Property Code for work performed or materials provided to private property owners;⁴ (2) the Texas Government Code for work performed or materials provided to state and local governments or their agencies;⁵ and (3) the Federal Miller



Act for work performed or materials provided on federal government construction projects.⁶ Unpaid subcontractors and suppliers may also have a claim under the Texas Construction Trust Fund Statute, regardless of whether the subcontractor or supplier has complied with the procedural requirements of the mechanic's lien laws.⁷

It would be impossible to provide on these few pages a comprehensive review of every potential issue impacting creditors on Texas construction projects. The purpose of this article is to address some of the basic concepts and requirements associated with asserting lien and bond claims on Texas construction projects.⁸

Lien Filing Deadlines

The original contractor⁹ is not required to provide any preliminary notices to assert a lien claim. The only requirement for the original contractor to perfect a claim is the timely filing of a lien affidavit. To assert a lien claim, an original contractor, as well as a subcontractor and/or materialman (as discussed below), must "file an affidavit with the county clerk of the county in which the property is located...not later than the 15th day of the fourth calendar month after the day on which the indebtedness accrues."¹⁰ The indebtedness for an original contractor accrues on the last day of the month during which the "written declaration" that terminates the contract is received, or "on the last day of the month in which the original contract has been completed, finally settled or abandoned."¹¹ In other words, the debt accrues on the last day of the month following termination of the contract or completion of the project.

For lien filing purposes, the indebtedness for a subcontractor or materialman accrues “on the last day of the last month” in which labor was performed or material was furnished.¹² For a supplier, the date of actual physical delivery to the project site controls, not the date that title technically transferred to the customer, for purposes determining when the supplier must file its lien claim.¹³

Derivative Claimants: Preliminary Notice

In addition to filing the appropriate lien affidavit, subcontractors and materialmen must also give certain preliminary notices in order to perfect their lien claim.¹⁴ Under Section 53.056 of the Texas Property Code: “[i]f the lien claim arises from a debt incurred by a subcontractor, the claimant must give to the original contractor written notice of the unpaid balance...not later than the 15th day of the second month following each month in which all or part of the claimant’s labor was performed or material delivered.”¹⁵ This preliminary notice provision does not apply to first tier subcontractors who have a direct contractual relationship with the original contractor since the original contractor is already on notice that payment is past due.

Fund Trapping Notice

If the subcontractor or materialman continues to remain unpaid, then the claimant must give written notice of the unpaid balance to “the owner or reputed owner and the original contractor *not later than the 15th day of the third month* following each month in which all or part of the claimant’s labor was performed or material or specially fabricated material was delivered.”¹⁶ This notice is commonly referred to as the “fund trapping notice” and the purpose is twofold:

- (1) to “trap” funds in the owner’s hands; and
- (2) to assert a claim against the statutory retainage.

In order to trap funds in the hands of the owner, this notice must state that “if the claim remains unpaid, the owner may be personally liable and the owner’s property may be subjected to a lien unless:

- (1) the owner withholds payments from the contractor for payment of the claim; or
- (2) the claim is otherwise paid or settled.¹⁷

Chapter 53, Subchapter D of the Texas Property Code permits owners who receive a fund trapping notice to withhold from payments to the original contractor the amount claimed by a subcontractor.¹⁸ The owner may withhold this amount immediately upon receipt of the notice.¹⁹

Enforcement

A lawsuit to foreclose the lien must be brought within two (2) years after the last day the claimant may file the lien affidavit or within one (1) year after completion of the project, whichever is later.²⁰

Statutory Retainage

Texas law also provides for statutory retainage, which requires the owner to withhold ten percent (10%) of the original contract price for thirty (30) days after the project has been completed.²¹ This retainage is used to satisfy subcontractors’ claims toward the end of the project when funds cannot be properly trapped.

Generally, in order to have a claim against statutory retainage, the claimant must send all notices required by Chapter 53 and file a lien affidavit “not later than the 30th day after the earliest of the date: (A) the work is complete; (B) the original contract is terminated; or (C) the original contractor abandons performance under the original contract.”²²

While recording a lien in order to perfect a claim is not prohibited by the automatic stay, bringing suit to enforce the lien is a violation of the automatic stay.

The 2011 Texas Legislature extended the deadline for filing lien affidavits on statutory retainage in some instances, as well as contractual retainage. Prior to 2011, Section 53.106(b)(6) provided that the lien must be filed not later than the 30th day after the date of completion. Now, if an owner files an affidavit of completion, the lien must be filed not later than the 40th day after the date of completion. Similarly, prior to 2011, Section 53.107(b)(7) provided that the lien must be filed not later than the 30th day after the date of termination or abandonment.

Now, if an owner provides notice of termination or abandonment, the lien must be filed not later than the 40th day after the date of termination or abandonment.

Effect of Bankruptcy

If an owner or contractor files bankruptcy, the automatic stay prevents third parties from taking actions against the debtor or property of the bankruptcy estate.²³ As discussed above, the Texas Property Code requires lien claimants to give notice and record liens within specific time limits in order to perfect a lien. Fortunately, Bankruptcy Code Section 362(b)(3) specifically provides that the automatic stay does not operate as a stay “of any act to perfect, or to maintain or continue the perfection of, an interest in property.” This provision alleviates the hardship of the automatic stay by incorporating the provisions of 11 U.S.C. § 546(b) which permits mechanics and materialmen to perfect their liens post-petition simply by “giving notice within the time fixed by...state law.”²⁴

Some courts have held that filing of notice of a secured claim in the bankruptcy case is sufficient to perfect a state law lien claim under Section 546.²⁵ However, to ensure perfection of a lien claim after a bankruptcy petition is filed a claimant should

follow all notice provisions provided for by state law, as well as file notice of a secured claim in the bankruptcy proceeding. Lien claimants should also beware that the filing of a bankruptcy petition does not extend the time for filing the lien affidavit, so the state law time limits discussed above apply.²⁶

While recording a lien in order to perfect a claim is not prohibited by the automatic stay, bringing suit to enforce the lien is a violation of the automatic stay. If the deadline to file suit to foreclose the lien occurs during the pendency of the bankruptcy, then the lien claimant still has 30 days after the bankruptcy case is closed (“termination or expiration of the stay”) to file suit because the state law cause of action is tolled by virtue of Bankruptcy Code 11 U.S.C. § 108(c).

As a general rule, the automatic stay applies only to the debtor and no other members of the construction chain. Thus, in the case of an owner’s bankruptcy, an unpaid subcontractor could proceed against the general contractor or the surety under a payment bond.

At least one Texas court has concluded that the statutory lien requirements for a commercial project continue to apply even after the home is sold to individuals who intend to reside there.

Sale or Foreclosure of Property

A mechanic’s or materialman’s lien claim may only be foreclosed judicially. To prevail, the lien claimant must file a lawsuit and obtain a judgment that forecloses the lien, and orders a sale of the property subject to the lien.

Claims against the Leasehold

Courts in Texas “have long held that a mechanic’s and materialman’s lien attaches to the interest of the person contracting for construction.”²⁷ Accordingly, when a lessee contracts for construction, any resulting mechanic’s lien attaches only to the leasehold interest and not to the fee interest of the lessor.²⁸ Unless the owner of the land is also a party to the construction contract or the lessee is acting as the authorized agent of the lessor, no mechanic’s lien attaches to the fee estate.²⁹ The critical issue, therefore, becomes whether the fee owner authorized the work.

Specially Fabricated Materials

When a materialman or subcontractor manufactures materials specially fabricated for a particular project, and thus cannot be returned to inventory for resale, then the manufacturer may assert a lien claim even though the owner or contractor may have canceled the order before delivery of the materials. To perfect a claim for undelivered specially fabricated materials, the materialman or subcontractor must give the owner and the original contractor notice not later than the 15th day of the second month after the month in which the claimant

receives and accepts the order for the materials.³⁰ The claimant must also provide notices and file a lien affidavit as discussed above.

Claims against the Homestead

The Texas Constitution provides special protections for the homestead, which are meant to protect the citizens of Texas from losing their homes.³¹ Homesteads are generally protected from forced sale for the payment of debts, except for those debts specifically enumerated in the constitution, which include debts incurred for purchase money on the homestead, for taxes owed thereon, and for work or services performed thereon.³² Because the homestead protection does not extend to debts incurred for improvements made to the homestead, laborers may secure valid mechanic’s and materialman’s liens against the homestead on which the work was performed, but only by following certain constitutional and statutory procedures.³³ Subcontractors and suppliers making improvements on a homestead must comply with the requirements found in Section 53.254 of the Texas Property Code in order to attach a valid lien.³⁴

This article does not include all of the many requirements necessary to perfect a claim against a homestead. However, some of the requirements are set forth below.

Prior to labor or material being furnished, the owner and spouse must execute a written contract which is filed with the county clerk.³⁵ Before the residential construction contract is executed, the original contractor must deliver to the owner a disclosure statement including language mandated by the Texas Property Code regarding the owners’ rights and responsibilities.³⁶

Furthermore, claimants asserting claims against a homestead must include additional language mandated by the Texas Property Code in their fund trapping notice letter.³⁷ This fund trapping notice letter, which includes the additional statutory warnings, must be sent to the owner or reputed owner and to the original contractor on a residential construction project on or before the 15th day of the second month following each month in which the claimant performed all or part of the labor or delivered material or specially fabricated material.³⁸

Next, the lien affidavit must be filed by the 15th day of the third calendar month after the day on which the indebtedness accrues, which is one month earlier than the general lien filing deadline for non-residential projects.³⁹ The lien affidavit must contain the following notice in 10-point boldface type at the top of the page: “NOTICE: THIS IS NOT A LIEN. THIS IS ONLY AN AFFIDAVIT CLAIMING A LIEN.”⁴⁰

Residential Construction

There are certain additional requirements for residential construction projects that apply regardless of whether the property constitutes a homestead. Section 53.256 requires the original contractor to provide a detailed list of subcontractors

and suppliers the original contractor intends to use on the project.⁴¹ As that list changes, the contractor is obligated to update the information no later than the 15th day after the date the subcontractor or supplier is added or deleted.⁴² An owner may waive the right to receive this list only if the waiver conspicuously makes the disclosures outlined in the statute.⁴³ However, failure to comply with these provisions does not invalidate a properly perfected statutory lien.⁴⁴

It is common in the construction industry for a contractor or developer to build several homes, then sell the homes to individuals who intend to live there as their homestead before the construction is complete. This creates an interesting question as to which statutory lien provisions apply—the rules that relate to a commercial project, since the project at its inception was a commercial project, or the rules applicable to a residential construction project. At least one Texas court has concluded that the statutory lien requirements for a commercial project continue to apply even after the home is sold to individuals who intend to reside there.⁴⁵ The court reasoned that since the purchaser had personal knowledge of improvements being made to the home before purchasing it, then the purchaser had sufficient notice of the contractor's right to assert a mechanics' lien claim under Texas law.

Payment and Bond Claims

Payment bonds provide another potential remedy available to general contractors, subcontractors, and materialmen to ensure they receive payment for the services and materials they provide to a construction project. The type of project will determine the applicable law covering payment bond claims on the project. As a practical matter, the payment bond effectively functions as an insurance policy purchased by the general contractor to insure subcontractors and materialmen are paid.

An owner of a private project may require an original contractor to furnish a payment bond against which claims may be asserted. These types of claims are governed by Chapter 53 of the Texas Property Code.

State and local public works projects are those in which a local or state governmental or quasi-governmental authority or entity is the owner of the property being improved or the party awarding the prime contract. These entities include: cities, counties, water and utility districts, river authorities, school districts, state owned colleges and universities, and agencies and departments of the State of Texas. With respect to public projects, Texas law prohibits lien claims, but requires payment bonds to protect unpaid contractors. Chapter 2253 of the Texas Government Code governs these types of claims. Similar to the procedures regarding Texas mechanic's liens set forth above, there is a vast and complicated array of notices and deadlines required to perfect payment bond claims under Texas law.

Federal public works projects are those in which the United States Government, including any of its agencies or depart-

ments, is the owner of the project or is the party awarding the contract to the general contractor. These types of claims for contracts are governed by the Federal Miller Act.⁴⁶

The Texas Construction Trust Fund Statute

In addition to bond and lien claims, unpaid subcontractors and suppliers may also have a claim under the Texas Construction Trust Fund Statute. The Texas Legislature adopted the Trust Fund Statute to provide an additional protection for laborers and materialmen.⁴⁷ The statute "discourage[s] contractors from engaging in the customary practice of paying the last job's expenses with the next job's financing."⁴⁸ The Trust Fund Statute "imposes fiduciary responsibilities on contractors to ensure that subcontractors, mechanics and materialmen are paid for work completed."⁴⁹

Construction payments become trust funds if they are "made to a contractor or subcontractor or to an officer, director, or agent of a contractor or subcontractor, under a construction contract for the improvement of specific real property in this state."⁵⁰ An individual who furnishes labor or materials under such a contract is a "beneficiary" of the trust funds.⁵¹ The trustee, in turn, is a "contractor, subcontractor, or owner or an officer, director, or agent of a contractor, subcontractor, or owner, who receives trust funds or who has control or direction of trust funds."⁵² Under the Trust Fund Statute, a trustee is liable for misapplication of trust funds if he "intentionally or knowingly or with intent to defraud, directly or indirectly retains, uses, disburses, or otherwise diverts trust funds without first fully paying all current or past due obligations incurred by the trustee to the beneficiaries of the trust funds."⁵³

New Rules Regarding Texas Highway Construction Projects

Pursuant to legislation enacted in 2005, the Texas Department of Transportation (TxDOT) has the ability to enter Comprehensive Development Agreements (CDA) for the purpose of completing highway construction projects. According to TxDOT, a CDA is "the tool TxDOT uses to enable private development by sharing the risks and responsibilities of design and construction."⁵⁴ Significantly, CDAs can alter the deadlines for asserting claims in connection with TxDOT projects, giving rise to potential catastrophes for subcontractors and suppliers who have simply followed the familiar protocol laid out under the Texas Government Code.

Under Section 223.205 of the Texas Transportation Code, in negotiating CDAs, TxDOT can require typical payment and performance bonds, or an alternative form of security, such as a letter of credit.⁵⁵ When TxDOT authorizes an alternative form of security, the claims process can vary from project to project based on the requirements set forth in the security documents. Subcontractors and suppliers performing work on TxDOT projects should carefully review the requirements set forth in the applicable CDA.

1. Act of Jan. 23, 1839, 3rd Cong., Repub. Tex. Laws, reprinted in 2 H.P.N. Gammel, THE LAWS OF TEXAS 1822–1897, at 66 (Austin, Gammel Book Co. 1898).
2. Tex. Const. of 1869, art. XII, § 47.
3. TEX. PROP. CODE ANN. §§ 53.001 et seq. (Vernon).
4. *See id.*
5. TEX. GOV'T. CODE ANN. §§ 2253.001 et seq. (Vernon).
6. 40 U.S.C.A. §§ 3131, 3132. (West).
7. TEX. PROP. CODE ANN. §§ 162.001 et seq.
8. The information included in this article is for informational purposes only, and nothing herein should be in any way construed as constituting legal advice. An attorney should always be consulted regarding specific legal questions.
9. The original contractor has a direct relationship with the property owner. The original contractor can also be referred to as the “prime contractor” or the “general contractor.”
10. TEX. PROP. CODE ANN. § 53.052(a).
11. *See id.* § 53.053(b).
12. *See id.* § 53.053(c).
13. S.A. Maxwell Co. v. R.C. Small & Associates, Inc., 873 S.W.2d 447, 452 (Tex. App.—Dallas 1994 writ denied).
14. TEX. PROP. CODE ANN. §§ 53.056 - 53.058.
15. *See id.* § 53.056(b) (emphasis added).
16. *See id.*
17. *See id.* § 53.056(d).
18. *See id.* § 53.081(a).
19. *See id.* § 53.081(b).
20. *See id.* § 53.158(a).
21. *See id.* § 53.101(a).
22. *See id.* § 53.103.
23. 11 U.S.C. § 362.
24. 11 U.S.C. § 546(b) (2004).
25. *See In re Village Properties*, 723 F.2d 441 (5th Cir. 1984).
26. *See Knopler v. Addison Bldg. Material*, 149 B.R. 522 (N.D. Ill. 1993).
27. *Commercial Structures & Interiors, Inc. v. Liberty Educ. Ministries, Inc.*, 192 S.W.3d 827, 835 (Tex.App.—Fort Worth 2006, no pet.) (quoting *Diversified Mortgage Investors v. Lloyd D. Blaylock Gen. Contractor, Inc.*, 576 S.W.2d 794, 805 (Tex.1978)).
28. *See 2811 Assocs. Ltd v. Metroplex Lighting & Elec.*, 765 S.W.2d 851, 853 (Tex.App.—Dallas 1989, writ denied).
29. *Inman v. Orndorff*, 596 S.W.2d 236, 238 (Tex.Civ.App.—Houston [1st Dist.] 1980, no writ).
30. TEX. PROP. CODE ANN. § 53.058(b).
31. TEX. CONST. ART. XVI, § 50.
32. *Id.* § 50(a)(1), (2), (5).
33. *Id.* § 50(a)(5); TEX. PROP.CODE ANN. § 53.254.
34. TEX. PROPCODE ANN. § 53.254.
35. *See id.* § 53.254(a).
36. *See id.* § 53.255.
37. *See id.* § 53.254(g).
38. *See id.* § 53.252(b).
39. *See id.*
40. *See id.* § 53.254(f).
41. *See id.* § 53.256.
42. *See id.*
43. *See id.* § 53.256(b).
44. *See id.* § 53.256(c).
45. *See Texas Wood Mill Cabinets, Inc. v. Butter*, 117 S.W.3d 98 (Tex. App.—Tyler 2003, no pet.).
46. 40 U.S.C. § 3131.
47. *RepublicBank Dallas, N.A. v. Interkal, Inc.*, 691 S.W.2d 605, 607 (Tex. 1985); *see also C & G, Inc. v. Jones*, 165 S.W.3d 450, 454 (Tex. App.—Dallas 2005, pet. denied) (“Chapter 162 was enacted to give protection to materialmen in addition to that provided by the materialman’s liens statutes.”).
48. *North Tex. Operating Eng’rs Health Benefit Fund v. Dixie Masonry*, 544 F.Supp. 516, 520 (N.D. Tex. 1982).
49. *In re Waterpoint Int’l LLC*, 330 F.3d 339, 345 (5th Cir. 2003).

50. TEX. PROP. CODE ANN. § 162.001(a).

51. *See id.* § 162.003.

52. *Id.* § 162.002.

53. *Id.* § 162.031(a).

54. Texas Department of Transportation, *Current Comprehensive Development Agreements*, <http://www.txdot.gov/business/partnerships/current-cda.html> (last visited Feb. 14, 2013).

55. *See* TEX. TRANSP. CODE ANN. § 223.205 (“the department shall require a private entity entering into a comprehensive development agreement under this subchapter to provide a performance and payment bond or an alternative form of security...”).

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