

# LEGAL VIEWS

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## Colorado's Trust Fund Statute Remains Important Tool for Recovery in the Construction Industry

By *Harvey L. Kramer, Esq.*

Colorado's mechanic's lien law provides a comprehensive statutory scheme intended to ensure payment of contractors, material suppliers and others who provide labor and materials for real property improvements ("Claimants"). The mechanic's lien law prevents unjust enrichment of a property owner who fails to pay for real property improvements.

The ability to file and enforce mechanic's liens against real property is a limited remedy subject to specific deadlines. Colorado law generally requires that the Claimants record a mechanic's lien within six months of completion of the project ("Mechanic's Lien Deadline"). Property owners often require a general contractor ("Contractor") to obtain a bond for the project to prevent the filing of mechanic's liens. The posting of a bond prohibits Claimants from filing mechanic's liens. If the Contractor defaults on payment, the Claimants' rights are limited to filing a claim against the bond. Generally, such claim must be filed within six months of the project's completion ("Bond Claim Deadlines"). Likewise, what is commonly known as the "Homeowner's Defense" prohibits the recording and enforcement of mechanic's liens against residential property that has already been sold to a consumer

In situations where no bond is in place and/or the real property has already been sold to a consumer, and the Contractor had misapplied money received for the project, property owners and Claimants faced the potential of incurring substantial losses. The property owner faced the prospect of paying twice for the same real property improvements because of the

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recording of mechanic's liens. If the property had been sold to a consumer, Claimants were left only with a breach of

### *Ideas \* News \* Resolutions*

**Craig Fleishman** recently represented the wife of a prominent physician and was able to achieve a very favorable result for her in a dissolution of marriage action.

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**Steve Shapiro** and **Craig Fleishman** obtained a successful ruling by the Colorado Court of Appeals, affirming the decision of the trial court in a matter where they obtained a multi-million dollar jury verdict on behalf of a client who suffered a traumatic brain

injury as a result of a motor vehicle collision. The briefs to the Court of Appeals were prepared by **Katherine Karamalegos Kust**.

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**Steve Shapiro** and **Craig Fleishman** successfully negotiated a seven figure settlement on behalf of a client who sustained a traumatic brain injury and severe headaches as a result of a motor vehicle collision where liability was in dispute.

contract claim against the Contractor. Potentially, the Contractor could then file bankruptcy and discharge the debts owed to the property owners or Claimants.

To provide protection against dishonest Contractors, Colorado adopted what is commonly known as the Trust Fund Statute. The Trust Fund Statute imposes a fiduciary duty on a Contractor to hold construction proceeds in trust for the benefit of Claimants and property owners ("Trust Funds"). The misappropriation of Trust Funds is considered a felony for theft under Colorado's criminal statute. The Trust Fund Statute prevents Contractors from discharging debts in bankruptcy to property owners and Claimants if such debts arise from the misappropriation of Trust Funds.

Until recently, the law under the Trust Fund Statute seemed relatively clear. A Contractor who received full payment on a construction project could not misappropriate Trust Funds, retain the benefit of the Trust Funds and discharge the resulting debts in bankruptcy.

Then, a Federal District Court held that a Contractor's fiduciary duties expired under the Trust Fund Statute if Claimants failed to record and enforce a mechanic's lien within the Mechanic's Lien Deadline ("Decision"). In other words, the Contractor could steal the Trust Funds and incur no liability whatsoever simply because a Claimant did not record a mechanic's lien within six months of the project's completion.

The Decision sent shockwaves throughout the Colorado construction industry. In practice, Claimants commonly refrained from recording and enforcing mechanic's liens for legitimate business reasons. A lien-happy supplier could damage its reputation with merchant homebuilders by delaying sales due to unresolved mechanic's liens. In the ordinary progression of construction projects, property owners, Contractors and lenders often insist on periodic lien releases as a condition of moving forward. When Contractors act dishonestly, Claimants and

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*The misappropriation of Trust Funds is considered a felony for theft under Colorado's criminal statute.*

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property owners often negotiate compromises to prevent mechanic's lien filings and/or attempt to work out repayment arrangements with the dishonest Contractor. Finally, because of the Homeowner's Defense, the Claimant providing work at the end of the Project could lose the right to record a mechanic's lien and simultaneously its claim in bankruptcy against the Contractor merely because of when it provided its labor or materials.

On appeal, the Tenth Circuit certified to the Colorado Supreme Court the ques-

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## F&S Focus: Harvey L. Kramer



Mr. Kramer's practice emphasizes practical, creative and aggressive representation of the firm's clients in the areas of commercial, real estate, construction, creditors' rights, and bankruptcy litigation.

He attended the University of Denver College of Law where he graduated as member of the *Order of St. Ives*, was a member and editor of the *Denver University Law*

*Review*, and received awards of academic excellence in Criminal Law, Bankruptcy and Conflicts of Law.

Mr. Kramer has handled a variety of successful trials and appeals in state and federal courts. Prior to joining Fleishman & Shapiro, he successfully represented a major client in a commercial litigation matter involving the entrustment and sale of motor vehicles under Colorado's Commercial Code and concerning the discharge of debts under Chapter 13 of the Bankruptcy Code. Subsequently, he successfully litigated the question of the dischargeability of claims in bankruptcy arising from the theft of construction funds under Colorado's Trust Fund Statute.

Mr. Kramer is licensed to practice law in Colorado and Wyoming, and is a member of the Colorado and Wyoming Bar Associations. Mr. Kramer is a member of the *Faculty of Federal Advocates*, a public interest organization providing pro bono representation in the United States Bankruptcy Court for the District of Colorado. Mr. Kramer is an avid backcountry skier and a member of Colorado's Backcountry Snowsport Alliance, an organization promoting backcountry safety and the preservation of Colorado's backcountry.

## Marlo J. Greer



Ms. Greer centers her practice in the areas of personal injury, medical practice, nursing home negligence, and criminal defense. Having lived in Colorado for most of her life, she attended the University of Colorado at Denver for her undergraduate work, receiving the Dean's scholarship for academic achievement. She received her J.D. from the University of Denver College of Law earning the

distinction of Student of the Year in the Student Law Office. Her experience in injury assessment gives her a unique perspective that helps her assist clients that have been involved in severe accidents.

After graduating law school, she practiced criminal defense and personal injury with a solo practitioner. She later worked with a mid-sized defense firm representing numerous physicians, hospitals, nurses, and nursing homes in health care related issues. Her background provides her with valuable courtroom experience and medical knowledge that is indispensable in representing clients at Fleishman & Shapiro.

She is licensed to practice in Colorado State courts, the United States District Court for the District of Colorado, and the Tenth Circuit Court of Appeals, and is a member of the American and Colorado Trial Lawyers Associations, the Criminal Bar Association, and the Colorado and Denver Bar Associations.

## Trust Fund Statute (continued from front)

tion of whether a Contractor's liability under the Trust Fund Statute terminated if no mechanic's lien is timely recorded and enforced. The American Subcontractors Association and several local suppliers filed amicus briefs requesting reversal of the Decision. The decision created the potential for a flurry of mechanic's lien filings and litigation to preserve Trust Fund Claims. This threatened to harm the Claimants with increased litigation costs and property owners as the other direct beneficiaries of the Trust Fund Statute.

In a 4-3 decision, the Colorado Supreme Court answered the question in the negative. The Court concluded that if the Colorado legislature intended to limit the time for enforcing the Trust Fund Statute to six months it would have done so. The Court noted that the Colorado legislature adopted the Trust Fund Statute to protect both Claimants and property owners from dishonest and profligate Contractors. The Court reasoned that because property owners cannot record liens against their own property, it would be

absurd to require the recording and enforcement of mechanic's liens as a condition to enforcing the Trust Fund Statute. The Court held that Trust Fund Claims are subject to a three or six year statute of limitations.

Based upon the Colorado Supreme Court's decision, the Trust Statute shall remain an important tool of recovery in the construction industry. Now, it is clear that property owners and Claimants shall not forfeit their Trust Fund Claims against Contractors merely because they took practical steps to minimize their losses. Additionally, the decision prevented the potential filing of numerous mechanic's liens and court cases saving all beneficiaries of the Trust Fund Statute substantial costs. Given the practical realities of a contrary ruling, the Colorado construction industry can breathe a sigh of relief as one judge's vote prevented the unjust enrichment of dishonest Contractors and a potential onslaught of mechanic's lien litigation.

## FLEISHMAN & SHAPIRO ON THE MOVE

- **Fleishman & Shapiro P.C.** is delighted to welcome **Harvey Kramer** and **Marlo Greer** as Associates to the firm. Harvey has been practicing law for over eight years, and will focus his practice in the domestic relations, real estate, creditors' rights, bankruptcy and all general civil and commercial litigation areas. Marlo has been practicing law for six years and is focusing her practice in the areas of civil litigation, personal injury and criminal defense.

- **Brian Reynolds** will be a featured speaker at an upcoming seminar entitled "Legal Ethics in Colorado". The seminar is

designed for all practicing attorneys and will be held on July 19, 2007. For more information, please contact our office.

- **Steve Shapiro**, with the assistance of **Katherine Karamalegos Kust**, recently gave a seminar entitled "Technology: Can't Live with It, Can't Live Without It", to members of the legal community. Mr. Shapiro was asked to present at this seminar by the Honorable Judge Charles Hoppin. The seminar focused on the advantages and disadvantages of technology in litigation.