

February 28, 2014

Rep. Sarah Stevens and Rep. Dean Arp
c/o Bill Patterson
North Carolina General Assembly

VIA E-MAIL ONLY
Bill.Patterson@ncleg.net

Re: House Committee on Mechanics Liens and Leasehold Improvements (LRC 2013)
SLO File No. 12-9040

Dear. Rep. Stevens and Rep. Arp:

I am writing as a member of and representative for the American Subcontractors Association of the Carolinas ("ASAC"), a trade organization with approximately 300 member firms and eight subchapters throughout North and South Carolina. ASAC was actively involved in the stakeholder meetings and legislative discussions regarding the 2011-12 amendments to the lien and bond laws and the 2013 technical corrections, and continues to be interested in the proposals presently before the House study committee.

ASAC wishes for me to express the following positions on the proposals before the Committee for the March 3, 2014 meeting:

1. Bill Draft 2013-MNz-15 [v.8] (02/19)

Section 1 - Addition of N.C. Gen. Stat. 44A-8.1: ASAC takes no exception to this proposal.

Section 2 - Amendment to N.C. Gen. Stat. 44A-26: ASAC strongly supports this proposal, as it serves to protect the interests of subcontractors working on projects involving public leases to private developers. Additionally, this proposal would in most (if not all) cases address the particular issues raised by the *Pete Wall* scenario.

Section 3 - Addition of N.C. Gen. Stat. 42-3.1: ASAC supports this proposal.

2. NCLTA Proposed Changes to Mechanic's Lien Law - February 2014

Section 1 - Changes to Notice to Lien Agent form: ASAC takes no exception to this proposal.

Section 2 - Amendment to N.C. Gen. Stat. 11.1(a): ASAC opposes this proposal. We do not believe the statute should be amended to provide implicit endorsement of a late appointment of a lien agent. The title insurance industry insisted that having lien agents was necessary to protect them against hidden liens. Any effort to excuse delays in appointing lien agents undermines the rationale for having the lien agent structure in the first place, and calls into question their necessity.

Section 3 - Amendment to N.C. Gen. Stat. 44A-20(d): ASAC strongly opposes this proposal, as it would not only erase the improvements made to the lien laws in the consensus bill passed as HB 1052 only two years ago, but it would actually erode the rights of subcontractors and suppliers further than the original (pre-2012) laws. While the Land Title Association purports to be concerned about a situation where a later-performing subcontractor (who performs after a contractor has subordinated its lien rights) may step ahead of the lender, the proposal would actually permit a lender to jump ahead of an earlier-performing subcontractor who could rely upon its own priority date. This outcome would be highly inequitable, damaging to relations between contractors and subcontractors, and moreover has nothing to do with either the leasehold lien issue for which the House established this study committee or the payment verification issue that the Land Title Association claimed was a high priority to it.

More importantly, the proposal is based on a legally faulty premise. Under no circumstances can a subcontractor obtain a higher priority by way of a “wrongful payment” lien, because such a lien creates a direct claim of lien against the real property, rather than being a subrogated claim through the general contractor. A claim of lien based on a wrongful payment by an owner over a properly-served notice of claim of lien upon funds, constitutes a *direct* claim of lien on the real property for the benefit of the subcontractor whose rights were violated by the illegal payment. As such, that subcontractor does not rely upon the first furnishing date of any party other than that subcontractor, because in effect the subcontractor becomes the “contractor” for purposes of the lien. A hypothetical subcontractor who first furnished work *before* a sale or refinancing of the property, but who failed to give notice to the lien agent, would already be subordinated by virtue of the statutory changes obtained at the behest of the title insurance industry. A hypothetical subcontractor who first furnished work *after* a sale or refinancing would already be subordinate to the new owner and/or lender because of the later priority date. Section 44A-23(d), as already implemented, limits the application of utilizing a higher-tier contractor to a lien “through which the claim of lien on real property is being asserted.” A wrongful payment lien under 44A-20(d) is not claimed through any other party, so the requested revision serves no purpose except the unfair enrichment of parties other than the subcontractor or supplier whose lien rights were already abused by that wrongful payment.

Section 4 - Amendment to N.C. Gen. Stat. 44A-23(d): ASAC strongly opposes this proposal for the same reason as that stated regarding Section 3 above. The reasoning put forward by the Land Title Association is also specious for the reason that under the compromise passed by the General Assembly under Senate Bill 42 (the LTA’s bill) and then improved in the technical corrections bill in 2013, a subcontractor

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or supplier can already have its lien rights cut off by the waiver of lien rights by the general contractor prior to the filing of a claim of lien on real property. Contrary to what the LTA has stated in its proposal, a subcontractor does not get to "choose" the contractor's start date and thereby avoid the contractor's lien waiver. Sections 44A-20(d) and 44A-23(c) already explicitly detail when a subcontractor's rights can be cut off by a contractor's lien waiver. No amendment is necessary.

3. Amendments to N.C. Gen. Stat. sections 44A-7(6), 44A-9.1, and 44A-23.1

My understanding is that the committee has received the proposals from Henry Jones, which suggests the creation of a noticing system to allow all potential lien claimants to notify private owners of real estate of improvements where a leasehold is involved. A copy of the proposed language is also attached with this letter.

The proposal borrows from concepts implemented in other states, but places a greater responsibility upon the contractor/sub/supplier to give the initial notice, while placing a relatively limited burden upon the land owner to disclaim financial responsibility for the improvement. While the proposal is far from an ideal protection for the rights of those furnishing improvements, it will at least give those parties advance or early warning that they contract at their own risk. We believe that having that particular information will enable market forces - including the refusal of contractors to undertake such work in the absence of payment assurances or security - to encourage those land owners to ultimately participate in the contracting process.

On behalf of ASAC and its members, I want to thank you for considering this submission. If you have any questions, please do not hesitate to contact me.

Sincerely,



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BJS:
Enclosures

cc: Perry R. Safran, Esq.
ASAC (ew/lb/cs)

Part 1: Amend Section 44A-7 as follows:

(6) Owner.--A person who has an interest in the real property improved and for whom an improvement is made and who ordered the improvement to be made. "Owner" includes successors in interest of the owner, any person acting for, on behalf of, or with the consent of such owner, and agents of the owner acting within their authority.

Part 2: Add new Section 44A-9.1:

§ 44A-9.1. Notice of Nonresponsibility

- (a) A contractor who contracts for the improvement of real property, wherein the owner holds only a leasehold interest, may, to the extent of the claim, enforce the claim of lien on real property against the interest of the owner of the fee simple interest in the real property, provided:
- (1) The contractor serves the owner of the fee simple interest in the real property with a Notice of Potential Lien Claimant in compliance with G.S. § 44A-9.1(b); and
 - (2) The owner of the fee simple interest in the real property fails to serve a Notice of Nonresponsibility in compliance with G.S. § 44A-9.1(c).
- (b) The Notice of Potential Lien Claimant shall be in writing and contain the following:
- (1) Name and address of the owner of the fee simple interest in the real property at the time this Notice of Potential Lien Claimant is served;
 - (2) Name and address of the owner of the leasehold interest in the real property;
 - (3) Description of the real property to be improved (Street address, tax lot and block number, reference to recorded instrument, or any other description is sufficient, whether or not it is specific, if it reasonably identifies the real property);
 - (4) Name and address of the party with whom the Potential Lien Claimant may contract for the improvement of the real property;
 - (5) General description of the labor to be performed or materials to be furnished for the improvement of the real property;
 - (6) "Owner of the real property set out herein is notified that within ten (10) days of service of

this Notice of Potential Lien Claimant, you are required to serve the undersigned with a Notice of Nonresponsibility and failure to do so within the time provided by G.S. § 44A-9.1 shall permit the undersigned, to the extent of his claim, to enforce a claim of lien against the real property consistent with Chapter 44A of the North Carolina General Statutes.

- (7) Name, address and signature of the person, firm or corporation serving the Notice of Potential Lien Claimant.

The Notice of Potential Lien Claimant shall be served upon the owner of the fee simple interest in the real property no later than five (5) days from the Potential Lien Claimant's first date of furnishing labor or materials for the improvement of the real property. Proof of service of the Notice of Potential Lien Claimant shall be in any manner authorized by G.S. § 1A-1, Rule 4.

- (c) Notice of Nonresponsibility from Owner of real property.

- (1) An owner of the fee simple interest in the real property, who is notified by a Potential Lien Claimant, pursuant to section (b) above, and with whom this owner did not contract, may give notice to the Potential Lien Claimant of nonresponsibility for the improvement of the real property.

- (2) The Notice of Nonresponsibility under this section shall be in writing and include all of the following information to the extent known to the person giving the notice:

- i. The name and address of the owner of the real property and the nature of the owner's title or interest in the real property;
- ii. The name and address of the leasehold owner and the nature of the leasehold owner's title or interest in the real property;
- iii. A statement that the owner of the fee simple interest in the real property is not responsible for claims arising of the Potential Lien Claimant for labor to be performed or materials to be furnished for the improvement of the real property.

- (3) A Notice of Nonresponsibility is not effective unless, within ten (10) days after service of a valid Notice of Potential Lien Claimant, the owner of the fee simple interest in the real property serves the Potential Lien Claimant with a Notice of

- Nonresponsibility as provided herein. Proof of service of the Notice of Nonresponsibility shall be in any manner authorized by G.S. § 1A-1, Rule 4.
- (4) A valid Notice of Nonresponsibility shall be otherwise subject to Chapter 44A of the North Carolina General Statutes and shall not create any presumption, be asserted in defense of or serve as a bar against any other basis under which a contractor may be permitted to enforce a claim of lien against the real property.

Part 3: Add new Section 44A-23.1:

§ 44A-23.1. Notice of Nonresponsibility

- (a) A first tier subcontractor, second tier subcontractor, or third tier subcontractor who contracts for the improvement of real property, wherein the owner holds only a leasehold interest, may, to the extent of the claim, enforce the claim of lien on real property of the contractor against the interest of the owner of the fee simple interest in the real property, provided:
- (1) The subcontractor serves the owner of the fee simple interest in the real property with a Notice of Potential Lien Claimant in compliance with G.S. § 44A-23.1(b); and
 - (2) The owner of the fee simple interest in the real property fails to serve a Notice of Nonresponsibility in compliance with G.S. § 44A-23.1(c).
- (b) The Notice of Potential Lien Claimant shall be in writing and contain the following:
- (1) Name and address of the owner of the fee simple interest in the real property at the time this Notice of Potential Lien Claimant is served;
 - (2) Name and address of the owner of the leasehold interest in the real property;
 - (3) Name and address of the contractor, if known. If the Potential Lien Claimant does not know who is contracted with the owner of the leasehold interest, the Potential Lien Claimant shall enter "contractor unknown";
 - (4) Description of the real property to be improved (Street address, tax lot and block number, reference to recorded instrument, or any other description is sufficient, whether or not it is specific, if it reasonably identifies the real property);

- (5) Name and address of the party with whom the Potential Lien Claimant may contract for the improvement of the real property;
- (6) General description of the labor to be performed or materials to be furnished for the improvement of the real property;
- (7) "Owner of the real property set out herein is notified that within ten (10) days of service of this Notice of Potential Lien Claimant, you are required to serve the undersigned with a Notice of Nonresponsibility and failure to do so within the time provided by G.S. § 44A-23.1 shall permit the undersigned, to the extent of his claim, to enforce a claim of lien against the real property consistent with Chapter 44A of the North Carolina General Statutes.
- (8) Name, address and signature of the person, firm or corporation serving the Notice of Potential Lien Claimant.

The Notice of Potential Lien Claimant shall be served upon the owner of the fee simple interest in the real property no later than five (5) days from the Potential Lien Claimant's first date of furnishing any labor or materials for the improvement of the real property. Proof of service of the Notice of Potential Lien Claimant shall be in any manner authorized by G.S. § 1A-1, Rule 4.

(c) Notice of Nonresponsibility from Owner of real property.

- (1) An owner of the fee simple interest in the real property, who is notified by a Potential Lien Claimant, pursuant to section (b) above, and with whom this owner did not contract, may give notice to the Potential Lien Claimant of nonresponsibility for the improvement of the real property.
- (2) The Notice of Nonresponsibility under this section shall be in writing and include all of the following information to the extent known to the person giving the notice:
 - i. The name and address of the owner of the real property and the nature of the owner's title or interest in the real property;
 - ii. The name and address of the leasehold owner and the nature of the leasehold owner's title or interest in the real property;
 - iii. A statement that the owner of the fee simple interest in the real property is not responsible for claims of the Potential Lien

Claimant for labor to be performed or materials to be furnished for the improvement of the real property.

- (3) A Notice of Nonresponsibility is not effective unless, within ten (10) days after service of a valid Notice of Potential Lien Claimant, the owner of the fee simple interest in the real property serves the Potential Lien Claimant with a Notice of Nonresponsibility as provided herein. Proof of service of a Notice of Nonresponsibility shall be in any manner authorized by G.S. § 1A-1, Rule 4.
- (4) A valid Notice of Nonresponsibility shall be otherwise subject to Chapter 44A of the North Carolina General Statutes and shall not create any presumption, be asserted in defense of or serve as a bar against any other basis under which a subcontractor may be permitted to enforce a claim of lien against the real property.