

The Lien Law Is Not Read Into a Private Contract

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Mechanic's liens are important tools to force payment, however, not every project can be "liened."

The Lien Law is very specific regarding the different timing, notice and content for mechanic's liens filed on public and private improvements. There is a gap, however, when there is private improvement on public land. Under this scenario, there is no right of mechanic's lien. The property is owned by a municipality and/or state agency so the mechanic's lien cannot attach or be attached to the physical property. Additionally, because private monies are funding the project, there is no public fund for a mechanic's lien to attach.

To address this situation, the Legislature enacted Lien Law Sec. 5. This section provided that where there is no public fund to finance the improvement with an estimated cost in excess of \$250,000, "the chief financial officer of the public owner shall require the private entity from whom the public improvement is being made to post, or cause to be posted, a bond or other form of undertaking guaranteeing prompt payment of moneys due to the contractor, his or her subcontractors and to all persons furnishing labor or materials."

In a recent case that went all the way to New York's highest court, NY Court of Appeals, a construction manager was suing the private developer for, among other things, breach of contract for failure to comply with Lien Law Sec. 5.

In this major private development project in New York City, the construction manager faced extensive delays and after the date for substantial completion passed, the construction manager served its intent to terminate the agreement. One of the reasons stated for the termination was the developer's failure to comply with Lien Law Sec. 5. Ultimately, the construction manager stopped work and commenced an action against the developer and other entities.

The agreement between the developer and the public owner required the developer to satisfy all requirements of Lien Law Sec. 5. Pursuant to that agreement, a non-party and related entity of the developer, made a Guaranty in favor of the public owner which, among other things, guaranteed the developer's completion of the construction work and that the developer would use all monies disbursed by the lender to pay all costs, expenses and liabilities, including construction costs, incurred in connection with the guaranteed work.

The Appellate Division (intermediate appellate court) held that the Guaranty satisfied the mandate of Lien Law Sec. 5. Two Justices dissented and would have held that the Guaranty did not qualify as an "other form of undertaking" within the meaning of the statute. The construction manager then further appealed.

The Court of Appeals, in upholding the dismissal of the construction manager's breach of

contract claim based on Lien Law Sec. 5, did not even address whether the Guaranty complied with the Lien Law. Rather, the Court of Appeals reviewed the construction manager's agreement with the developer and determined that there was no provision of that agreement in which the developer breached in connection with Lien Law Sec. 5. In fact, the court held that the construction manager did not even identify which, if any, provision or provisions were purportedly breached. Unlike the developer's agreement with the public owner, the construction management agreement did not contain an express provision requiring compliance with the Lien Law.

The construction manager argued that Lien Law Sec. 5 should be read into the agreement because the contract is governed by New York law. The Court rejected this argument and held that this was merely a choice of law provision which does not impose any contractual obligation. The Court further held that the mere fact that an agreement and disputes are governed by the law of a particular jurisdiction does not transform all statutory requirements that may otherwise be imposed under that body of law into contractual obligations.

Based upon this finding, the Court specifically did not reach the merits of the parties' arguments concerning either the interpretation of Lien Law Sec. 5 or whether the Guaranty satisfies its mandate.

Commentary

The major take-away from this case is that a private developer on public land is not bound by the provisions of the Lien Law, unless such requirement is specifically set forth in its contract with its construction manager. This holding, which appears to be inconsistent with the Legislature's mandate and public policy, is inconsistent with the developer's obligation to comply with the Lien Law as set forth in its agreement with the public owner.

This case is an egregious example of a court, and in this case the highest court in New York, failing to understand the importance of the Lien Law and the unique situation where private development is undertaken on public land. The problem is, this situation is becoming more commonplace. There are major developments currently under construction where this same problem is likely to reoccur.

From the construction manager/general contractor's point of view, when negotiating the contract with the private developer, the construction manager/general contractor must make sure that the written agreement imposes Lien Law Sec. 5 obligations on the private developer. Additionally, the construction manager/general contractor must obtain a copy of and scrutinize the "bond or other undertaking" prior to executing the contract. The construction manager/general contractor must be satisfied that what is being presented complies with the statute.

Subcontractors and materialmen should ask for a copy of the "bond or other undertaking" prior to executing a subcontract with the construction manager/general contractor. If

there is no bond or other undertaking for the project, the subcontractor and materialman should give pause and determine the risk of non-payment, which is possible in the absence of mechanic's lien rights.

Finally, all contractors and subcontractors and all construction associations should lobby their local and State representative to have the Legislature amend Lien Law Sec. 5 to specifically state that the provisions of that section are to be read into every contract and that these provisions cannot be waived by contract.

Feel free to contact me to discuss lien rights.