

SECURITY OPTIONS DURING DIFFICULT ECONOMIC TIMES: MECHANIC'S LIENS DEMYSTIFIED

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It is an understatement to say that grasping the requirements of the mechanic's lien statute can be difficult and frustrating, not to mention boring. Understandably, most of you do not have the urge to master the basics of lien law, at least not without a good dose of caffeine at the ready. Well, it's time to bite the bullet and fill your cup with high test. In today's economy, a basic understanding of the mechanic's lien law could provide you with the tools you need to protect yourself from the devastating results of an upstream business failure or an otherwise uncollectible payment claim.

I. The Definition

A "Mechanic's Lien" is a statutory lien granted to contractors, subcontractors and suppliers who provide labor and materials necessary to build a structure. The mechanic's lien statute, known as RSA 447, was enacted by the legislature specifically to protect contractors, subcontractors and suppliers who add value to property through their contributions to the construction process. RSA 447 grants these contributors a lien on the materials supplied, the structure into which they were incorporated and any interest that the owner of the structure has in the land on which it sits. Mechanic's liens enjoy priority over many other types of recorded liens, regardless of recording order. As a result, they are very effective payment tools.

II. How it Works

In order to claim the benefit of the lien, you must meet a few simple requirements set forth in the statute. I won't bore you with the details, except to say that if you have supplied labor or materials necessary to build a structure, or appurtenant roads and infrastructure, you are almost certainly entitled to claim a lien. It is important to understand, however, that the New Hampshire mechanic's lien statute does not treat all types of contractors equally.

A. Direct Contracts

The New Hampshire statute makes a critical distinction between the lien rights available to those who have a direct contract with the owner (typically the general contractor) and those who do not (subcontractors and suppliers). If you have a direct contract with the owner, the mechanic's lien granted by RSA 447 arises *automatically* from the first day of work and you need do nothing more to solidify your rights until it is time to "perfect" and record your lien.

B. Indirect Contracts: Notice

IMPORTANT: In the event that you do *not* have a direct contract with the owner, the statute requires you to give *written notice directly to the owner* disclosing that you have provided labor and materials to the project and informing the owner that you will enforce the provisions of RSA 447 and perfect a mechanic's lien in the event that a payment problem arises. Here's the catch...you must send this notice to the owner before starting the work at the project. If these

requirements are met, then you will have lien rights identical to the contractor who has a direct agreement with the owner. Any lien you subsequently file will relate back to your first day of work. The form the notice should take is simple and can be drafted by your attorney for use on most projects.

Countless times my subcontractor clients have questioned my sanity in advising them to send a notice of this type, indicating that doing so would surely alienate the general contractor with whom they have an established relationship. After agreeing to do so, however, most subcontractors find that sending a well worded, non adversarial notice which merely preserves the subcontractors rights as required by statute, generally does not enrage the general contractor or alienate the owner. Most general contractors understand the business reasons behind the notice and are not typically offended by a subcontractors honest attempt to preserve its legal rights.

C. What? I Didn't Send a Notice and I Already Started Work!

Don't despair. If you are already on site and did not send an advance lien notice, you will still have an opportunity to claim a lien, but it will be limited in scope. The statute provides that you are entitled to give notice of your lien rights *after* the work begins, but your lien will be limited to the amount which is due, or which may later become due, from the owner to the general contractor on the date the notice is received. Put another way, as a subcontractor or supplier giving notice *after* providing labor and materials, your lien is limited to the amount the owner owes to the general on the date of notification, plus any amounts which later become due.

The obvious danger in waiting to give your lien notice is that your notice will arrive so late in the progress of the work that the owner has already paid *in full* by the time your notice arrives. In that case your lien is valid only to the extent that funds are still due from the owner to your contractor. If *nothing* is due when your notice arrives, then your lien is not valid. You may also run into a situation where there is a balance due from the owner, but is it far less than you are owed. As a result, you may have a valid lien, but it will not be enough to cover your claim.

To add insult to injury, the "limited lien" available to you if your notice is given *after* work begins is also subject to offsets by the owner. For example, if the general contractor defaults, is terminated or has left defective work behind, and the owner incurs costs to correct or finish the work, the owner's costs may be offset against the amount owed at the time your notice is received. This often reduces or eliminates the owner's debt to your contractor, or at a minimum, limits the amount owed to a low number. If absolutely nothing is owed to the general contractor after the offsets are applied, then your lien will be eliminated.

In light of the above, filing your notice before the work begins can mean the difference between a fully secured claim for payment and the complete loss of your lien rights. It is good practice to always file the notice on every project to make sure you have protected your rights to the greatest extent possible.

III. Perfection of the Lien (Lawyer Stuff)

The last thing you have to contend with is probably the most complicated. Let's assume

that you've done everything right. You either have a direct agreement with the owner (and therefore did not have to provide notice) or you did not have a direct agreement, but you fulfilled your notice requirements to the letter. Well, you're not off the hook yet. Your lien will eventually expire unless you take specific steps to "perfect" it before deadline set by the statute.

According to RSA 447, a mechanic's lien continues in force for 120 days after the last date labor is performed or materials are supplied to the project. The 120-day period begins to run at the time your work required by the contract is completed, which is the date when the last substantial labor and materials were furnished. *Before the 120-day period expires*, the contractor must take the steps necessary to perfect the lien, or it is lost. As a result, all of the steps required to perfect the lien must be taken prior to the expiration of the 120-day period.

Unfortunately (for you), lien perfection is a complex process that must typically be completed by your lawyer. I have seen many amateur lien perfection attempts and have not seen one succeed. The perfection process requires filing a lawsuit, obtaining a court order granting the mechanic's lien, properly preparing a Writ form that must be worded in specific manner, recording the pleadings at the Registry of Deeds and serving them on the parties to the lawsuit. This procedure must be followed to the letter, and be completed before the lien expires, or your lien will be subject to challenge by the opposing party. As a result, it is probably in your best interests to consult an attorney to complete these steps for you.

IV. Beware of the Hidden Waiver Provisions

Keep in mind that, in some cases, you may have signed a contract in which you waived your right to file a mechanic's lien. In New Hampshire, the Supreme Court has ruled that a contract which contains a clear and precise waiver provision will be enforced. As a result, your lien rights will be extinguished if you sign a contract in which you waive your right to seek or record a mechanic's lien. Consequently, you must beware of hidden waiver provisions. They are very common in modern contract forms.

V. What it all Means

In the event that the perfection of your lien goes smoothly, you will ultimately hold a recorded lien on the project which has priority over many other types of property liens, even if they were recorded prior to your lien. As a result, you may be in a better position to negotiate with your contracting party or directly with the owner to obtain the payment you have earned. Property cannot be sold or refinanced without dealing with the issue of your lien. Moreover, construction financing will often come to a standstill if the lender's title search discloses your lien. Accordingly, mechanic's liens represent one of the most effective methods for getting paid in a difficult economy.

VI. The Moral

Know your lien law basics so that you have the knowledge to send the appropriate notices and contact your counsel at the appropriate time to perfect your lien before it expires. Clearly, notice is the name of the game for subcontractors. If you take the time to send a

relatively simple letter to the owner at the outset of the project, it could mean the difference between a devastating financial loss and collecting some or all of the amounts owed to you. The potential for receiving some payment on an otherwise uncollectable claim is well worth the small investment of time and effort required to forward the notice to the owner.