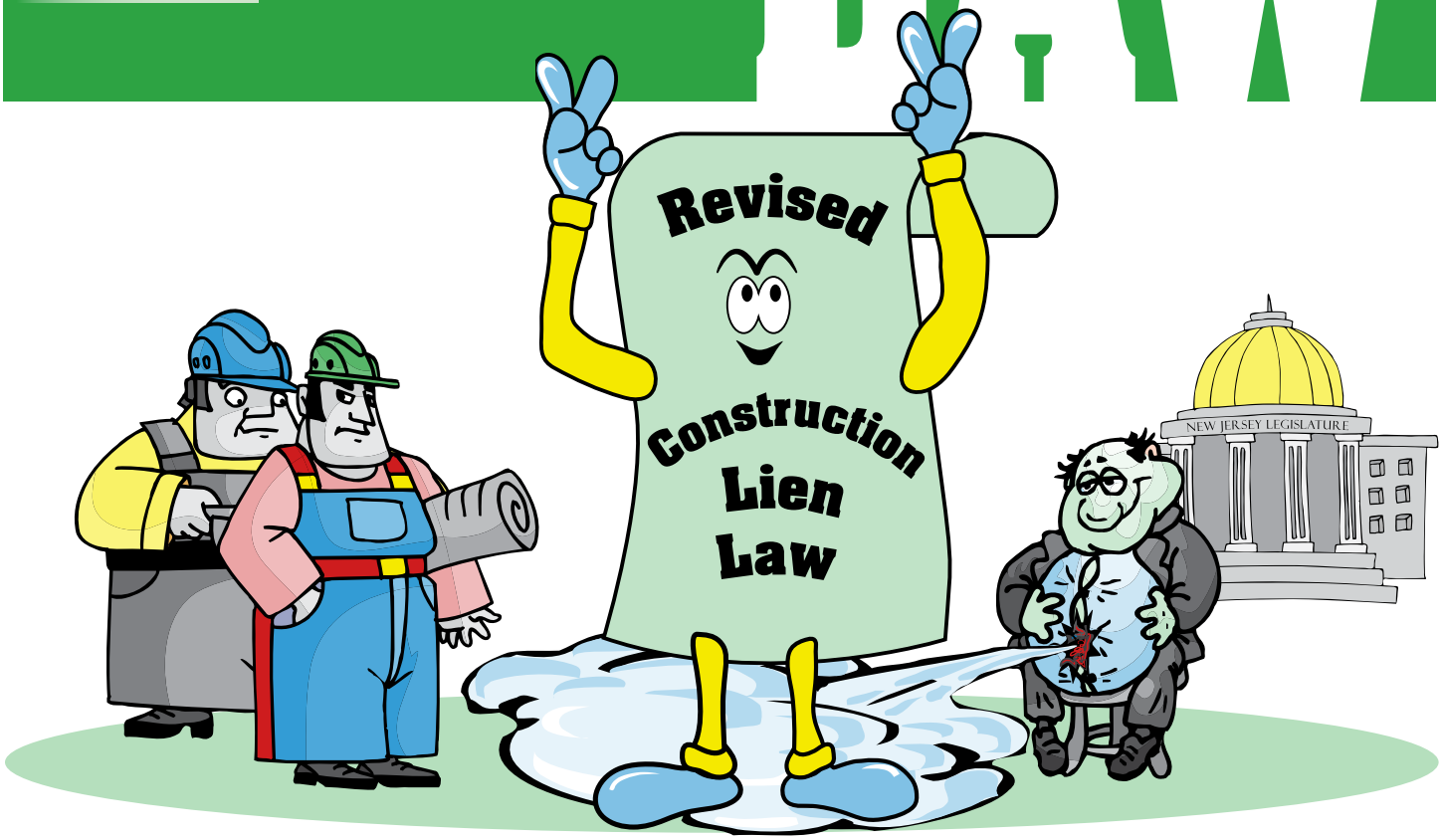
Plumb LAW

Construction Lien Law Special Edition



While little acorns might make mighty oaks, little legislative efforts have an unfortunate tendency to produce things like the 2011 revisions to the New Jersey Construction Lien Law (the "Revisions"). The New Jersey Law Revision Commission generated a lot of "under the hood" clarifications which will be helpful to lawyers, but taken together, they don't help the construction industry. Lien rights have been narrowed, some questionable new ideas have been added, and newly ambiguous language has replaced some old ambiguous language. The Revisions do some good, but as one of the law's original drafters, I think they are a real disappointment.

New Forms: Throw out all your old forms because there is a new construction lien claim, amended lien claim and Notice of Unpaid Balance and Right to File Lien ("NUB"). The Revisions also add a new form for "bonding off" a construction lien. The same underlying information is needed, but the new lien form finally states that contract amendments include change orders, and it no longer requires a breakdown of payments into the original contract and contract amendments. The new forms could also use a design makeover because the forms' attempts to cover more alternatives make them harder to follow.

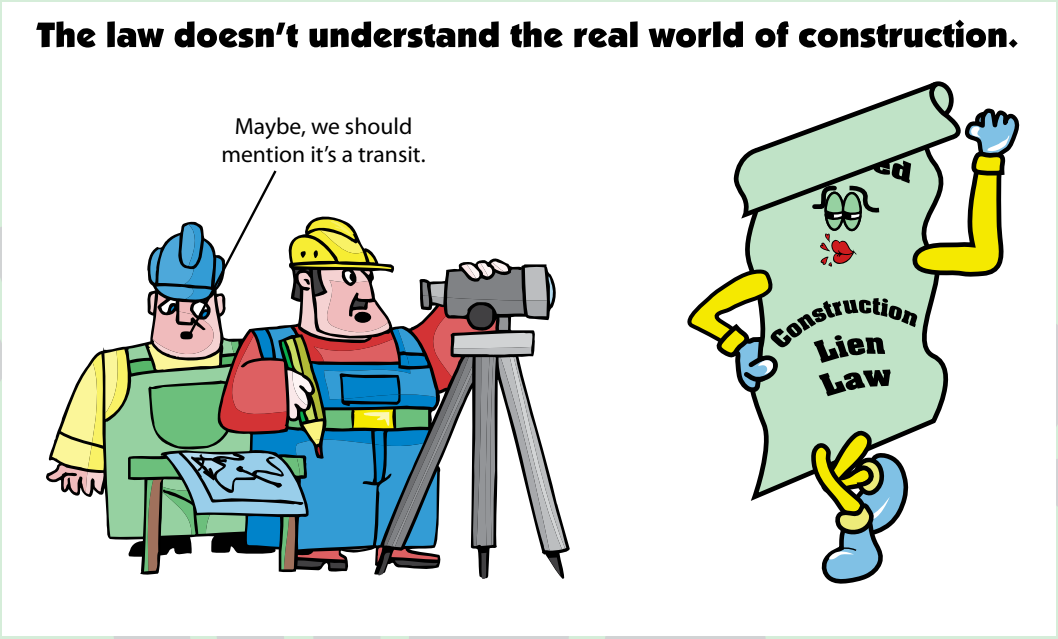
The Contract and Change Orders: Under the original version, a construction lien could only be filed if based on "any agreement, or amendment thereto, in writing, evidencing the respective responsibilities of the contracting parties." While a signed contract or change order qualified, there was no explicit requirement for a signature. That left room for situations where, for example, a subcontractor signed and returned a subcontract to a GC and started performance but the GC did not execute and return it. Unsigned change orders which were approved but not signed also fell within statutory protection. Construction contracting is a messy business, and the old language met that situation.

Under the Revisions, a lien must now be supported by a contract and change orders signed by the other party. But, the word "signature" has been expanded to include

Continued on p. 2

a "mark or symbol" by the party which is "sufficient to authenticate it". The courts will now have to decide if things like e-mail confirmation of change orders are close enough to an authenticating mark or symbol even though on a separate "page." So, the law basically swapped an old ambiguity for a new one.

Supplier Issues: The one clearly favorable change was to grant lien rights to suppliers of suppliers of owners, GC's, construction managers and design professionals. But, all suppliers must now face slightly tougher documentary requirements. Suppliers can still support a lien with a signed contract, order slip or delivery ticket signed by the buyer. For delivery tickets and order slips, however, the document must identify the site where the materials were to be used or delivered. A small loophole is still open for suppliers because the revisions do not explicitly state that suppliers can only base a lien on those signed writings. Be warned, however, that earlier court decisions do not permit a supplier's lien to be based on an unsigned invoice.



Practical Tips: For this law, a written contract can be as simple as a signed napkin scribble so long as it identifies the parties, the price and the work scope. Make sure to include retainage as part of the amount due.

Filing: The expiration periods for all liens run until the date the county clerk's office receives the liens instead of the date the clerk files them. One good change was to require all the counties' clerks to accept a $15.00 filing fee instead of the hodgepodge which has varied by county.

Lien Service: When liens are being served by mail, two copies must now be sent instead of one. One copy can be sent by certified or registered mail, and now, by private courier like Federal Express. A second copy, however, must also be sent by regular mail. The served copy must also have a county clerk's acknowledgement of its receipt. In addition, the number of days to serve the lien has been trimmed to 10 calendar days from 10 business days. As before, the failure to timely serve a lien will only render it ineffective if this causes "prejudice" to the property owner or another party who should have received it. Proving prejudice is now a little easier.

Tenancy Attachments: The real estate industry scored a clear win with the virtual destruction of lien rights against leased real estate. When construction work is for a tenant, the ordinary rule is that a contractor can only file a lien against the tenancy. Tenants who don't pay for construction are often in financial difficulty and on their way to defaulting on their lease. The landlord can then re-take the space without paying for the work. Contractors had a little protection where the construction included the owner's participation by allowing a lien against the underlying property if it had "been authorized in writing by the owner of the fee simple interest". Creative lawyers could find this in things like leases where the landlord agreed to pay for part of the construction costs.

The Revisions have now choked this exception to death. First, the landlord must either: (a) sign a writing which "provides that the person's interest is subject to a lien for this improvement"; (b) sign a lease which says the same thing; or (c) has paid or agreed in writing to pay "the majority of the cost of the improvement." Even then, the owner's liability is limited to the amount it has actually committed to the project, less prior payments made for construction. We think this is unfair. If a landlord has pledged an amount for construction which was not released to the defaulting tenant, at least that amount ought to be available to pay contractors.

Lien Amendments: A good correction was to explicitly permit lien amendments to be filed for reasons other than

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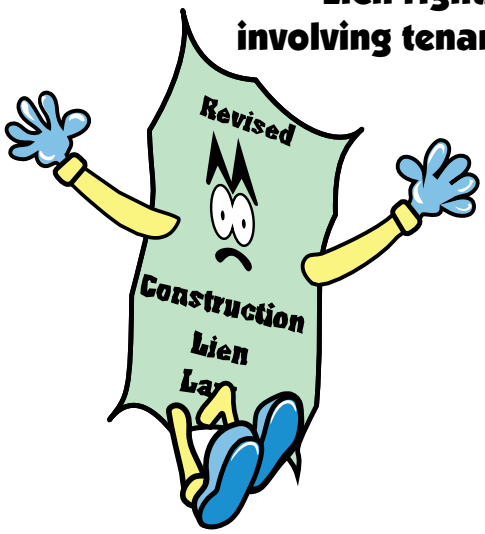
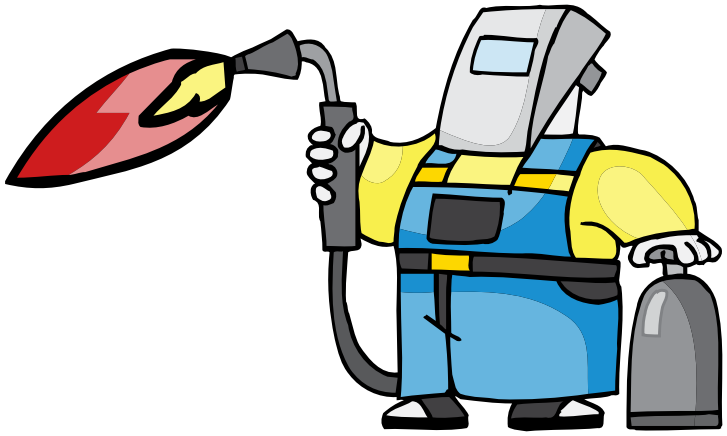
Lien rights have been cut back on property involving tenants and large real estate developments.





an increase in their amounts. Previously, this right had only been assumed. A bad exception, however, prohibits lien amendments where the original lien contained the type of defect which would allow a court to order the claimant to discharge the lien and pay damages. This exception discourages lien claimants from voluntarily fixing defective liens and encourages court battles. The law should have simply preserved the right to sue for damages even after a lien amendment.

The Lien Fund: The Revisions do not change the original law's meaning, but they do adopt some important court decisions which were issued after its passage. The purpose of the lien fund is to limit recovery on a lien to the amount the owner had not paid for construction. After the original law was "on the books", however, the courts began to limit the right of the owner to reduce the lien fund when the courts felt that reductions were unfairly depriving contractors of their payment rights. For example, one really important court ruling broke with prior law to decide that the owner could not reduce the lien fund after a lien filing by the cost paid to complete the claimant's work. Other prohibitions against lien fund reductions mentioned by the courts included payments not made in accordance with the contract, collusive or advance payments, and offsetting claims for liquidated damages. The Revisions include those, along with some related ones. While the Revisions do a pretty good job at incorporating court decisions, they too loosely use "retainage" without distinguishing between: (a) retained but unreleased progress payments, and (b) designated contract retainage. This raises doubt if that earlier court case is still good at stopping lien fund reductions from (a) as well as (b).

Residential Liens: The biggest revisions impact residential property, and in particular, large residential developments. First, the right to file a lien against residential property has been increased from 90 days to 120 days. In real time, however, the 30 additional days should be viewed as an additional 10 days. This is because the law now

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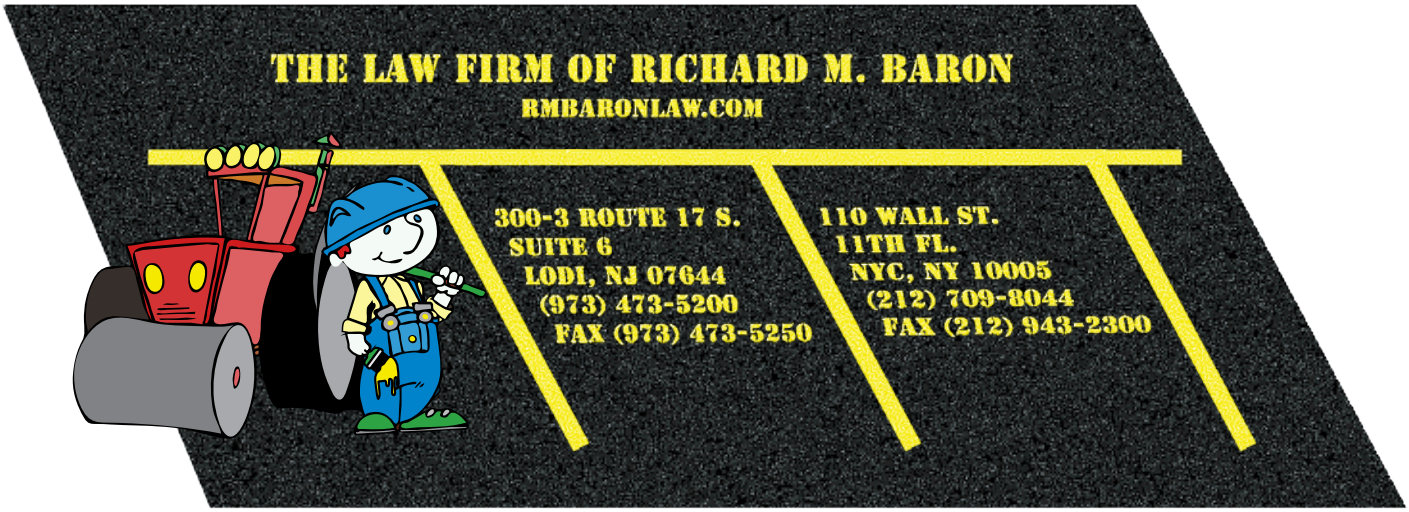

Plumb Law On-line

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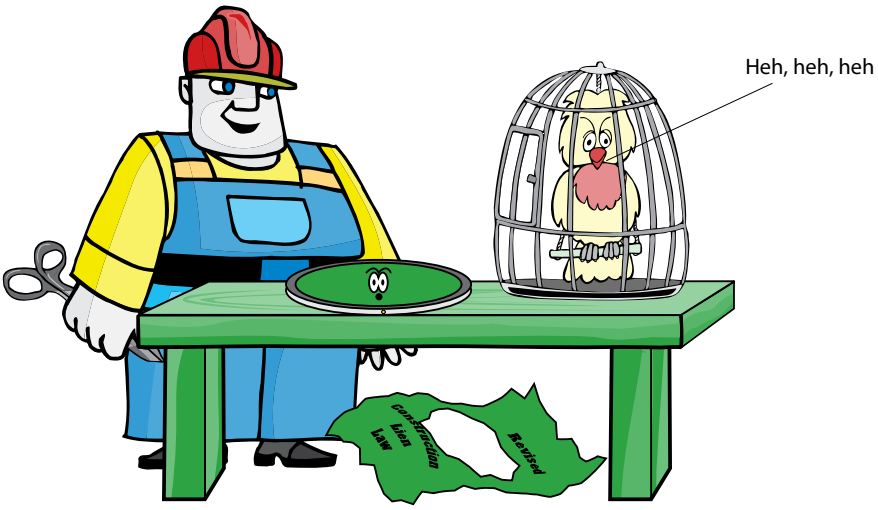
Continued from p. 3

requires a potential lien claimant to start the process of securing a lien by first filing a NUB within 60 days of its last performance. The original law had no deadline, but to safely meet the old 90 day mark required a NUB filing, dispute resolution and lien filing to begin by day 50. Permission to file a residential lien still requires dispute resolution, and the designated method is still before the American Arbitration Association unless the parties otherwise agree. Technical procedures in arbitration have also been altered. An arbitrator only has 7 days to make a decision if a NUB is uncontested, and the same arbitrator who decides one NUB on a project should decide them all.

Larger Projects: Real estate interests secured another win by banning the right to foreclose on a lien where the work is solely performed for the managing association on the common elements of a condominium or other form of multi-unit residential development bigger than 3 units. Instead, a lien claimant who wins in court just gets a right to a forced assessment against the association's unit owners. This effectively relieves pressure on the association to promptly pay its bills and it is likely to encourage lawsuits by frustrated contractors. For other situations: (1) if the construction is directly for a unit owner, a lien claimant may only foreclose against the unit and its share of the common elements; or (2) if the construction is for the developer, the lien claimant can lien and foreclose upon the whole of the property subject to construction, except for any portions transferred out before a lien or NUB had been received by the county clerk for filing. Do not forget that all these projects still must meet the law's requirements for residential liens.



30 Day Demand to Start Suit: Under the original law, a property owner could serve a written demand stating that if the claimant failed to sue in 30 days, the claimant must discharge the lien. The Revisions extend this right to everyone else who is affected. Unlike lien service, this demand must still be by certified letter or personal service.

One that "Got Away": A lot of legal fees will be continually wasted because of this omission: once a lien claimant has started a lawsuit, the time limits for the other lien claimants to start suit against the same property should be considered as met. The law has always stated that all lien claimants must be joined in the same action because they all share out of the same lien fund. Since the law did not include language which stopped time for other claimants, some attorneys have started their own lawsuits even though their own client's liens are already going to be evaluated in the first lawsuit. With 10 hyper-technical lawyers starting 10 lawsuits, all the other parties must file responses to each one even though they all basically say the same thing. Then, even more money is wasted to consolidate them. The Revisions should have borrowed New York's law which effectively states that one timely lawsuit protects every other lien claimant.

Bird cage liner may seem like a harsh analogy for a revised law which does some good. But instead of providing stronger payment protection rights for contractors and a simplified filing and enforcement process, the Revisions have headed the law in the opposite direction. The industry deserved better.