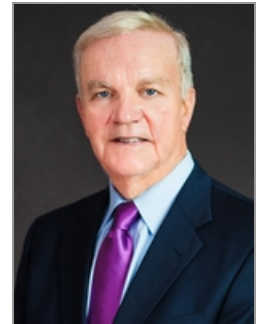


A Guide To Construction Liens In New Jersey

By **Charles Kenny and Scott Kearns**

This article discusses construction liens (also referred to as mechanic's liens) pursuant to the New Jersey Construction Lien Law (CLL), N.J. Stat. § 2A:44A-1 et seq., and explains the filing requirements, including who is entitled to file a lien, timing requirements and the types of work that give rise to lien rights.

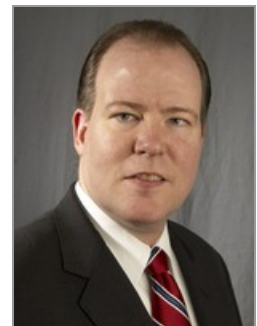
The CLL became effective on April 22, 1994, replacing New Jersey's existing mechanic's lien law for projects having building permits issued on or after the effective date. The CLL was substantially amended by legislation enacted on Jan. 5, 2011.



Charles Kenny

What is a Construction Lien?

A construction lien is a security interest in the real property on which the construction work has been performed. Properly placed, filed and served, it stays with the property regardless of who may subsequently own the property. From a practical standpoint, the construction lien prevents the property owner from selling the property or borrowing more money against the property without resolving the underlying claim. The value of the land becomes the fund for payment of the persons who supplied labor, materials and services in improving the land. Ultimately, the property can be sold to pay the lien claimant in an action to foreclose the construction lien.



Scott Kearns

The construction lien is not absolute — it can be subject to prior liens, such as acquisition financing and prior judgments — but it is a powerful tool.

What Other Remedies are Available?

The CLL does not alter any other rights of the parties. Therefore, in addition to any construction lien rights, a contractor, subcontractor, designer or supplier retains whatever rights it may have to sue the party with whom it contracted for breach of contract. In fact, in a breach of contract suit or arbitration, the damages that can be sought may greatly exceed the amount that can be subject to a construction lien, because breach of contract claims are not subject to the specific procedural requirements and restrictions applicable to construction liens.

Parties Entitled to File a Construction Lien

The Three Tiers

Contractors, subcontractors and suppliers in the first three contractual tiers who provide work, services, material or equipment are entitled to file construction liens. To file a construction lien, two requirements must be met:

1. The claimant must provide work, services, material or equipment under a signed contract or a signed contract amendment. -and-
2. Subject to certain additional requirements discussed below, the claimant must be within the first three levels, or "tiers," in the construction process.

The first tier is the prime contractor (or construction manager) in privity with the owner. In addition, the law permits construction managers, architects, engineers and surveyors in privity with the owner to file liens.

The second tier is the subcontractor or supplier in privity with the prime contractor, or the subconsultant in privity with the architect or engineer. The third tier consists of subcontractors or suppliers having contracts with subcontractors who are in direct privity with contractors. Suppliers to suppliers do not have lien rights.

Summary of the Categories of Lien Claimants

Pursuant to the CLL, only certain parties are entitled to file a construction lien. Below is a list of such parties:

- General contractors
- Licensed architects, engineers, land surveyors, certified landscape architects and professional planners who contract with the owner
- Construction managers
- Prime contractors on a multiple prime project
- Subcontractors to a general contractor, a prime contractor or a construction manager
- Sub-subcontractors to a subcontractor
- Suppliers who have a contract with the owner, a general contractor, a prime contractor, construction manager or a subcontractor

Licensed Trades

There is one important limitation as to who can file a construction lien, with respect to licenses. If the work to be performed requires a license, then any party who performs it without a license has no lien rights. This includes architects, engineers, plumbers, HVAC contractors and electricians.

The Written Contract Requirement

For a lien claimant to be entitled to a lien, the claimant must have provided work, services, material or equipment pursuant to a signed written contract. For suppliers of material or equipment, this shall be in the form of a contract between the supplier and the person who ordered the supplies or a delivery slip or order slip, either of which must be signed by the person to whom the supplier has furnished material or equipment.

Although a written contract must include a contract price, the statute does not preclude the possibility that a contract price can include unit pricing or cost plus pricing where the measurement of the price elements are not left to uncertainty. However, the price must be calculable from the terms of the contract.

Contract Amendments

A construction lien can only be filed for written, signed amendments. Usually, a written contract amendment is a change to the contract that has been agreed to by both construction parties. In most instances, it will be in the form of a change order or contract modification.

If a contractor files a lien and is later owed more money because more work is performed under a written change order, the contractor can file an amended lien claim that includes the additional amount.

Amended lien claims can also be used to correct a mistake in a previously filed lien claim. Amended lien claims may be filed by any party that is entitled to file the original lien claim under N.J. Stat. § 2A:44A-3.

Types of Work Creating Lien Rights

If there is a written contract or a written contract amendment, almost any type of construction work supports a lien. Thus alterations, reconstruction work and additions are lienable in the same manner as new construction. Furthermore, a lien for services may attach to the property if there is only a proposed improvement to the property, but no actual construction work. Thus, an architect in direct contract with the property owner who prepares a detailed design for a building which is not actually used, or a construction manager retained to perform surveys, value engineering and preconstruction studies, may still file a lien for the work performed if he or she is not paid in accordance with their written contracts. However, a lien can only be claimed with respect to work or material already provided. Also, the amount of the lien cannot include lost profits for work not performed.

In general, a claimant may assume that any work on the construction site supports a lien. The following are examples of the types of work for which liens may attach:

- Design work on a building
- Performing construction management services
- Building a house, an office building, a warehouse, or a manufacturing facility
- Excavating a basement
- Rewiring a house
- Building an addition
- Installing a permanent generator outside of an office building even if there is no construction work on the office building itself
- Building a dock
- Supplying lumber for construction of a particular building (a construction lien may be filed for the full value of the lumber even if some of it is waste that is not actually used or incorporated into the building)
- Repair or renovating a building
- Landscaping and grading

Categories of work not covered include:

Equipment or material purchased by a claimant but not intended for a specific project. Thus, a contractor who buys a crane for use on several projects may not file a lien against one project for the full value of the crane. The use of the crane on a particular project, however, is lienable work.

When the purchase price of material utilized at an otherwise lienable improvement is secured by documentation. For example, where a UCC-1 may be filed the seller of that material may not file a lien.

- "Evaluate work" where no construction work is proposed or occurs because no property is being improved may not be the basis of a construction lien. The most common example would probably be an engineer's feasibility study that does not result in the initiation of a project. The statute requires that the study must be for a proposed or actual physical change to the property.
- Personal property that does not become a part of the real estate.
- Public works.

The Amount of the Lien

A lien claimant is automatically entitled to a construction lien for the value of the work or services performed, or materials and equipment supplied as measured by the contract price, to the extent the contract price has not been paid. However, one cannot lien for work yet to be performed or for lost profits on work that has not been performed. Nor can one lien for delay damages or other costs that are not within the contract price.

A construction lien amount can never exceed the price of the contract between a contractor and a property owner less the payments made against that contract. Thus, a subcontractor's or supplier's lien is limited, not only by the balance of its own contract, but also by the balance of the contractor's contract. This same rule is applied to sub-subcontractors and suppliers to subcontractors, whose lien rights are limited by the balance of their own contracts as well as the balances of the contractor's and subcontractor's contracts. These limits are set in order to prevent the property owner or other party in the contractual chain from having to pay twice for the same work.

A materials supplier has a duty to apply the contractor's payments to the individual project account from which those payments were derived. It must ascertain the source of the payments it receives, and allocate those payments correctly. In 2004, New Jersey's Supreme Court held that, if a payor (such as a contractor) is under a duty to a third person (such as an owner) to devote money paid by him to the discharge of a particular debt, the payment must be so applied if the creditor (such as a materials supplier) knows, or has reason to know, of the payor's duty, in spite of the fact that the payer directs that the payment shall be applied to the discharge of another debt. *Craft v. Stevenson Lumber Yard Inc.*, 843 A.2d 1076 (N.J. 2004). The Appellate Division has since interpreted *Craft* as holding only that a supplier has a duty to allocate payments correctly only "if the supplier 'knows or should know' the source of the payment" that it received. *L&W Supply Corp. v. DeSilva*, 57 A.3d 558 (N.J. Super. Ct. App. Div. 2012).

Time Limits for Filing a Lien Claim and Foreclosing on a Lien Claim

A lien claim is only valid if filed with the clerk of the county or counties where the project is located within a statutorily prescribed time period. For commercial projects, the construction lien must be filed within 90 days from the date the lien claimant's last work or services were furnished. The 90-day filing period is statutory and may not be extended by warranty work, service calls, miscellaneous work after completion or termination of the contract. This time period cannot be extended by agreement of the parties.

For residential and mixed-use projects, the claim must be filed 120 days from the date of the lien claimant's work. For residential construction, a notice of unpaid balance (NUB) must be filed within 60 days of the last day worked and arbitration must be initiated for permission to file a lien. The whole process must be completed within the 120-day period

noted above. Residential rules apply to condominium projects and planned unit developments as well as mixed residential and business use projects.

Any lawsuit to foreclose a lien must be started within one year from the date the work or services were last furnished. This time limitation is also not flexible. Owners who want to force a lien claimant to court also have the right to make a written demand upon the lien claimant that an action must be started within 30 days. Failure to sue within the 30 days will result in the lien claimant's forfeiture of lien rights.

Service of Claim

In addition to filing with the county clerk, the lien claim must also be personally delivered or sent by registered or certified mail to the owner within 10 business days after filing. Subcontractor lien claims must be similarly served on general contractors. However, in contrast to the rigidity of the filing limitation, if service is untimely, the lien claim is still valid unless the party who is served can show that it suffered some demonstrable impact or material prejudice. If the owner disburses funds without actual knowledge of the filing of the lien claim, that disbursement meets the owner's initial burden of showing material prejudice.

Penalties

One of the major innovations of the CLL is its significant penalties for filing an invalid lien or failing to adhere to the statutory requirements. The potential penalties include payment of the other party's attorneys' fees, court costs and any damages. These liabilities apply to:

- Filing an exaggerated lien. Liabilities will also be imposed against a claimant who files a lien claim "without basis," if the amount is "willfully overstated," or the filing is not in a substantial form, manner or within the time required by law. The contractor will also forfeit its right to file a later lien for the face amount of the first lien. Liens for additional work, however, are not affected.
- Raising a defense to a lien that is "frivolous or without basis"
- Failing to discharge a lien when the time to sue has expired
- Failing to discharge a lien within 30 days after it has been paid, settled, satisfied or forfeited
- Serving a verified list that omits a potential claimant

Discharge of Lien

The CLL provides simple methods to discharge property from a lien. When a lien claim has been paid, satisfied or settled by the parties or forfeited by the claimant, the claimant is required to file a certificate of discharge within 30 days in the county where the project is located.

If the claimant fails to discharge a lien, the claimant will be liable for all court costs and legal expenses incurred to obtain that discharge of the lien. In addition, the claimant may also be liable for damages sustained by all adversely affected parties.

The CLL provides that a lien claim may be discharged by a county clerk upon:

- The filing of a surety bond or deposit of funds in an amount equal to 110% of the lien claim
- The receipt of a certificate of discharge -or-

- Pursuant to an order of discharge by the court

At any time, a surety bond or a deposit of funds with the court equal to 110 percent of the lien claim may be posted to substitute security for debt instead of the lien property.

Any surety bonds deposited in court should be discharged and/or returned if certain filings are made to the clerk of the court. These are:

- A certificate of discharge from the lien claimant
- A court order
- A judgment dismissing the case against the owner -or-
- A final stipulation of dismissal of the case by the claimant

Waiver of Lien Rights

The CLL holds that agreements waiving construction lien rights are against public policy and therefore the CLL makes such agreements unenforceable. There is however an exception: where the waiver is given in consideration for payment for work, services, materials or equipment. In such case, the waiver is effective only if the payment is actually received.

Special Rule for Leaseholds

If a tenant contracts for improvements that are not authorized in writing by the property owner/landlord, the lien attaches only to the lease and not to the underlying property unless the owner has authorized in writing that the improvement and its interests are subject to a lien, has paid or agrees to pay the majority of the costs of improvement, or agrees in the lease that its interests are subject to a lien.

Forms

The CLL prescribes forms for construction lien claims, amendments of liens, NUBS, bonds for discharging liens and certificates to discharge a lien claim.

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