Real property transfers prior to filing a mechanic’s lien and a contractor’s recourse under the lien law - by Andrew Richards and Giulia Escobar

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Transfers of real property prior to filing a mechanic’s lien do not completely extinguish a contractor’s recourse under the lien law

Generally speaking, pursuant to New York Lien Law §10, a mechanic’s lien can be filed at any time during construction and within eight months after the last day work is performed at the project. A

mechanic's lien does not create liability of the owner to the contractor or subcontractor. Rather, the mechanic's lien is security to enforce any judgment that the contractor or subcontractor obtains against the owner whereby the liability of the owner is established. The time to file a mechanic's lien on a single-family residence is four months. So, what happens if a contractor performs work at a project and the property is sold within the eight-month period? Can the contractor still file a lien? Is the contractor without any recourse against the property? Is a subcontractor in an even worse position since it does not have a contract with the owner and the contractor may not have funds to pay the subcontractor?

Once an improved property is sold and a deed recorded, a subsequently filed mechanic's lien by a contractor or subcontractor would be unenforceable against the property. Setting aside a contractor's or subcontractor's right to bring a breach of contract action, all is not lost. Subsection 5 of Lien Law §13 provides some relief to contractors and especially subcontractors if they did not file a lien prior to the sale of the property and recording of the deed. Said subsection states in pertinent part that "[n]o instrument of conveyance recorded subsequent to the commencement of the improvement, and before the expiration of the period specified in section ten of this chapter for filing of notice of lien after the completion of the improvement, shall be valid as against liens filed within a corresponding period of time measured from the recording of such conveyance, unless the instrument contains a covenant by the grantor that he will receive the consideration for such conveyance and will hold the right to receive such consideration as a trust fund to be applied first for the purpose of paying the cost of the improvement and that he will apply the same first to the payment of the cost of the improvement before using any part of the total of the same for any other purpose."

First, if this language is not in the deed, any lien filed within the eight or four-month period is valid against the purchaser of the property. However, almost all deeds, especially bargain and sale deeds, have this language. Assuming the language is in the deed, then what? Then the contractor and subcontractor have a claim against the "trust" funds that are paid to the seller by the purchaser of the property. This will give rise to an additional cause of action for the contractor and subcontractor in addition to their garden-variety breach of contract actions. The additional cause of action is for a breach of the trust obligations under the statute in the event the trustee (i.e., the seller of the property) does not retain the funds to pay for the improvements of the property. Then, if for some reason the trustee, which is generally a corporation or limited liability company, has no funds to pay the claims, the contractor and subcontractor may recover the sums from the individuals who knowingly made the transfer of funds. This is analogous to a claim under Article 3-A of the Lien Law for diversion of trust funds and a claim of fraudulent conveyance under the debtor-creditor law.

Personal liability for a breach of the trust is grounded in the notion that the contractors and subcontractors who provided the improvements to the property are beneficiaries of the trust created by Lien Law §13(5). The aspect of personal liability is the deterrent to the distribution of the trust funds by the corporation or limited liability which may not care if they incur the same liability as a breach of contract claim. Liability of the corporation or limited liability company alone would not provide any greater security or relief as the garden variety breach of contract claim. Clearly, without the personal liability aspect of a breach of the Lien Law §13(5), contractors and subcontractors who

do not get paid by the owner would not have any true recourse under the Lien Law if the lien is not filed prior to the sale of the property and recording of the deed.

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