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CONSTRUCTION CITES

A periodic bulletin citing and analyzing legal and other developments affecting the construction industry

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ILLINOIS MECHANIC'S LIEN ACT UPDATES

The Illinois courts have recently considered the strict scrutiny requirement under the Illinois Mechanic's Lien Act, 770 ILCS 60/1 et seq. (the "Lien Act"), with respect to notice of liens. The courts have also reviewed the definition of "completion" under the Lien Act, contractual arbitration provisions, the fiduciary duty owed to a subcontractor and the general contractor's duty to provide sworn statements to the owner.

Section 24 of the Lien Act Provides for the Notice That Is Required to Perfect a Claim for Mechanic's Lien and Must Be Strictly Construed

Faxed Notice of Potential Lien Claim Is Insufficient under Section 24 of The Lien Act. In *Seasons-4, Inc. v. Hertz Co.*, 788 N.E.2d 179, 272 Ill. Dec. 875 (1st Dist. 2003), the Illinois Appellate Court held that failure to strictly comply with the notice requirements under the Lien Act bars a subcontractor's suit to foreclose on a mechanic's lien. In this case, plaintiff subcontractor Seasons-4 ("Seasons") entered into a contract with defendant general contractor Crown Temperature Engineers, Inc. ("Crown") to provide an air-conditioning unit. When Crown failed to pay Seasons for the AC unit, Seasons faxed a letter to the owner, Hertz, within ninety days of delivery of the unit, indicating the outstanding balance. Seasons then served a notice of claim for lien on Crown after ninety days had elapsed since delivery of the unit and also filed a foreclosure action. Crown brought a motion to dismiss on the grounds that Seasons failed to serve timely notice of its lien claim. Seasons countered that the facsimile notice of the amount outstanding qualified for notice of a lien claim in accordance with section 24 of the Lien Act.

The appellate court disagreed with Seasons and concluded that the specific procedure for certified or hand delivery of the notice of lien claim under the Lien Act was a substantive requirement that must be strictly construed. In addition, the court noted that the content of Season's facsimile notice did not serve to notify the owner or the general contractor that Seasons was asserting any claim.

Subcontract Notice of Lien Claim to the Recorder's Office Will Not Be Sufficient under the Lien Act If the Owner, Agent, Superintendent and/or Architect Is a Resident of the Location of the Project or Can Be Located. In *Rothers Construction Inc. v. Centurion Industries, Inc.*, 786 N.E.2d 644, 272 Ill. Dec. 105 (4th Dist. 2003), the Appellate Court of Illinois held that a subcontractor failed to comply with the notice requirements of the Lien Act when it served notice of its lien claim with the recorders' office. In this case, Rothers Construction ("Rothers") contracted with Centurion Industries, Inc.

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d/b/a A-Lert Construction to build grain bins and material handling systems for the owner, O'Malley Grain, Inc. Rothers completed the required services and three months later served notice of its lien claim and recorded it with the office of the recorder of deeds against the owner's property and filed a suit to foreclose.

The owner moved to dismiss the complaint arguing that the lien was not properly perfected due to the fact that the owner had not received notice of the lien claim in accordance with section 24 of the Lien Act. Rather, Rothers had only served its ninety-day notice on the recorder of deeds in accordance with section 25 of the Lien Act. Pursuant to section 25 of the Lien Act, a subcontractor's ninety-day notice may be served on the recorder of deeds if the owner is not a resident of the county where the project is located or if it does not have any representative at the job site.

The trial court, however, dismissed Rothers' foreclosure action, finding that the owner had a representative at the project and, thus, notice should have been perfected under section 24 of the Lien Act. In affirming the trial court's dismissal, the appellate court reiterated that proper notice under the statute is a prerequisite for the creation of a lien. Absent the required ninety-day notice under section 24 of the Lien Act, a lien is never created. In addition, when an owner does not receive timely written notice, as in this case, no lien attaches. The appellate court concluded that notice was required under section 24—and not under section 25, as Rothers had argued. Under section 24, only after reasonable diligence has been made to find the owner or its surrogates may notice through the recorder of deeds be appropriate. In this case, the owner had a representative at the job site three to four times per week. The subcontractor's failure to use reasonable diligence to serve the owner's representative, in this case, barred the subcontractor's rights to assert a mechanic's lien.

Accurate Description of the Contract Is a Prerequisite for Perfecting a Lien Claim

In *Bale d/b/a Bale Excavating v. William Barnhart*, 2003 WL 21702482 (4th Dist. 2003), the court dismissed a general contractor's mechanic's lien action on the grounds that it failed to identify specific information in its lien claim in violation of section 7 of the Lien Act. Specifically, the contractor, Bale, timely recorded its lien claim in accordance with section 7 of the Lien Act. Bale also brought an action to foreclose after four months had elapsed since its completion of work on the project. The lien claim, however, failed to accurately describe the parties to the contract. Accordingly, the owner, Barnhart, and the mortgagee, Huntington, brought motions to dismiss, which were sustained.

The appellate court affirmed the trial court and concluded that a description of the contract within the meaning of section 7 of the Lien Act includes an accurate description of the parties to the contract. Bale's lien claim, on the other hand, interchanged the actual claimant's name with the name of the individual who prepared the lien claim.[1] Thus, the holding of this case only pertains to the rights of the third-party mortgagee. The court held that such an ambiguity in the contract description rendered the description inaccurate pursuant to section 7 of the Lien Act and thus invalidated the lien claim. Moreover, because Bale's foreclosure action was filed after four months of completion of the project, Bale had no preserved lien rights that it could assert as to Huntington.

The Completion Date under the Lien Act Is Not the Completion of the Contract

In *Citizen Savings Bank v. Covey*, the U.S. Bankruptcy Court for the Central District of Illinois, 2002 Bankr. LEXIS 997 (2002), the plaintiff mortgagee, Citizen Savings Bank, moved for summary judgment on complaints regarding several mechanic's liens filed by Gingerich Plumbing Co. ("Gingerich") on land owned by the debtor, PAK Builders, on the grounds that the lien claims were recorded more than four months after the work had been performed and that, therefore, the bank had priority over Gingerich's liens in the bankruptcy proceedings. In this regard, the bank asserted that Gingerich was required to file its lien within four months of the last date the work

[1] The appellate court only considered the order dismissing the matter as to the mortgagee, Huntington, on the grounds that the court did not find the dismissal of Barnhart's action to be final and appealable.

was performed, even if the contract work was not fully completed.

Gingerich's contract provided for work to be performed on multiple parcels of land arising under one contract. Gingerich prepared separate lien claims for each of the parcels but did not record some of the claims within four months after the completion of the work on the specific parcel. Gingerich argued, however, that, pursuant to section 7 of the Lien Act, the four months did not begin to accrue until after the completion of the overall contract.

The court disagreed and held that, in Illinois, the four-month period in which to record a lien claim begins to accrue with the completion of the work for which the claimant seeks to assert a lien. Because Gingerich had completed its work more than four months prior to the filing of the lien claims as to the lots at issue, those claims were deemed invalid, even though the claims had been recorded within four months of completion of the overall contract.

Filing a Lien Claim Does Not Waive Arbitration

A party does not waive its right to arbitrate a dispute by filing a mechanic's lien before requesting arbitration, *LaHood v. Ill. Constr., Inc.*, 335 Ill. App. 3d 363, 781 N.E.2d 585, 269 Ill. Dec. 788. In this case, Lahood (the owner) contracted with plaintiff contractor, Illinois Construction, Inc. ("Illinois Construction"), to build a shopping center. Illinois Construction filed a mechanic's lien against the owner's property after a dispute arose regarding the project. Subsequent to filing the lien, Illinois Construction pursued arbitration under the Illinois Uniform Arbitration Act as was provided under its contract with the owner. Illinois Construction then immediately filed an action pursuant to section 24 of the Lien Act. The trial court held that Illinois Construction retained its right to arbitrate irrespective of any lien it filed.

The owner appealed, arguing that by filing a mechanic's lien action Illinois Construction waived and abandoned any contractual right they may have had to arbitrate the issue. The owner also claimed that by attempting to adjudicate the same issue in two different forums, Illinois Construction acted inconsistently with the arbitration clause. Illinois Construction, in turn, argued that they did not act inconsistently with the arbitration clause because it requested arbitration before it was forced to file a lien against the owner's property and sought thereafter an immediate stay of the claim pending the arbitration results.

On appeal, the appellate court affirmed. While the court noted that a contractual right to arbitration may be waived, it held that first seeking arbitration and subsequently filing a mechanic's lien action was not inconsistent with the arbitration clause in the agreement. Generally, waiver of the right to arbitrate occurs when a party acts in a manner inconsistent with the clause and serves as an abandonment of such right. In this case, Illinois Construction did not act inconsistently, but rather simply "sensibly" protected its lien interest in the property, the time limitations for which will not be suspended pending an arbitration proceeding. Moreover, by requesting a stay of the lien action pending arbitration, Illinois Construction reserved its right to arbitrate.

A Fiduciary Duty Pursuant to Section 21.02 Will Arise If a Lien Waiver Is Submitted for Payment

In *Doing Steel, Inc. v. Castle Construction, Corp.*, 2002 U.S. Dist. LEXIS 22836 (2002), the U.S. District Court for the Northern District of Illinois held that a fiduciary relationship did not arise between a contractor and subcontractor upon the contractor's receipt of money owed to the subcontractor for work performed. In this case, defendant Castle Construction Corp. ("Castle") contracted with Illinois School District No. 148 to build a new school and with Doing Steel, Inc. ("Doing Steel") to provide the labor and materials to complete the steel work on the project. Castle paid Doing Steel for their work on the project performed before January 31, 2000. After January 31, Doing Steel continued to work on the project and Castle continued to request payment for Doing Steel's services from the school district during this time.

Castle, however, received payments from the school district for Doing Steel's services, Castle failed to ever

pay Doing Steel. As a result, Doing Steel filed a complaint alleging, amongst other claims, that Castle breached a fiduciary duty owed to a subcontractor under section 21.02 of the Lien Act. Doing Steel argued that the Act created a fiduciary duty between a contractor and a subcontractor when the former receives compensation due the latter, regardless of whether the subcontractor had issued a lien waiver. The district court rejected this argument and held that such a fiduciary duty only arises when a subcontractor submits its lien waiver to the general contractor.

Failure to File Sworn Contractor Statement Did Not Prevent Recovery for Breach of Contract

In a recent Second District case entitled *Northwest Millwork Co. v. Komperda*, 338 Ill. App. 3d 997, 788 N.E.2d 399 (2003), an owner challenged a general contractor's rights to assert a breach-of-contract action against the owner on the grounds that the contractor failed to submit a sworn statement under section 5 of the Lien Act. The owner argued that section 5 of the Act imposes an obligation on the contractor to submit a sworn statement from its subcontractors in connection with payments for the same to protect the owner from third-party subcontractor claims.

The owner relied on *Abbott Electric v. Ladin*, 144 Ill. App. 3d 974, 977, 494 N.E.2d 1251 (1986), which held that, pursuant to section 5 of the Lien Act, when a contractor has been asked by an owner to submit a sworn statement and fails to do so, the contractor will be barred from asserting a breach of contract action against the owner. The contractor in *Northwest* argued, relying on *Wrecking v. Midwest Terminal Corp.*, 234 Ill. App. 3d 750, 601 N.E.2d 999 (1992), that section 5 neither expressly nor impliedly bars contract actions where the contractor fails to submit a sworn statement.

The *Northwest* court agreed with the contractor and distinguished the *Abbott* case on the grounds that in this instance the owner had no risk of third-party claims from subcontractors and had not previously requested that a sworn statement be submitted by the contractor. Consequently, the court could not find that as a matter of law the contractor's failure to provide a sworn statement prevented it from pursuing a breach-of-contract action against the owner.

TRUSTEES OF COLLECTIVE BARGAINING AGREEMENTS HAVE STANDING TO ASSERT LIEN RIGHTS

Illinois has recently recognized that the trustees of a collective bargaining agreement have standing under the Lien Act to assert a lien against the owner. In addition, over the past few years, other jurisdictions have reached similar conclusions.

Fringe Benefits Are Lienable Items under the Illinois Mechanic's Lien Act

In *Divane v. Smith*, 332 Ill. App. 3d 548, 774 N.E. 2d 361 (1st Dist. 2002), the Illinois Appellate Court held that the trustee of a fringe benefits fund had standing under the Lien Act to pursue past-due contributions that the subcontractor employer failed to pay the electrical laborers. In *Divane*, the subcontractor utilized electricians from Local 134 pursuant to a collective bargaining agreement under which the subcontractor was to pay contributions to the employees. When the subcontractor failed to make such payments, the trustee sued on behalf of the fund and asserted a lien claim against the Board of Education of Chicago (the owner). In addition to arguments brought by the owner and the general contractor regarding the trustee's failure to comply with the notice requirements of section 23(b) of the Lien Act, which position was subsequently reversed by the appellate court, the owner and general contractor also challenged the trustee's standing under the Lien Act to assert a lien claim.

The First District reversed the lower court and found that the trustee's right to assert a lien claim was analogous to those issues raised in *United States ex rel. Sherman v. Carter*, 353 U.S. 210, 77 S. Ct. 793 (1957), in which the trustees of a benefit fund sued the surety on a contractor's payment bond when the contractor failed to make required

contributions to the fund. The *Sherman* court analyzed that the trustees in that instance stood in the shoes of the laborers and had standing to pursue outstanding contributions against the payment bond, which was there for the protection of the subcontractors. Similarly, in the *Divane* matter, the court likened the trustee to those in *Sherman* in that it stood in the electrician's shoes and was entitled to enforce its rights and thus had standing under the Lien Act.

In Nebraska, Any Person Who Furnishes Materials or Services to a Real Estate Improvement Contract May File a Construction Lien

In a recent case entitled *Omaha Construction Industry Pension Plan v. Children's Hospital*, 11 Neb. App. 35, 642 N.W.2d 849, the Nebraska Court of Appeals held that union employees of a subcontractor had standing to file a lien against a property owner. In this case, the owner, Children's Hospital, entered into a general contract with Kiewit Construction Co. ("Kiewit"), who in turn subcontracted with Borchman Construction Co. ("Borchman"). Borchman hired several union members to complete the job. The compensation for these employees included their hourly pay as well as contributions to the health and welfare plans of the union. After Borchman failed to make the required contributions, the plan, on behalf of the employees, filed a mechanic's lien against the owner and a petition to foreclose the lien. The trial court dismissed the action on the grounds that the plan did not have standing under the Nebraska Mechanic's Lien Act to assert a lien claim.

In reversing the trial court, the appellate court first concluded that the subcontractor's employees could file a construction lien against a property owner. In reaching this conclusion, the court noted that the Nebraska Lien Act entitled any person who furnishes materials or services to a real estate improvement contract to file a construction lien. The court further held that the plan itself had standing to both file and enforce a lien on behalf of its employees, likening the trustee relationship to that of an assignee to a lien claim. Finally, the court ruled that the plan sufficiently pled a cause of action by alleging that the union employees furnished services and materials and did not receive the full amount of their contract price.

In Oregon, Lien Statute Gives the Lien Claimant, Not the Union, the Right to Enforce a Lien

In *International Brotherhood of Electrical Workers Local No. 48 v. Oregon Steel Mills*, 168 Ore. App. 101, 5 P.3d 1122 (2000), the Court of Appeals of Oregon held that while the trustees of a collective bargaining agreement had standing to foreclose a lien under Oregon's construction lien statute, the union and collection agency involved with unpaid contribution funds did not have such standing. In *International Brotherhood*, defendant Oregon Steel Mills (OSM) utilized laborers from Industrial Construction Services, Inc. (ICS) on several construction projects. The laborers performed under the terms of a bargaining agreement entered between Local 48 and the Oregon-Columbia Chapter of the National Electrical Contractors Association. Under this agreement, employers were required to make contributions to various union trust and administrative funds. ICS failed to make the required contributions, and consequently the union, the trustees and collection agent filed notice of a construction lien for the delinquent contributions.

The trial court, however, dismissed the lien claims on the grounds that neither the union nor the collection agency had standing to foreclose on a lien. The trial court also held that the trustees, however, did have standing to enforce the lien because the legislature had specifically provided for this remedy in the lien statute that related to the rights of trustees to collect outstanding dues. The Court of Appeals affirmed the trustee's standing on the grounds that the statute had been amended to specifically include a remedy for trustees of trust funds. However, because the lien statute did not specifically include unions and collection agencies, the court denied them the right to assert a lien claim.

In Hawaii, Trustees of an Employee Benefit Trust Fund, in an Attempt to Enforce Employer's Obligation to Contribute to the Fund, File a Mechanic's Lien on the Property Improved through the Work of the Laborer

The Supreme Court of Hawaii in *Hawai'i Laborers' Trust Fund v. Maui Prince Hotel*, 81 Haw. 487, 918 P.2d 1143 (1996), has also ruled that the Hawaii Laborer Trust Fund could assert a lien claim under the Hawaii Mechanic's Lien Act for delinquent trust fund contributions. In this case, the Maui Prince Hotel Corporation and Wailea Resort Company, Ltd. (the owners) contracted with Greenscape, Ltd. ("Greenscape") to build two golf courses. Greenscape in turn contracted with Hunnicutt International, Inc. ("Hunnicutt") to perform the landscape and construction work for both golf courses, and Hunnicutt contracted with Local 368 to provide labor for the work. In addition, Hunnicutt executed labor agreements with the union in which they promised to make contributions to the fund for each labor hour worked. Hunnicutt paid the laborers for their work but failed to make the required contributions to the fund. The fund subsequently brought suit for back contributions and obtained a default judgment against Hunnicutt. The fund also brought suit against the owners, claiming they were liable for Hunnicutt's failure to make the agreed-upon contributions.

The fund asserted a mechanic's lien against both golf course projects and asserted its right to foreclose. The trial court dismissed the fund's foreclosure action, concluding that it was preempted by ERISA. The trial court did not, however, address whether the fund had standing under the Hawaii Lien Act or whether a claim for contribution constituted lienable services under the Lien Act. The fund appealed to the Supreme Court of Hawaii, which reversed the trial court's ruling as it related to ERISA. The supreme court further confirmed that the fund under a collective bargaining agreement seeking past-due compensation of employees that performed work on a construction project was an association furnishing labor and materials within the meaning of the Hawaii Lien Act.

Wisconsin Recognizes That Contribution Funds Can Be Recovered under Construction Lien Law

In *Plumber's Local 458 Holiday Vacation Fund v. Immel*, 151 Wis. 2d 233, 445 N.W.2d 43 (Wis. Ct. App. 1989), the Court of Appeals of Wisconsin affirmed a lower court ruling and held that unpaid benefit contributions to Local 458's holiday vacation fund, pension fund, health fund, industry fund, and union office assessment fund may be recovered under the construction lien law. In this case, Howard Immel, Inc. (the contractor) contracted with Appleton Papers, Inc. (the owner) to finish a construction project. The contractor subcontracted with Augie's Construction to perform the plumbing work on the project. The subcontractor employed labor from Local 458 pursuant to a collective agreement. As part of this agreement, the subcontractor was to make contributions to the various funds on behalf of its employees.

When the subcontractor failed to make the contributions, the union local asserted a lien claim on behalf of the employees and sought to foreclose on the same. The contractor argued in opposition, in part, that contribution dues were not "wages" under the Wisconsin Lien Act. The trial court rejected the contractor's argument and ruled in favor of the union local.

The Court of Appeals of Wisconsin affirmed the decision reached by the trial court and held that, even if a construction lien only applies to unpaid wages, the term "wages" included not only the hourly rate, but also contributions for vacation, pension and health insurance benefits. In so holding, the court refused to interpret the construction lien statute so narrowly as to undercut the very purpose of the law itself.

A CONSTRUCTION COMPANY COULD BE CHARGED WITH CRIMINAL BEHAVIOR

In a case of first impression, on May 1, 2003, the U.S. District Court for the Northern District of Illinois dismissed a two-count indictment against one of two electrical

contractors criminally indicted for willfully violating Occupational Safety and Health Administration regulations. On December 11, 2002, MYR Group, Inc. ("MYR") and its wholly owned subsidiary, L.E. Myers Co. ("L.E. Myers"), both electrical contractors, were charged in a four-count indictment for alleged workplace safety violations stemming from the deaths of two L.E. Meyers employees, who were both electrocuted while working on high-voltage transmission towers. MYR and L.E. Myers, prior to the dismissal, were each facing a two-count indictment, one count arising from each death. If convicted of the charges, misdemeanor in nature under the OSHA statute, the companies each face a fine up to $1 million and a maximum penalty of five years probation. The indictment alleges that both defendants failed to properly oversee and conduct safety training, instruction and enforcement for its employees.

Magistrate Judge Geraldine Brown heard arguments on MYR's motion to dismiss the indictment and ultimately dismissed the two counts. In its decision, the court agreed with MYR's argument that ultimately only the employees' employer had responsibility for ensuring that employees received the proper job-site training. The court further rejected the government's contention that *U.S. v. Pitt-Des Moines, Inc*. was controlling, wherein an employer who creates a safety hazard can be liable regardless if those threatened are its own or another's employees. Unlike *Pitt*, where the defendant's violation created a hazard which ultimately led to the death of two employees, MYR is not charged with violating any obligations owed to its own employees. The regulations alleged to have been violated related to the employees of L.E. Meyers, not MYR. Moreover, the court determined that it found no indication in the indictment that suggested that MYR had any hand in creating the physical condition which created the hazard. The allegations also fail to establish that MYR represented a "controlling" employer at the work sites.

Finally, the court held that there was no support in law or in the allegations of the indictment for the argument that MYR could be held liable as a "joint employer." No authority was presented to sustain the imposition of criminal liability on an entity, like MYR, which provided training to the employee but was not the employer of the injured employee. This failure proved fatal, in the court's view. Ultimately, the court failed to find the required foundation to support the criminal indictment against MYR and dismissed the indictment.

The U.S. Attorney for the Northern District of Illinois appealed the dismissal of the indictment ordered by the district court to the United States Seventh Circuit Court of Appeals. The two-count indictment against L.E. Myers Co. still stands and is pending before the court.

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Vedder, Price, Kaufman & Kammholz, P.C.

Chicago
222 North LaSalle Street
Chicago, Illinois 60601
312/609-7500
Fax: 312/609-5005
Robert J. Stucker

New York
805 Third Avenue
New York, New York 10022
212/407-7700
Fax: 212/407-7799
Alan M. Koral

New Jersey
354 Eisenhower Parkway, Plaza II
Livingston, New Jersey 07039
973/597-1100
Fax: 973/597-9607
John E. Bradley

www.vedderprice.com