



NCBANKERS

NORTH CAROLINA BANKERS ASSOCIATION

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## Legal Memorandum

August 30, 2013

Vol. 45, No. 4

TO: *Legal Memorandum* Mailing List

RE: Updates to North Carolina's Mechanics Lien Law

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In January, the NCBA published a *Legal Memorandum*, Vol. 45, No. 1, by Jim Creekman of the Ward and Smith law firm in which he summarized changes to North Carolina's mechanics lien law that were scheduled to go into effect April 1. After the North Carolina General Assembly made further technical and clarifying changes during the 2013 legislative session, Jim Creekman undertook the task of further updating his summaries and guidance. As his accompanying letter describes in more detail, this new *Legal Memorandum* replaces the document distributed in January. We thank him for his insights and perspective on the new laws.

Sincerely,

A handwritten signature in black ink that reads 'Nathan'.

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August 26, 2013

Mr. Nathan R. Batts  
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Post Office Box 19999  
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RE: Introducing Changes to North Carolina's  
Mechanic's Lien Law  
Our File 680000-00015

Dear Mr. Batts:

In January of this year, the North Carolina Bankers Association published in its Weekly Bulletin materials I prepared that addressed significant changes to North Carolina's mechanic's lien law adopted by the General Assembly in summer of 2012.<sup>1</sup> Some of the changes became effective July 12, 2012; others became effective January 1, 2013. However, the most important substantive changes – in particular, the provisions introducing the new lien agent process – became effective April 1, 2013.

Once the changes that were to take effect on April 1 of this year were carefully studied by the various stakeholders, it became apparent that some technical corrections were needed to clarify the intent of the drafters and to avoid some problems that were sure to arise. As a result, the General Assembly adopted two technical corrections bills during the 2013 legislative session, Session Law 2013-16 (which became effective April 1, 2013) and Session Law 2013-117 (which became effective June 22, 2013).

The materials I prepared for you in January of this year are now outdated – they need to be updated to reflect the two technical corrections bills adopted by the General Assembly in 2013.

Two documents accompany this letter:

1. A summary of the significant statutory changes enacted during the 2012 and 2013 legislative sessions; and
2. An outline that describes how, from a lender's perspective, North Carolina's mechanic's lien laws work subsequent to June 22, 2013, the date all of the statutory changes enacted in

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<sup>1</sup> 2013 Legal Memoranda, Vol. 45, No. 1 dated January 29, 2013.

WARD AND SMITH, P.A.

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2012 and 2013 became fully effective. I hope the outline will be useful as a reference tool for your members.

The two documents that accompany this letter supersede and replace the corresponding documents included with my letter that you published on January 29, 2013 in the NCBA's Weekly Bulletin as 2013 Legal Memoranda Vol. 45, No. 1.

Yours very truly,

  
James E. Creekman

**SUMMARY OF THE SIGNIFICANT CHANGES TO THE MECHANIC'S LIEN LAW  
ADOPTED BY THE NORTH CAROLINA GENERAL ASSEMBLY IN 2012 AND 2013<sup>1</sup>**

**1. Addressing the "Hidden Lien" Problem – Introducing the Lien Agent Process.**

The "hidden lien" problem is a product of the "relation back" rule. If a lien claimant (i) files (and thereby perfects) its claim of lien on real property within 120 days after the claimant last furnished labor or materials at the construction site, and (ii) subsequently commences an action to enforce that perfected claim of lien within 180 days after the claimant last furnished labor or materials at the construction site, then the perfected claim of lien "relates back" in time for priority purposes to the date the lien claimant first furnished labor or materials at the construction site. The resulting mechanic's lien will have priority over (and trump) the rights of any person who acquired an interest in, and any lender who acquired a lien on, the property subsequent to the date the lien claimant first furnished labor or materials to the construction site.

Between the date that labor or materials were first furnished at the construction site until the claim of lien on real property was actually filed with the Clerk of Superior Court, the lien was truly a "hidden lien" – nothing suggesting the existence or possibility of the potential lien appeared on public record and no amount of due diligence performed by a purchaser, lender, settlement agent, or title insurance company in anticipation of a real estate closing could guarantee there was no inchoate mechanic's lien that might, if timely perfected and enforced, have priority over the rights of the parties in the pending transaction.

The hidden lien problem has festered for years and has resulted in substantial and prolonged litigation, difficulties in selling and refinancing properties, millions of dollars in claims against hundreds of purchasers and lenders, and substantial losses to title insurance companies.

In an effort to address the hidden lien problem, the General Assembly introduced a "lien agent" process in North Carolina this year that is patterned, at least in part, after a similar process introduced several years ago in Virginia for residential construction projects. However, the lien agent process in North Carolina is not limited to residential construction projects.

North Carolina's new lien agent process now applies to any project to improve an owner's real property if the first furnishing of labor or materials at the site of the improvements occurred on or after April 1, 2013, and the total cost of the undertaking will be \$30,000 or more either (i) at the time the original building permit is issued, or (ii) if no building permit is required, at the time the contract for the improvements is entered into with the owner. However, regardless of the anticipated costs of the improvements, the owner may, but is not required to, designate a lien agent for improvements to an existing single-family residential dwelling unit that is occupied by the owner as a residence, or for the addition of an accessory building or accessory structure (as defined in the North Carolina Uniform Residential Building Code), the use of which is incidental to that residence.

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<sup>1</sup> Session Law 2012-175; Session Law 2012-158; Section 65.3(a)-(c) of Session Law 2012-194; Session Law 2013-16; and Session Law 2013-117.

With respect to projects that are outside the scope of the new lien agent law, the "hidden lien" problem continues unabated.

The lien agent concept is really quite simple – by requiring potential lien claimants to "identify" themselves early in the process (and well before the potential lien claimants must file their claims of lien on real property), a diligent purchaser, lender, settlement agent, or title insurance company in a real estate transaction can address the legitimate interests of potential lien claimants as part of the closing process and obtain appropriate lien waivers and subordinations – all without cluttering the public record.

Here is how the process works:

- (a) In any private project to improve real property that is subject to the new lien agent law, the owner of the construction site is required to designate a lien agent. The lien agent designated by the owner must be chosen from among the list of registered lien agents maintained by the North Carolina Department of Insurance. Only title insurance companies and title insurance agencies authorized to do business in North Carolina that have consented to serve as lien agent and registered with the North Carolina Department of Insurance for that purpose may serve as lien agent.
- (b) The identity of the lien agent and the lien agent's contact information will be readily available to all of the project's contractors and subcontractors.
- (c) A contractor, subcontractor, or supplier who wishes to preserve its right to assert a claim of lien on the real property will be required to send a simple one-page form (a "Notice to Lien Agent") to the lien agent announcing that it is a potential lien claimant working on or providing materials to the construction site. The Notice to Lien Agent can be sent before, during, or after the potential lien claimant furnishes labor or provides materials to the construction site.
- (d) Receipt by the lien agent of a Notice to Lien Agent puts the lien agent on notice that the potential lien claimant may at some future time assert and pursue a claim of lien on the real property.
- (e) The lien agent then serves as an information "clearinghouse." An interested party (*i.e.*, the property owner; a person who has contracted to purchase the property; a potential lien claimant; a lender, closing attorney, or settlement agent involved in a transaction involving the property; a title insurance company or title insurance agency issuing a title insurance policy on the property; and their respective authorized agents) may at any time request the lien agent to provide (and the lien agent is required to provide to any interested party requesting it) a listing of all of the potential lien claimants who have filed a Notice to Lien Agent with the lien agent. This permits the requesting party to identify all potential lien claimants, thereby reducing the risk of hidden liens. Thus, for example, a settlement agent should request the lien agent to provide a list of the potential lien claimants immediately before a loan closing in order to address any potential claims against the real property and obtain appropriate lien waivers and subordinations as part of the loan closing process.

- (f) To simplify the mechanics of the lien agent process, most of the title insurance companies licensed to do business in North Carolina banded together to create and implement an online website – <http://liensnc.com> – that permits (i) an owner (or, in certain cases, the owner’s custom contractor) to designate a lien agent online, (ii) a potential lien claimant to file a Notice to Lien Agent with the designated lien agent online, and (iii) an interested party to request and receive up-to-date information from the designated lien agent concerning the identity of potential lien claimants online.

It is important to understand that the basic lien rights of contractors and subcontractors (both with respect to claims of lien on real property and claims of lien upon funds) remain unchanged. However, in those transactions where the new lien agent law applies and is followed, the ability of a contractor or subcontractor to assert a claim of lien against real property and/or the priority of the lien claimant's resulting lien are influenced by whether (and when) the contractor or subcontractor delivers the statutory Notice to Lien Agent to the lien agent. Thus, subject to certain exceptions, the new lien agent law provides that a potential lien claimant (whether a contractor or subcontractor) may perfect a claim of lien on real property only if at least one of the following conditions is met:

- The lien agent received a Notice to Lien Agent from the potential lien claimant no later than 15 days after the potential lien claimant first furnished labor or materials.
- The lien agent received a Notice to Lien Agent from the potential lien claimant before an instrument is recorded that conveys an interest in the real property to a bona fide purchaser for value who is not an affiliate, relative, or insider of the owner and whose priority is protected by the State's recording statute, G.S. 47-18.
- The potential lien claimant filed a claim of lien on real property with the Clerk of Superior Court pursuant to G.S. 44A-11 before an instrument is recorded that conveys an interest in the real property to a bona fide purchaser for value who is not an affiliate, relative, or insider of the owner and whose priority is protected by the State's recording statute, G.S. 47-18.

In addition, the new lien agent law provides specific lien priority protection for lenders under certain circumstances. Subject to certain exceptions, when a lien claimant's claim of lien on real property is filed *after* a mortgage or deed of trust on the property for the benefit of one who is not an affiliate, relative, or insider of the owner has been recorded, the claimant's lien is automatically subordinate to the lien of the previously recorded mortgage or deed of trust unless either or both of the following conditions are met:

- The lien agent received a Notice to Lien Agent from the potential lien claimant no later than 15 days after the potential lien claimant first furnished labor or materials.
- The lien agent received a Notice to Lien Agent from the potential lien claimant before the date the mortgage or deed of trust was recorded.

While it represents a major first step in addressing the hidden lien problem, the new lien agent process does not fully resolve the problem – there are still some significant gaps, most notably (i) during the 15 days after a potential lien claimant first furnished labor or materials, (ii)

transactions outside the scope of the new lien agent law, and (iii) special exceptions for "custom contractors" and "design professionals."

## **2. Claims of Lien on Real Property – Perfection and Statutory Form Issues.**

In the past, a claim of lien was "perfected" if the claim of lien on real property was filed in the Office of the Clerk of Superior Court in the county where the real property is located within 120 days after the date the lien claimant last furnished labor or materials at the site of the improvement.

Several procedural changes regarding the perfection of a claim of lien on real property became effective on January 1, 2013.

First, in addition to filing the claim of lien on real property in the Office of the Clerk of Superior Court in the county where the real property is located within 120 days after the date the lien claimant last furnished labor or materials at the site of the improvement, the lien claimant must also serve a copy of the claim of lien on real property upon the record owner of the real property. If the claim of lien on real property is being asserted by a subcontractor or supplier by right of subrogation, the claim of lien on real property must also be served on the contractor through which subrogation is being asserted. Because a claim of lien on real property will not be perfected until it is both served and filed, both acts must, as a practical matter, occur within 120 days following the date the lien claimant last furnished labor or materials at the site of the improvement.

In addition, two changes were made to the statutory form used to assert a claim of lien on real property:

- A claim of lien on real property must now contain an affirmative certification of proper service.
- If the claim of lien on real property is being asserted by a subcontractor, it must now name the contractor through which subrogation is asserted.

If the claim of lien on real property is being asserted by a subcontractor by right of subrogation, G.S. 44A-23(a) now expressly permits a subcontractor to state in its claim of lien on real property either (i) the date of the first or last furnishing of labor or materials on the real property by the subcontractor making the claim, or (ii) the date of the first or last furnishing of labor or materials on the real property by the contractor through which the subcontractor's claim of lien is being asserted.

## **3. The "Bankruptcy Fix."**

In recent years, several bankruptcy cases have created confusion as to exactly when a lien upon funds arises or attaches, and therefore whether a notice of claim of lien upon funds can be served after a party in the contractual chain files bankruptcy.

Effective January 1, 2013, amendments to § 44A-18 resolve this issue. A lien upon funds "arises, attaches, and is effective immediately upon the first furnishing of labor, materials, or

rental equipment at the site of the improvement by a subcontractor." The lien is subsequently perfected "upon the giving of notice of claim of lien upon funds in writing to the obligor . . . ."

However, until a lien claimant serves a notice of claim of lien upon funds, "any owner, contractor, or subcontractor against whose interest the lien upon funds is claimed may make, receive, use, or collect payments thereon and may use such proceeds in the ordinary course of its business."

These clarifications are intended to permit a subcontractor to

- Serve a notice of claim of lien upon funds after another party "up the chain" files for bankruptcy, and
- Confirm the ability of a party in the contractual chain to apply funds in the ordinary course of its business until it receives a notice of claim of lien upon funds from a lien claimant.

#### **4. The Effect on a Subcontractor of a Lien Waiver Signed by a Contractor.**

The amendments to the mechanic's lien law adopted by the General Assembly in 2012 and 2013 clarified in a piecemeal fashion the effect a lien waiver signed by a contractor has upon a subcontractor's right to claim a lien on real property:

- According to G.S. 44A-20(d) and G.S. 44A-23(c), a lien waiver signed by a contractor before a subcontractor perfects its claim of lien on real property pursuant to G.S. 44A-11 is sufficient to waive the subcontractor's right to assert the contractor's claim of lien on real property by right of subrogation, but the contractor's lien waiver does *not* affect the subcontractor's right to a claim of lien upon funds or the subcontractor's right to assert a direct claim of lien on real property under the authority of G.S. 44A-20(d) when an owner/obligor improperly "pays over" the subcontractor's validly perfected claim of lien upon funds.
- According to G.S. 44A-23(a1) and G.S. 44A-23(b)(5), no action by a contractor will be effective to prejudice the rights of a subcontractor without the subcontractor's written consent once the subcontractor has perfected its claim of lien on real property in accordance with G.S. 44A-11. Otherwise (presumably), action on the part of the contractor will prejudice the rights of a subcontractor.

The basic and longstanding rule regarding lien waivers contained in G.S. 44A-12(f) was not changed by recent legislation. Simply stated, an agreement by a contractor or subcontractor to waive the right to file a claim of lien on real property or the right to serve a notice of claim of lien upon funds is against public policy and is unenforceable if the agreement is entered into in anticipation of and in consideration for the awarding of any contract, either expressed or implied, for the making of an improvement on real property. However, a subsequent waiver supported by adequate consideration is valid according to its terms. Further, G.S. 44A-12(f) does not prohibit the subordination or release of a lien.

## **5. Sanctions for False Statements.**

Under the "old" law, a contractor or other person who knowingly furnished a false statement of the sums due or claimed to be due and received payment for improvements to real property was guilty of a Class 1 misdemeanor. Effective January 1, 2013, G.S. 44A-24 was amended to provide that any licensed contractor or subcontractor that knowingly submits a false statement will also be subject to administrative penalties and disciplinary action under Chapter 87 of the General Statutes. As a result, a contractor or subcontractor who knowingly furnishes a false statement may have its license revoked, suspended, or otherwise restricted. Moreover, an individual involved may also lose his or her ability to act as a "qualifying party" for a license.

## **6. Necessary and Property Parties to Lien Enforcement Lawsuits.**

In an effort to "cover all bases," a lien claimant who brings an action to enforce a claim of lien on real property typically joins anyone who may have an interest in the property as a party to the litigation – including, for example, the current owner of the property, the former owner who sold the property to the current owner, and any lender who has or claims a lien on the real property.

Effective July 12, 2012, certain owners, lenders, and title insurance companies are no longer necessary or proper parties to a lien enforcement action. Assuming there is no independent claim that is separate and distinct from the enforcement of the claim of lien, G.S. 44A-13 now provides that a former owner of the property at the time the lien arose (*i.e.*, when construction was first commenced) is not a necessary party in a lien enforcement action if the former owner did not hold any ownership interest in the property at the time the lawsuit to enforce the claim of lien is commenced and if the lien claimant seeks no direct relief from the former owner. Similarly, a subsequent purchaser and a subsequent purchaser's lender are not necessary or proper parties to a lawsuit to enforce a claim of lien on real property once the lien on the real property has been discharged pursuant to G.S. 44A-19 by the filing of an adequate cash deposit or a surety bond with the Clerk of Superior Court.

## **7. Addressing the "Double Payment" Problem in Public Projects.**

Article 3 of Chapter 44A, entitled "Model Payment and Performance Bond," deals with payment and performance bonds issued in connection with public construction projects. Effective January 1, 2013, Article 3 was amended to provide that contractors who enter into construction contracts with the State of North Carolina or any of its departments, agencies, or political subdivisions are now afforded some protection against the risk of having to make double payments. Reduced to basics, a contractor is required to furnish any potential lien claimant with a copy of the required payment bond within seven days after the claimant's written request. As amended, Article 3 also requires contractors to provide their subcontractors and suppliers with a "Project Statement." Similarly, at each level, each subcontractor must pass on a copy of the Project Statement to its subcontractors and suppliers. Upon receipt of a Project Statement, subcontractors and suppliers may serve a "Notice of Public Subcontract" on the contractor, thereby preserving their rights to payment under the payment bond. If a Notice of Public Subcontract is sent late or not at all, there is a substantial risk that the subcontractor will lose its ability to recovery from the project's payment bond some or all of the amounts it may ultimately be owed.

**AN OVERVIEW FROM A LENDER'S PERSPECTIVE  
AS TO  
HOW NORTH CAROLINA'S MECHANIC'S LIEN LAW WORKS  
BEGINNING JUNE 22, 2013<sup>1</sup>**

- I. Key Definitions. There are several terms defined in G.S. 44A-7 that are used throughout North Carolina's mechanic's lien law (and elsewhere in this outline). They are essential for a clear understanding of how the mechanic's lien law works.
- Improve – To build, effect, alter, repair, or demolish any improvement upon, connected with, or on or beneath the surface of any real property, or to excavate, clear, grade, fill or landscape any real property, or to construct driveways and private roadways, or to furnish materials, including trees and shrubbery, for any of such purposes, or to perform any labor upon such improvements, and shall also mean and include any design or other professional or skilled services furnished by architects, engineers, land surveyors and landscape architects registered under Chapter 83A, 89A, or 89C of the General Statutes, and rental of equipment directly utilized on the real property in making the improvement.
  - Improvement – All or any part of any building, structure, erection, alteration, demolition, excavation, clearing, grading, filling, or landscaping, including trees and shrubbery, driveways, and private roadways, on real property.
  - Real property – The real estate that is improved, including lands, leaseholds, tenements and hereditaments, and improvements placed thereon.
- II. The Cast of Characters. In connection with any real estate-secured loan transaction, the cast of characters may include some or all of the following:
- Lender.
  - Borrower (but not necessarily the owner of the real property in question).
  - Purchaser of the real property in question.

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<sup>1</sup> In the summer of 2012, the North Carolina General Assembly enacted Session Law 2012-175, Session Law 2012-158, and Section 65.3(a)-(c) of Session Law 2012-194, each of which amended North Carolina's mechanic's lien law. In 2013, the North Carolina General Assembly enacted Session Law 2013-16 in March and Session Law 2013-117 in June, each of which made technical corrections to the new lien agent process that went into effect on April 1, 2013. All of the statutory citations in this outline are to the North Carolina General Statutes as of June 22, 2013, after all of the changes to the mechanic's lien law adopted by the General Assembly in 2012 and the technical amendments adopted 2013 became effective.

- Owner. For mechanic's lien law purposes, the "owner" is defined in G.S. 44A-7 as "a person who has an interest in the real property improved and for whom an improvement is made and who ordered the improvement to be made." The term "owner" expressly includes (i) an owner's successors-in-interest, and (ii) the owner's agents when acting within the scope of their authority.<sup>2</sup>
- Contractor.<sup>3</sup> "Contractor" is defined in G.S. 44A-7 as "a person who contracts with an owner to improve real property."
- Subcontractor.<sup>4</sup> Because their lien rights differ, the mechanic's lien law identifies four different subcategories of subcontractor. They are:

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<sup>2</sup> A person who contracts to purchase the property to be improved and who subsequently purchases the property has a sufficient equitable interest in the property to be considered an "owner" when, before the purchaser actually consummates the purchase, the purchaser (rather than the then owner of the property) enters into a contract to improve the property. *Carolina Builders Corporation v. Howard-Veasey Homes, Inc.* 72 N.C. App. 224, 324 S.E.2d 626 (1985). Similarly, our courts have consistently held that when a lessee contracts with a contractor to improve the leasehold estate, the lessee is considered an "owner" for purposes of the mechanic's lien law, but only with respect to the leasehold estate. A claim of lien on the real property asserted by or through the contractor will be valid only to the extent of the lessee's leasehold interest in the property. *Pete Wall Plumbing Co., Inc. v. Sandra Anderson Builders, Inc.*, 721 S.E.2d 663 (N.C. Ct. App. 2011).

<sup>3</sup> **IMPORTANT NOTE REGARDING CONTRACTORS AND SUBCONTRACTORS:** The statutory definitions for contractor and for first, second, and third tier subcontractors are somewhat misleading because they go far beyond what we commonly consider to be a contractor or subcontractor. There are two reasons for this.

The first reason involves our common conception of "contractor." We commonly think of a contractor as a licensed general contractor – that is, one who has overall responsibility for a construction project and who subcontracts out work to subcontractors. However, under North Carolina's mechanic's lien law, **any person who contracts directly with the owner to improve real property is considered a contractor**, whether that person is a licensed general contractor or not. Any person who does not contract directly with the owner is, by definition, a "subcontractor." Accordingly, a lender's focus must necessarily be on the parties to the specific contract in question, and the lien rights are determined by where the lien claimant is in the following contractual "chain":

- Owner
- Contractor
- First tier subcontractor
- Second tier subcontractor
- Third tier subcontractor
- Subcontractor more remote than a third tier subcontractor.

The second reason relates to the statutory definition of "improve." In addition to those who perform work on the property (and who we commonly consider to be contractors and subcontractors), the terms "contractor" and "subcontractor" include (i) material suppliers who furnish materials for the improvements, including trees and shrubbery (for example, a building supply company or a nursery), (ii) equipment leasing companies that lease equipment directly utilized on the property in making the improvements, and (iii) licensed architects, engineers, land surveyors, and landscape architects who provide design or other professional or skilled services in connection with the improvements.

<sup>4</sup> "First tier subcontractor," "second tier subcontractor," and "third tier subcontractor" are all terms defined in G.S. 44A-7. The term "subcontractors more remote than third tier" is a descriptive term used in the mechanic's lien statutes, but it is not a defined term.

First tier subcontractor – a person who contracts with a contractor to improve real property.

Second tier subcontractor – a person who contracts with a first tier subcontractor to improve real property.

Third tier subcontractor – a person who contracts with a second tier subcontractor to improve real property.

Subcontractors more remote than a third tier subcontractors.

- Lien agent.<sup>5</sup> A "lien agent" is a title insurance company or title insurance agency designated by an owner pursuant to G.S. 44A-11.1 to serve as the owner's lien agent in connection with a construction project. The role and responsibility of the lien agent is critical in addressing the hidden lien problem.
- Obligor. "Obligor" is defined in G.S. 44A-7 as "an owner, contractor, or subcontractor in any tier who owes money to another as a result of the other's partial or total performance of a contract to improve real property." Identifying an obligor is important in the context of a subcontractor's lien upon funds, described in detail below.
- Potential lien claimant. The term "potential lien claimant" is a precisely defined term that applies only in the context of a transaction subject to the new lien agent law. A "potential lien claimant" is defined in G.S. 44A-7 as "any person entitled to claim a lien for improvements to real property under this Article [*i.e.*, the North Carolina mechanic's lien statute] who is subject to G.S. 44A-11.1 [*i.e.*, the new lien agent statute]." Depending on the circumstances, a potential lien claimant may be a contractor or a first, second, or third tier subcontractor.

III. Basic Lien Rights. As will be discussed in greater detail below, there are two different types of liens that can be asserted under North Carolina's mechanic's lien laws: a lien on real property and a lien upon funds. Lenders are usually more concerned with a claim of lien on real property than a claim of lien upon funds for the simple reason that a claim of lien on real property immediately puts at issue the lien priority of the lender's deed of trust – that is, does the perfected mechanic's lien on the real property have priority over the lien of the lender's deed of trust? Lenders should not, however, ignore the implications of a claim of lien upon funds, which in their own right can "freeze" the flow of funds and lead to a claim of lien on real property.

A. Contractor's Lien Right. The first type of mechanic's lien (and most important from a lender's perspective) is a contractor's claim of lien on real property.<sup>6</sup>

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<sup>5</sup> G.S. 44A-7(4b).

<sup>6</sup> G.S. 44A-8. As will be discussed in greater detail elsewhere in this outline, there are also two situations in which a subcontractor may assert a claim of lien on real property. In the most common situation, G.S. 44A-23 permits a

Provided it is properly perfected, a contractor's claim of lien on real property relates back in time and has priority from the time of the first furnishing of labor or materials at the site of the improvement by the lien claimant.<sup>7</sup> To assert the claim of lien on real property, a lien claimant must prepare and sign a statutory form entitled "Claim of Lien on Real Property."<sup>8</sup> To perfect its claim of lien on real property, the lien claimant must:

- Serve a copy of the Claim of Lien on Real Property on the record owner of the real property in question. If the claim of lien on real property is being asserted by a subcontractor by right of subrogation (discussed below), then the Claim of Lien on Real Property must also be served on the contractor through which subrogation is being asserted.<sup>9</sup>
- Within 120 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant, file the Claim of Lien on Real Property with the Clerk of Superior Court in each county where the real property in question is located.<sup>10</sup> If the Claim of Lien on Real Property is filed more than 120 days after the last furnishing of labor or materials, the lien is ineffective.

Once a Claim of Lien on Real Property has been filed, it cannot be amended. However, it can be cancelled and a new Claim of Lien on Real Property may be filed in substitution for the cancelled one, provided all this is accomplished within 120 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant.<sup>11</sup>

A properly and timely perfected Claim of Lien on Real Property will cease to be effective unless the lien claimant commences an action to enforce the claim of lien no later than 180 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant.<sup>12</sup>

These longstanding time limits (*i.e.*, a lien claimant has 120 days after the last furnishing of labor or materials to perfect a Claim of Lien on Real Property and 180 days after the last furnishing of labor or materials to commence an action to enforce the claim of lien) were not affected by the legislation adopted in 2012 or 2013, and remain unchanged.

- B. Subcontractors' Lien Rights. As described above, a contractor's lien right is relatively simple and straightforward – a contractor can assert on its own behalf a direct lien on the owner's real property by the timely filing and service of a claim of lien on real property. The rights of a subcontractor are more complex and, in a sense, derivative. Based on the

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subcontractor to assert the contractor's claim of lien on real property by right of "subrogation," a legal concept that permits a subcontractor who has not been paid to "stand in the shoes" of the contractor and assert the contractor's claim of lien on real property. In the other situation (which is much more limited and happens infrequently), a subcontractor has the right to file a direct claim of lien on real property in its own right pursuant to G.S. 44A-20(d) without relying on the doctrine of subrogation.

<sup>7</sup> G.S. 44A-10; G.S. 44A-14(a).

<sup>8</sup> The statutory form appears in G.S. 44A-12(c).

<sup>9</sup> G.S. 44A-11(a)(1) and G.S. 44A-23. G.S. 44A-11(b) and (c) govern the means by which service may be obtained.

<sup>10</sup> G.S. 44A-11(a)(2) and G.S. 44A-12.

<sup>11</sup> G.S. 44A-12(d).

<sup>12</sup> G.S. 44A-13(a); G.S. 44A-16(a)(3).

circumstances, a subcontractor may have (i) a right to assert the contractor's claim of lien on real property by right of subrogation, (ii) a lien upon funds owed by an obligor to a contractor or subcontractor "up the chain," and/or (iii) a right in very limited circumstances to assert a direct claim of lien on real property.

1. Subcontractor's Right to Assert a Claim of Lien on Real Property by Subrogation.

To the extent of their respective claims, first, second, and third tier subcontractors have the right to assert and enforce the direct claim of lien on real property held by the contractor in their "chain" "by right of subrogation."<sup>13</sup> However, it is important to remember that a subcontractor's right of subrogation is both limited and dependent – it cannot exceed the lesser of (i) amount owed to that subcontractor, or (ii) the amount the owner owes the contractor and for which the contractor could assert a direct claim of lien in its own right. Thus, for example, if an owner has fully paid the contractor under the terms of the contract between the owner and the contractor and no more money is or will become due to the contractor, then any attempt by a subcontractor who has not been paid to assert the contractor's claim of lien on real property by right of subrogation will be ineffective because there is no longer any "money on the table." The subcontractor's subrogation claim is only as strong as the contractor's claim.

The procedures, time constraints, and forms subcontractors must use to assert the contractor's lien rights are essentially the same as would apply to the contractor were the contractor to assert a claim of lien on real property in its own right.<sup>14</sup> However, there are a few additional provisions that apply only when a subcontractor seeks to assert by subrogation the contractor's right to claim a lien on real property:

- (a) When completing the statutory "Claim of Lien on Real Property" form,<sup>15</sup> a subcontractor may use as the date upon which labor or materials were first furnished on the real property either (i) any date on or after the date of the first furnishing of labor or materials on the real property by the subcontractor making the claim, or (ii) any date on or after the date of the first furnishing of labor or materials on the real property by the contractor through which the subcontractor's Claim of Lien on Real Property is being asserted. Similarly, a subcontractor may use as the date upon which labor or materials were last furnished on the real property either (i) any date on or before the date of the last furnishing of labor or materials on the real property by the subcontractor making the claim, or (ii) any date on or before the date of the last furnishing of labor or materials on the real property by the contractor through which the subcontractor's Claim of Lien on Real Property is being asserted<sup>16</sup>

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<sup>13</sup> G.S. 44A-23(a) and (b). Under the doctrine of subrogation, a first, second, or third tier subcontractor can "stand in the shoes" of the contractor to assert the contractor's claim of lien on real property.

<sup>14</sup> G.S. 44A-23(a) and (b)(4).

<sup>15</sup> The statutory form appears in G.S. 44A-12(c).

<sup>16</sup> G.S. 44A-23(d).

(b) A second or third tier subcontractor is prohibited from asserting through subrogation the contractor's right to assert a claim of lien on real property if either:<sup>17</sup>

(1) Within 30 days after a building permit is issued or within 30 days after the date of the contract between the owner and the contractor (whichever is later), the owner or contractor properly posts on the property and files with the Clerk of Superior Court of the county in which the real property is located a properly completed and signed "Notice of Contract," and the second or third tier subcontractor thereafter fails to serve a properly completed and signed "Notice of Subcontract" upon the contractor; or

(2) After a signed Notice of Contract has been properly posted and filed and the second or third tier subcontractor has served a Notice of Subcontract on the contractor, the contractor serves a "Written Notice of Payment" on the second or third tier subcontractor within five days after each payment is made by the contractor to the first tier contractor. The notice of payment should set forth the date of the payment to the first tier subcontractor and the period for which payment is made.

2. Subcontractor's Lien Upon Funds. Subcontractors have a lien upon funds to secure amounts they are owed under their contracts as a result of having furnished labor, materials, or rental equipment at the site of the improvement.<sup>18</sup> To the extent of the subcontractor's claim (including interest), a subcontractor has the following lien rights upon funds:<sup>19</sup>

<u>Subcontractor</u>	<u>Has a Direct Lien</u>	<u>And Is Subrogated</u>
First tier subcontractor	Upon funds that are owed to the contractor with whom the first tier subcontractor dealt.	No subrogation rights.
Second tier subcontractor	Upon funds that are owed to the first tier subcontractor with whom the second tier subcontractor dealt.	To the extent of the second tier contractor's direct lien claim, to the lien upon funds of the first tier subcontractor with whom the second tier subcontractor dealt. <sup>20</sup>

<sup>17</sup> G.S. 44A-23(b). The provisions that can bar a second or third tier subcontractor from asserting the contractor's claim of lien on real property by right of subrogation are not widely known and are rarely relied upon. However, as an additional defensive measure, a prudent lender is well advised to require the owner or contractor to post a copy of the statutory Notice of Contract beside the building permit on the property to be improved and to record the Notice of Contract in the office of the Clerk of Superior Court in each county where the property to be improved is located. The statutory forms for the Notice of Contract and the Notice of Subcontract appear in G.S. 44A-23(b)(2) and (3).

<sup>18</sup> G.S. 44A-18(e).

<sup>19</sup> G.S. 44A-18 (a)-(d).

<sup>20</sup> Under the doctrine of subrogation, a second tier subcontractor can "stand in the shoes" of the first tier subcontractor to assert the first tier subcontractor's lien upon funds owed to the contractor with whom the first tier subcontractor dealt.

<u>Subcontractor</u>	<u>Has a Direct Lien</u>	<u>And Is Subrogated</u>
Third tier subcontractor	Upon funds that are owed to the second tier subcontractor with whom the third tier subcontractor dealt.	To the extent of the third tier contractor's direct lien claim, (i) to the lien upon funds of the second tier subcontractor with whom the third tier subcontractor dealt, and (ii) to the extent the second tier contractor is subrogated thereto, to the lien upon funds of the first tier subcontractor with whom the second tier subcontractor dealt. <sup>21</sup>
Subcontractor more remote than the third tier subcontractor	Upon funds that are owed to the person with whom the subcontractor dealt.	No subrogation rights.

A subcontractor's lien upon funds "arises, attaches, and is effective immediately upon the first furnishing of labor, materials, or rental equipment at the site of the improvement by a subcontractor."<sup>22</sup> However, to perfect its lien, the subcontractor must give a "Notice of Claim of Lien upon Funds" in writing to the obligor against whom the lien is asserted.<sup>23</sup> The form of the Notice of Claim of Lien upon Funds and the method by which the notice must be served are prescribed by statute.<sup>24</sup> Until a subcontractor perfects its lien upon funds by giving the obligor a Notice of Claim of Lien upon Funds, "any owner, contractor, or subcontractor against whose interest the lien upon funds is claimed may make, receive, use, or collect payments thereon and may use such proceeds in the ordinary course of its business."<sup>25</sup>

3. Duties of the Obligor and the Subcontractor's Right in Limited Circumstances to Assert a Direct Claim of Lien on Real Property. What happens after an obligor receives a Notice of a Claim of Lien upon Funds from a subcontractor? The

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<sup>21</sup>Under the doctrine of subrogation, a third tier subcontractor can "stand in the shoes" of both the second tier subcontractor and the first tier subcontractor to assert their respective lien rights on funds owed by persons "up the chain."

<sup>22</sup> G.S. 44A-18(f). This subsection was substantially re-written effective January 1, 2013, to resolve uncertainty as to exactly when a lien upon funds arises and attaches. The statute now provides that a subcontractor's lien upon funds "arises, attaches, and is effective immediately upon the first furnishing of labor, materials, or rental equipment at the site of the improvement by a subcontractor." Note that the statute says "a subcontractor," not "the subcontractor asserting the claim of lien upon funds." This language may be interpreted to mean that the lien rights of all subcontractors relate back in time to the date labor, materials, or rental equipment were first furnished at the site of the improvement by any of the subcontractors.

<sup>23</sup> G.S. 44A-18(f).

<sup>24</sup> G.S. 44A-19.

<sup>25</sup> G.S. 44A-18(g).

simple answer is that, from a practical standpoint, the flow of funds on the project comes to a halt until the claim of lien upon funds is resolved.

The duties and liability of an obligor are set out in G.S. 44A-20. The analysis must begin with a determination of the amount of money that each obligor in the contractual chain owes to the contractor or subcontractor with whom the obligor dealt. Because the claim of lien is upon *funds owed by the obligor* (and not on *the real property* that has been improved by the subcontractor), the claim of lien upon funds is, as a practical matter, of no value if no sums are or will be owed by the obligor to the contractor or subcontractor with whom the obligor dealt. If, on the other hand, sums are or will be owed by the obligor to the contractor or subcontractor with whom the obligor dealt, then the obligor is under a duty to withhold and retain such sums as may be necessary to satisfy all of the claims of lien upon funds that the obligor has received.<sup>26</sup>

If, after having received a Notice of Claim of Lien upon Funds, an obligor fails to retain a sufficient amount of money to pay the lien and instead makes payment directly to the contractor or subcontractor with whom the obligor dealt (thereby depriving the lien claimant of the funds that would otherwise have been available to satisfy the claim of lien upon funds), the claimant's lien upon funds continues in effect upon the funds received by the contractor or subcontractor who received them, and, in addition, the obligor become personally liable to the lien claimant up to the amount of the wrongful payment, not exceeding the total claims with respect to which the Notice of Claim of Lien upon Funds was received prior to payment.<sup>27</sup> In short, if an obligor ignores a Notice of Claim of Lien upon Funds and pays the contractor or subcontractor with whom the obligor has dealt without "holding back" an amount sufficient to satisfy the claim of lien upon funds, the obligor is exposed to personal liability to the lien claimant and may end up having to pay twice.

In addition, if the obligor in question happens to be the owner of the property being improved, then the lien claimant may assert pursuant to G.S. 44A-20(d) a *direct* claim of lien on real property to the extent of the owner's personal liability.<sup>28</sup> However, a subcontractor may assert a direct claim of lien on real property in the subcontractor's own right only when (i) the subcontractor has properly and timely perfected its claim of lien upon funds, (ii) the obligor in question is the owner of the property being improved, (iii) the owner/obligor has incurred personal liability to the lien claimant because of wrongful payments made by the owner/obligor subsequent to receiving the lien claimant's Notice of Claim of Lien upon Funds, and (iv) the lien claimant properly and timely perfects its direct claim of lien on real property using the same procedures and subject to time constraints applicable to a contractor's claim of lien on real property. The subcontractor's direct Claim of Lien on Real Property must state the grounds the

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<sup>26</sup> G.S. 44A-20(a).

<sup>27</sup> G.S. 44A-20(b).

<sup>28</sup> G.S. 44A-20(d).

lien claimant believes give rise to personal liability on the part of the owner/obligor and include as an exhibit a copy of the Notice of Claim of Lien upon Funds given by the subcontractor, together with a "proof of service" affidavit.<sup>29</sup>

4. Pro Rata Recovery. What happens when the funds owed by obligors "up the chain" are insufficient to pay all of the subcontractors' claims of lien upon funds? The simple answer is that the subcontractors share all available funds on a pro rata basis.
  - (a) When the obligor in question is a contractor or subcontractor and the funds in the hands of the obligor and the obligor's personal liability, if any, under G.S. 44A-20(b) are less than the sum of all valid claims of lien upon funds received by the obligor, the lien claimants share the funds on a pro rata basis.<sup>30</sup>
  - (b) When the obligor in question is the owner and the funds in the hands of the owner/obligor and the owner/obligor's personal liability, if any, under G.S. 44A-20(b) are less than the sum of all valid claims of lien upon funds that have been received by the owner/obligor and all valid Claims of Lien on Real Property filed by the subcontractors by right of subrogation with the Clerk of Superior Court under G.S. 44A-23, the lien claimants entitled to liens upon funds and the lien claimants entitled to subrogation claims of lien on real property share the funds on a pro rata basis.<sup>31</sup>

#### IV. The New Lien Agent Process.

- A. Background. A driving force behind the 2012 legislative changes was the urgent desire to address the longstanding "hidden lien" problem. A properly perfected claim of lien on real property (whether asserted by a contractor or a subcontractor) relates back in time for priority purposes to the date on which labor or materials were first provided by the lien claimant to the jobsite. Because there has never been a formal public record of when this may have occurred, purchasers and lenders are unable to determine with certainty whether there is a possible lien, when that lien might have become effective, and whether it might take priority over the interests of the purchaser and/or lender.

In an effort to address the hidden lien problem, the General Assembly adopted Session Law 2012-158 in the summer of 2012. Session Law 2012-158 introduces a "lien agent" process in North Carolina that is patterned, at least in part, after a similar process introduced several years ago in Virginia for residential construction projects. The new lien agent law took effect on April 1, 2013.<sup>32</sup>

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<sup>29</sup> G.S. 44A-20(d).

<sup>30</sup> G.S. 44A-21(a).

<sup>31</sup> G.S. 44A-21(b).

<sup>32</sup> Session Law 2013-16 (effective April 1, 2013) and Session Law 2013-117 (effective June 22, 2013) made technical corrections to the lien agent process.

The lien agent concept is really quite simple – by requiring potential lien claimants to "identify" themselves early in the process (and well before the potential lien claimants must file their claims of lien on real property), a diligent purchaser, lender, closing attorney, settlement agent, title insurance company, or title insurance agency in a transaction involving the real property in question can address the legitimate interests of potential lien claimants as part of the closing process – all without cluttering the public record. The following is a brief summary of how the drafters and proponents of the lien agent legislation anticipate the process will work:

1. In any private project to improve real property that is subject to the new lien agent law, the owner of the construction site will designate a lien agent. The lien agent designated by the owner must be chosen from among the list of registered lien agents maintained by the North Carolina Department of Insurance. Only title insurance companies and title insurance agencies authorized to do business in North Carolina that have consented to serve as a lien agent and registered with the North Carolina Department of Insurance for that purpose may serve as a lien agent.
2. The identity of the lien agent and the lien agent's contact information will be readily available to all of the project's contractors and subcontractors.
3. A contractor or subcontractor who wishes to preserve its right to assert a claim of lien on the real property will be required to send a simple one-page form (a "Notice to Lien Agent") to the lien agent announcing that it is a potential lien claimant working on or providing materials to the construction site. The Notice to Lien Agent can be sent before, during, or after the potential lien claimant performs work or provides materials.
4. Receipt by the lien agent of a Notice to Lien Agent puts the lien agent on notice that the potential lien claimant may at some future time assert and pursue a claim of lien on the real property.
5. The lien agent then serves as an information "clearinghouse." An interested party (*i.e.*, an owner, purchaser, potential lien claimant, lender, closing attorney, settlement agent, title insurance company, or title insurance agency involved in a transaction involving the real property in question and their respective authorized agents) may at any time request the lien agent to provide (and the lien agent is required to provide to any interested party requesting it) a listing of all of the potential lien claimants who have filed a Notice to Lien Agent with the lien agent. This permits the requesting party to identify all potential lien claimants, thereby reducing the risk of hidden liens. Thus, for example, a settlement agent should request the lien agent to provide a list of the potential lien claimants immediately before a loan closing in order to address any potential claims against the real property and obtain appropriate lien waivers and subordinations as part of the loan closing process.<sup>33</sup>

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<sup>33</sup> G.S. 44A-11.1(f) is a curious provision adopted by the General Assembly at the behest of the Bar Association. It provides that an attorney serving as the "closing attorney" in a transaction involving real property subject to the new lien agent law who contacts the lien agent in writing within five business of the date the deed or deed of trust is

6. To simplify the mechanics of the lien agent process, most of the title insurance companies licensed to do business in North Carolina banded together to create and implement an online website – <http://liensnc.com> – that permits (i) an owner (or, in certain cases, the owner’s custom contractor) to designate a lien agent online, (ii) a potential lien claimant to file a Notice to Lien Agent with the designated lien agent online, and (iii) an interested party to request and receive up-to-date information from the designated lien agent concerning the identity of potential lien claimants online.

It is important to remember that the new lien agent law deals only with (i) the contractor's right to assert a direct claim of lien on real property, (ii) a subcontractor's right to assert the contractor’s claim of lien on real property by right of subrogation, and (iii) a subcontractor's right to assert a direct claim of lien on real property pursuant to G.S. 44A-20(d) when the owner/obligor becomes personally liable to a subcontractor because the owner/obligor made wrongful payments to the contractor without withholding sufficient funds to satisfy a claim of lien upon funds asserted by the subcontractor. The new lien agent law does not address a subcontractor's right to assert a claim of lien upon funds.<sup>34</sup>

- B. Effective Date of the New Lien Agent Law. The new lien agent law went into effect April 1, 2013. However, it applies only to those projects to improve real property for which the first furnishing of labor or materials at the site of the improvements occurred on or after April 1, 2013 – it does *not* apply to a project if the first furnishing of labor or materials at the site of the improvements for that project occurred before April 1, 2013.<sup>35</sup>
- C. Scope of Transactions Subject to the New Lien Agent Law. Beginning April 1, 2013, § 44A-11.1(a) of the North Carolina General Statutes requires an owner to designate a lien agent in any project to improve the owner's real property if the total cost of the undertaking will be \$30,000 or more either (i) at the time the original building permit is issued, or (ii) if no building permit is required, at the time the contract for the improvements is entered into with the owner. However, regardless of the anticipated costs of the improvements, the owner may, but is not required to, designate a lien agent for improvements to an existing single-family residential dwelling unit that is occupied by the owner as a residence, or for the addition of an accessory building or accessory structure (as defined in the North Carolina Uniform Residential Building Code), the use of which is incidental to that residence.<sup>36</sup>

Thus, the new lien agent law does not apply to a private project to improve real property if:

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recorded and requests copies of the Notices to Lien Agent received by the lien agent "shall be deemed to have fulfilled the attorney's professional obligation as closing attorney to check such notices to lien agent and shall have no further duty to request that the lien agent provide information pertaining to notices received subsequently by the lien agent." This 5-day standard is far too lax for a prudent lender. Through its loan closing instructions, a prudent lender should impose a more rigorous duty of inquiry on the closing attorney.

<sup>34</sup> G.S. 44A-11.2(p).

<sup>35</sup> Section 7 of Session Law 2012-158.

<sup>36</sup> G.S. 44A-11.1(a).

- The first furnishing of labor or materials at the site of the improvements occurred before April 1, 2013;
- The total cost of the undertaking is less than \$30,000; or
- Regardless of the total cost of the undertaking, the owner elects not to designate a lien agent for improvements to an existing single-family residential dwelling unit that is occupied by the owner as a residence, or for the addition of an accessory building or accessory structure (as defined in the North Carolina Uniform Residential Building Code), the use of which is incidental to that residence.

With respect to projects that are outside the scope of the new lien law, the "hidden lien" problem continues unabated.

D. Approved Methods for Delivering a Notice – G.S. 44A-11.2(g). The lien agent law permits or requires the delivery of a variety of different notices. In complying with the written notice requirements of the new lien agent law, G.S. 44A-11.2(g) provides that the notice must be addressed to the person required to be provided with the notice and, unless a different method of delivery is specifically required, delivered by any one of the following methods:

- Certified mail, return receipt requested;
- Signature confirmation as provided by the United States Postal Service;
- Physical delivery and obtaining a delivery receipt from the lien agent;
- Facsimile with a facsimile confirmation;
- Depositing with a designated delivery service authorized pursuant to 26 U.S.C. 7502(f)(2) (which includes, for example, FedEx);
- Electronic mail, with delivery receipt; or
- For certain limited purposes, utilizing an Internet Web site approved for such use by the designated lien agent, with delivery receipt. This method of delivery is expressly authorized for the transmission to the lien agent of (i) the owner's notice to the lien agent designating the lien agent as such, and (ii) a potential lien claimant's Notice to Lien Agent.

The term "delivery receipt" includes an electronic or facsimile confirmation. A return receipt or other receipt showing delivery of a notice to the addressee or written evidence that the notice was delivered by the USPS or other carrier to, but not accepted by the addressee, is prima facie evidence of receipt.

E. Owner's First Responsibility – Designating the Lien Agent. Under the new lien agent law, an owner is required to designate a lien agent "no later than the time the owner first

contracts with any person to improve the real property."<sup>37</sup> The lien agent must be a title insurance company or title insurance agency selected from among the list of registered lien agents maintained by the North Carolina Department of Insurance.<sup>38</sup> The owner is required to deliver to the lien agent written notice of the designation by any of the delivery methods authorized by G.S. 44A-11.2(g) (discussed above). The notice designating the lien agent must include the owner's contact information and the street address, tax map and block number, reference to a recorded instrument, or some other description that reasonably identifies the real property for the improvements for which the lien agent has been designated.<sup>39</sup>

An owner's designation of a lien agent does not make the lien agent an agent of the owner for purposes of receiving a Claim of Lien on Real Property, a Notice of Claim of Lien upon Funds, or for any other purpose other than the receipt of the Notice to Lien Agent required by G.S. 44A-11.2 (discussed below).<sup>40</sup>

The statute provides a simple process for the appointment of a new lien agent when a lien agent resigns, is no longer licensed to serve as a lien agent, revokes its consent to serve as lien agent, is removed by the owner, or otherwise becomes unable or unwilling to serve.<sup>41</sup>

F. Notice to Lien Agent. At the core of the new lien agent law is the "Notice to Lien Agent." A contractor or subcontractor that wishes to preserve its right to assert a claim of lien on real property is well-advised to deliver a simple, one-page statutory form (a "Notice to Lien Agent") to the lien agent announcing that it is a potential lien claimant working on or providing materials to the project site.<sup>42</sup>

1. The Notice to Lien Agent may be delivered to the lien agent before or after the potential lien claimant enters into a contract to perform work or provide materials, and before, during, or after the potential lien claimant actually performs work or delivers materials.<sup>43</sup> The Notice to Lien Agent can be delivered to the lien agent by any of the delivery methods authorized by G.S. 44A-11.2(g).<sup>44</sup>

2. A Notice to Lien Agent is not the same thing as, and does not satisfy the requirements for, a Notice of Claim of Lien upon Funds or a Claim of Lien on Real Property.

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<sup>37</sup> Remember that the definition of "improve" in G.S. 44A-7(3) expressly includes "any design or other professional or skilled services" provided by licensed architects, engineers, land surveyors, and landscape architects (each identified as a "design professional" in new G.S. 44A-11.2(i)). Because a building permit should not be issued unless and until a lien agent has been designated, it is likely that an owner will have designated a lien agent by the time the application for a building permit is submitted. It is less likely that an owner will designate a lien agent at the time the owner engages the services of, for example, an architect or a surveyor. To what extent does the lien agent law apply if the owner fails to designate a lien agent at or prior to "the time the owner first contracts with any person to improve the real property"? The statute is silent as to this. This is a very significant issue.

<sup>38</sup> G.S. 44A-11.1(b). The Department of Insurance is required by G.S. 58-26-45(e) to maintain a current list of registered lien agents on its Web site.

<sup>39</sup> G.S. 44A-11.1(a).

<sup>40</sup> G.S. 44A-11.1(a).

<sup>41</sup> G.S. 44A-11.1(d).

<sup>42</sup> The statutory form appears in G.S. 44A-11.2(j).

<sup>43</sup> G.S. 44A-11.2(q).

<sup>44</sup> G.S. 44A-11.2(g).

Similarly, the delivery to the lien agent of a Notice to Lien Agent does not satisfy the service or filing requirements applicable to the Notice of Claim of Lien upon Funds or a Claim of Lien on Real Property.<sup>45</sup> A Notice to Lien Agent merely adds the contractor or subcontractor submitting the notice to the list of potential lien claimants that have reserved their right to pursue a claim of lien on the real property, and declares that the potential lien claimant may at some future time assert and pursue a claim of lien on the real property identified in the notice.

G. Responsibilities of the Lien Agent. A lien agent adds transparency to the process by serving as a "clearinghouse" to (i) receive Notices to Lien Agent from potential lien claimants, and (ii) identify to any interested party<sup>46</sup> all of the potential lien claimants who have then delivered a Notice to Lien Agent to the lien agent. The responsibilities of a lien agent are set out in G.S. 58-26-45, a new section added to Article 26 of Chapter 58 of the North Carolina General Statutes, the Article regulating real estate title insurance companies.

Having been designated by an owner as the owner's lien agent, the lien agent's principal responsibilities are to receive Notices to Lien Agent delivered to the lien agent by potential lien claimants and to maintain an accurate record of the date and time of delivery and the information contained in those notices. In addition, the lien agent has several duties listed in G.S. 45-26-45(b) that are subject to specific time constraints:

<b><u>Time</u></b> <b>(if applicable )</b>	<b><u>Duty</u></b>	<b><u>Delivery Requirements</u></b> <b>(if applicable)</b>
Within three business days after receiving the owner's written notice of designation of lien agent.	Provide written notice acknowledging its designation as lien agent to the owner.	By the same method of delivery used by the owner in delivering the notice of designation to the lien agent.
Within three business days after receiving a Notice to Lien Agent from a potential lien claimant relating to improvements to real property for which the lien agent has been designated as the lien agent.	Provide written notice to the potential lien claimant confirming the lien agent's receipt of the potential lien claimant's Notice to Lien Agent.	By the same method used by the potential lien claimant in delivering the Notice to Lien Agent to the lien agent. If the notice is received by email, the acknowledgement sent by the lien agent must include the email the lien agent received, including the header showing the date and time of receipt.

<sup>45</sup> G.S. 44A-11.2(k).

<sup>46</sup> The persons authorized to request and receive a listing of the potential lien claimants from the lien agent are identified in G.S. 58-26-45(b)(7). They include (i) the property owner, (ii) a person who has contracted to purchase the property, (iii) potential lien claimants, (iv) a lender, closing attorney, or settlement agent involved in a transaction involving the property, (v) a title insurance company or title insurance agency issuing a title insurance policy on the property, and (vi) their respective authorized agents.

<b><u>Time</u> (if applicable )</b>	<b><u>Duty</u></b>	<b><u>Delivery Requirements</u> (if applicable)</b>
<p>Within three business days after receiving a Notice to Lien Agent from a potential lien claimant relating to improved real property for which the lien agent has <i>not</i> been designated as a lien agent.</p>	<p>Provide written notice to the potential lien claimant that the lien agent is <i>not</i> the designated lien agent for the improved property.</p>	<p>By the same method used by the potential lien claimant in delivering the Notice to Lien Agent to the lien agent.</p>
<p>Within one business day after receiving a request for information regarding potential lien claimants from any of the following persons or their authorized agents:</p> <ul style="list-style-type: none"> <li>• An owner of the improved property;</li> <li>• A title insurance company or title insurance agency issuing a policy of title insurance on the improved property;</li> <li>• A contracted purchaser of the improved property;</li> <li>• A potential lien claimant;</li> <li>• A closing attorney, lender, or settlement agent involved in a transaction involving the improved property.</li> </ul>	<p>Provide written notice of all of the potential lien claimants who have theretofore delivered a Notice to Lien Agent form to the lien agent pursuant to G.S. 44A-11.2, including information relating to any custom contractor identified by pursuant to G.S. 44A-11.2(h) and any design professional identified by the owner pursuant to G.S. 44A-11.2(i).</p> <p>In responding to any such request, the lien agent must include (i) the potential lien claimant's name, mailing address, telephone number, fax number (if available), and electronic mailing address (if available), (ii) the name of the party with whom the potential lien claimant contracted to improve the real property; and (iii) if specifically requested, a copy of each Notice to Lien Agent received by the lien agent.</p>	<p>No specific method of delivery is specified in the statute. Presumably, any method of delivery authorized by G.S. 44A-11.2(g) will be sufficient.</p>
<p>When the lien agent is removed by the owner or the lien agent resigns or otherwise becomes unable or unwilling to serve as such.</p>	<p>Transfer all notices received and other related documentation to any successor lien agent designated by the owner.</p>	

H. Lien Agent's Fees. Pursuant to G.S. 58-26-45(d), a registered lien agent "shall" collect from an owner the following fees for serving as the owner's designated lien agent:

- For improvements to real property comprising of one- or two-family dwellings, a fee of \$25.

- For services rendered pursuant to each designation as a lien agent for all other improvements to real property, a fee of \$50.

The lien agent is not authorized to charge or collect fees from potential lien claimants or those inquiring as to potential lien claimants.

- I. Actions that Must be Taken to Ensure that the Identity of the Lien Agent is Widely Known. As noted above, the owner is required to designate a lien agent "no later than the time the owner first contracts with any person to improve the real property."<sup>47</sup> Once the lien agent has been designated, the lien agent's contact information<sup>48</sup> must be widely disseminated and readily available to potential lien claimants.
  1. Building Permit/Posted Notice. A building permit issued with respect to a project subject to the new lien agent law must be conspicuously and continuously posted on the property for which the permit is issued until the completion of all construction.<sup>49</sup> The permit *should* include the lien agent's contact information.<sup>50</sup> If it does not, then a sign disclosing the lien agent's contact information must be conspicuously and continuously posted on the property until the completion of all construction.<sup>51</sup>
  2. Owner's Responsibility. Within seven days after receiving a request from a potential lien claimant by any of the approved delivery methods described in G.S. 44A-11.2(g) (discussed above), the owner is required by G.S. 44A-11.2(b) to provide a notice to the potential lien claimant containing the lien agent's contact information. The delivery method used by the owner must be the same delivery method used by the potential lien claimant in making the request.
  3. Responsibilities of Contractors and Subcontractors. Within three business days after contracting with a lower-tier subcontractor that is *not* required to furnish labor, materials, rental equipment, or professional design or surveying services at the site of the improvements, a contractor or subcontractor is required to provide the lower-tier subcontractor with a written notice containing the lien agent's contact information. It may be given (i) by any of the approved delivery methods described in G.S. 44A-11.2(g) (discussed above), or (ii) by including the lien agent's contact information in the written subcontract entered into by, or a written purchase order issued to, the lower-tier subcontractor entitled to the notice. Any contractor or subcontractor who previously received notice of the lien agent's contact information (regardless of how that information was received), and who thereafter fails to provide the lien agent's contact information to the lower-tier subcontractor within three business days, is

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<sup>47</sup> G.S. 44A-11.1(a).

<sup>48</sup> For purposes of the new lien agent law, the lien agent's "contact information" includes the lien agent's name, physical and mailing address, telephone number, facsimile number, and electronic mail address. G.S. 44A-11.2(a).

<sup>49</sup> G.S. 44A-11.2(e).

<sup>50</sup> G.S. 87-14(a)(3), G.S. 160A-417(d) and G.S. 153A-357(e).

<sup>51</sup> G.S. 44A-11.2(f). The requirement for posting a sign will also apply when, for example, the new lien agent law applies but the construction project does not require the issuance of a building permit.

liable to the lower-tier subcontractor for any actual damages incurred by the lower-tier subcontractor as a result of the failure to give notice.<sup>52</sup>

4. Exception. According to G.S. 44A-11.2(c), a potential lien claimant who requests the lien agent's contact information from the owner has no obligation to deliver a Notice to Lien Agent to the lien agent until the potential lien claimant receives the lien agent's contact information from the owner if (i) the potential lien claimant did not receive the lien agent contact information from a contractor or subcontractor (as described above), and (ii) the potential lien claimant either (a) has not then furnished labor, materials, rental equipment, or professional design or surveying services at the site of the improvements, or (b) last furnished labor, materials, rental equipment, or professional design or surveying services at the site of the improvements before the building permit or notice containing the lien agent's contact information was posted at the site of the improvements.

- J. Why It Is Important for a Potential Lien Claimant to Deliver a Notice to Lien Agent: Conditions Precedent to Perfecting a Claim of Lien on Real Property; Automatic Subordination of a Claim of Lien on Real Property; Exceptions to the General Rule. At the outset, it is important to remember that the conditions precedent and automatic subordination "rules" described below clearly apply:

- If the project is within the scope of, and subject to, the lien agent law;
- To a contractor's claim of lien on real property, whether asserted directly by the contractor or by a subcontractor by right of subrogation; and
- To a subcontractor's direct claim of lien on real property pursuant to G.S. 44A-20(d) when an owner/obligor improperly "pays over" the subcontractor's validly perfected claim of lien upon funds.

This discussion does not apply to, and does not limit, a subcontractor's claim of lien upon funds.

1. Conditions Precedent to Perfecting a Claim of Lien on Real Property.<sup>53</sup> Subject to the exceptions noted in 3 below, G.S. 44A-11.2(m) provides that a potential lien claimant (whether a contractor or subcontractor) may perfect a claim of lien on real property only if at least one of the following conditions is met:

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<sup>52</sup> G.S. 44A-11.2(d).

<sup>53</sup> The conditions precedent listed in G.S. 44A-11.2(m) are primarily intended to protect (i) the person who purchases property from an owner who had work performed on the property before the sale, and (ii) the purchaser's lender. Unless one of the conditions precedent is satisfied, a contractor or subcontractor who performed work or delivered materials at the jobsite will be barred from asserting a claim of lien on the real property, and the purchaser (and the lender who finances the purchase) will have "clear title."

- (a) The lien agent received a Notice to Lien Agent from the potential lien claimant no later than 15 days after the potential lien claimant first furnished labor or materials.<sup>54</sup>
  - (b) The lien agent received a Notice to Lien Agent from the potential lien claimant before the date an instrument is recorded that conveys an interest in the real property to a bona fide purchaser for value who is not an affiliate, relative, or insider<sup>55</sup> of the owner and whose priority is protected by the State's recording statute, G.S. 47-18.
  - (c) The potential lien claimant perfected its Claim of Lien on Real Property pursuant to G.S. 44A-11<sup>56</sup> before an instrument is recorded that conveys an interest in the real property to a bona fide purchaser for value who is not an affiliate, relative, or insider of the owner and whose priority is protected by the State's recording statute, G.S. 47-18.
2. Automatic Subordination of a Claim of Lien on Real Property.<sup>57</sup> In addition, G.S. 44A-11.2(n) provides specific lien priority protection for lenders under certain circumstances. Subject to the exceptions noted in 3 below, when a lien claimant's Claim of Lien on Real Property is not perfected pursuant to G.S. 44A-11<sup>58</sup> before a

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<sup>54</sup> To protect its right to assert a claim of lien on real property, a prudent contractor or subcontractor will routinely deliver a Notice to Lien Agent to the lien agent no later than 15 days after the contractor or subcontractor first furnishes labor or materials to the job site. This practice will likely become the norm. If so, then the conditions precedent and automatic subordination provisions contained in G.S. 44A-11.2(m) and (n) will have little practical effect. Permitting a contractor or subcontractor to satisfy the conditions precedent specified in G.S. 44A-11.2(m) and avoid the automatic subordination provisions contained in G.S. 44A-11.2(n) by delivering a Notice to Lien Agent within 15 days after the contractor or subcontractor first furnishes labor or materials to the job site perpetuates the hidden lien problem, albeit for a shorter period of time. For example, assume the contractor first furnishes labor at the construction site on July 1. The sale of the property occurs on July 10, and the deed to the purchaser and the lender's deed of trust are recorded on July 10. The contractor then delivers its Notice to Lien Agent to the lien agent on July 15. Between July 1 and July 15, the contractor has a hidden inchoate lien on the property that cannot be determined by requesting an updated list of potential lien claimants from the lien agent prior to closing, and a subsequent Claim of Lien on Real Property perfected by the contractor will have priority over the rights of the purchaser and the lien of the lender's deed of trust.

<sup>55</sup> According to G.S. 44A-11.2(m)(2) the terms "affiliate," "relative," and "insider" have the meanings ascribed to them by G.S. 39-23.1. Presumably, these terms as used in G.S. 44A-11.2(n) have the same meaning.

<sup>56</sup> To perfect its claim of lien on real property pursuant to G.S. 44A-11, the lien claimant must (i) file the Claim of Lien on Real Property with the Clerk of Superior Court in each county where the real property in question is located within 120 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant, and (ii) serve a copy of the Claim of Lien on Real Property on the record owner of the real property in question. If the claim of lien on real property is being asserted by a subcontractor by right of subrogation, then the Claim of Lien on Real Property must also be served on the contractor through which subrogation is being asserted.

<sup>57</sup> The automatic subordination rules set forth in G.S. 44A-11.2(n) are primarily intended to protect the lien priority of a lender's deed of trust in a loan transaction that does not involve a sale of the property. Because no "innocent purchaser" will be prejudiced by a claim of lien on the real property, the General Assembly considered it sufficient to subordinate the contractor's or subcontractor's claim of lien to the lien of the lender's deed of trust.

<sup>58</sup> To perfect its claim of lien on real property pursuant to G.S. 44A-11, the lien claimant must (i) file the Claim of Lien on Real Property with the Clerk of Superior Court in each county where the real property in question is located within 120 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant, and (ii) serve a copy of the Claim of Lien on Real Property on the record owner of the real property in question. If the

mortgage or deed of trust on the property for the benefit of one who is not an affiliate, relative, or insider of the owner has been recorded, the claimant's lien is automatically subordinate to the lien of the previously recorded mortgage or deed of trust unless either of the following conditions are met:

- (a) The lien agent received a Notice to Lien Agent from the potential lien claimant no later than 15 days after the potential lien claimant first furnished labor or materials.
  - (b) The lien agent received a Notice to Lien Agent from the potential lien claimant before the date the mortgage or deed of trust was recorded.
3. Exceptions. The conditions precedent to the filing of a Claim of Lien on Real Property and the automatic subordination of certain claims of lien discussed in 1 and 2 above are subject to four exceptions.
- (a) The first exception applies only if the contractor is a “custom contractor” and certain conditions are satisfied.<sup>59</sup>

A "custom contractor" is a duly licensed general contractor who has contracted with an owner who is not an affiliate, relative, or insider of the contractor to build a single-family residence on the owner's property to be occupied by the owner as a residence.

A custom contractor is “deemed” to have met the requirement of notice under G.S. 44A-11.2(m) and (n) on the date of the lien agent's receipt of notice of its designation as lien agent delivered to it by the custom contractor if, at the time of the lien agent's receipt of the notice, all of the following conditions are met:

- (1) The owner has not previously designated a lien agent for the improvements to which the notice of designation of lien agent relates.
- (2) The custom contractor is authorized to designate the lien agent on behalf of the owner under the written contract between the owner and custom contractor.
- (3) In addition to the information normally required to be included in the notice from the owner to the lien agent designating the lien agent as such, the notice of designation of lien agent contains the following additional information:
  - The custom contractor's name, mailing address, telephone number, fax number (if available), and electronic mailing address (if available).

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claim of lien on real property is being asserted by a subcontractor by right of subrogation, then the Claim of Lien on Real Property must also be served on the contractor through which subrogation is being asserted.

<sup>59</sup> G.S. 44A-11.2(h).

- The name of the owner with whom the custom contractor has contracted to improve the real property identified in the notice.

The effect of this exception is simple: In appointing the lien agent on behalf of the owner, the custom contractor may also provide the lien agent all of the information about the contractor that the contractor would otherwise have included in a separate Notice to Lien Agent. If the custom contractor does so, then there is no need for the custom contractor to file a separate Notice to Lien Agent – it would be redundant. Having already provided to the lien agent all of the information that would otherwise have been included in a separate Notice to Lien Agent, the custom contractor can file a Claim of Lien on Real Property without first delivering to the lien agent a separate Notice to Lien Agent and without fear that the claim of lien, if timely filed, will be subordinate to the lien of an intervening deed of trust.

After receiving a notice of its designation from a custom contractor, the designated lien agent is required to include the custom contractor's name and contact information in the lien agent's response to any person requesting a list of the potential lien claimants who have delivered a Notice to Lien Agent to the lien agent.

- (b) The second exception applies only when a lien agent is *not* identified in a contract for improvements to real property entered into between the owner and a "design professional" – that is, an architect, engineer, land surveyor, or landscape architect registered as such under North Carolina law.<sup>60</sup>

The design professional is "deemed" to have met the requirements of notice under G.S. 44A-11.2(m) and (n) on the date the lien agent receives the owner's notice of lien agent designation. As a result, the design professional can ignore the new lien agent provisions with impunity. The design professional can file a Claim of Lien on Real Property without first delivering to the lien agent a Notice to Lien Agent and without fear that the claim of lien, if timely filed, will be subordinate to the lien of an intervening deed of trust.

When a lien agent is *not* identified in the contract between the owner and the design professional (which will frequently be the case), then the owner (not the design professional) is required to deliver to the lien agent by any of the approved methods authorized in G.S. 44A-11.2(g) a written notice containing the following information pertaining to the design professional:

- The design professional's name, mailing address, telephone number, fax number (if available), and electronic mailing address (if available).

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<sup>60</sup> G.S. 44A-11.2(i)

- The name of the party with whom the design professional contracted to improve the real property (*i.e.*, the owner).
- A description of the real property sufficient to identify the real property, such as the name of the project, if applicable, or the physical address shown on the building permit.

Following the receipt of such information, the lien agent is required to include the design professional in the lien agent's response to any person requesting a list of the potential lien claimants who have delivered a Notice to Lien Agent to the lien agent.

- (c) The third exception is broader in its scope. A potential lien claimant is not required to deliver to the lien agent a "Notice to Lien Agent" and is not subject to the conditions precedent or to the automatic subordination provisions outlined above if (i) the lien agent contact information is not contained in the building permit (or an attachment thereto) or in a sign posted on the improved property at the time when the potential lien claimant was furnishing labor, materials, rental equipment, or professional design or surveying services at the site of improvements, and (ii) the owner failed to provide the lien agent's contact information to the potential lien claimant in a timely manner in response to a written request from the potential lien claimant to provide that information.<sup>61</sup>
- (d) The fourth exception is simple: The lien rights of a potential lien claimant who is given erroneous information by the owner regarding the identity of the lien agent are not be extinguished under G.S 44A-11.2(m) or subordinated under G.S 44A-11.2(n).<sup>62</sup>

## V. The Effect of Lien Waivers.<sup>63</sup>

- A. The G.S. 44A-12(f) Rule. The basic and longstanding rule regarding lien waivers contained in G.S. 44A-12(f) was not changed by recent legislation. Simply stated, an agreement by a contractor or subcontractor to waive the right to file a Claim of Lien on Real Property or the right to serve a Notice of Claim of Lien upon Funds is against public policy and is unenforceable if the agreement is entered into in anticipation of and in consideration for the awarding of any contract, either expressed or implied, for the

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<sup>61</sup> G.S. 44A-11.2(o).

<sup>62</sup> G.S. 44A-11.2(o).

<sup>63</sup> Unfortunately, the mechanic's lien law does not address the effect of a lien subordination agreement (as opposed to a lien waiver). Whether a lien waiver signed by a contractor affects the rights of a subcontractor may depend on whether the subcontractor has perfected its Claim of Lien on Real Property pursuant to G.S. 44A-11 at the time the contractor signs the lien waiver. To perfect its Claim of Lien on Real Property pursuant to G.S. 44A-11, a lien claimant must (i) file the Claim of Lien on Real Property with the Clerk of Superior Court in each county where the real property in question is located within 120 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant, and (ii) serve a copy of the Claim of Lien on Real Property on the record owner of the real property in question. If the Claim of Lien on Real Property is being asserted by a subcontractor by right of subrogation, then the Claim of Lien on Real Property must also be served on the contractor through which subrogation is being asserted.

making of an improvement on real property. However, a subsequent waiver supported by adequate consideration is valid according to its terms. Further, G.S. 44A-12(f) does not prohibit the subordination or release of a lien.

- B. The G.S. 44A-23(a1) and G.S. 44A-23(b)(5) Rule. According to G.S. 44A-23(a1) and G.S. 44A-23(b)(5), no action by a contractor will be effective to prejudice the rights of a subcontractor without the subcontractor's written consent once the subcontractor has perfected its Claim of Lien on Real Property in accordance with G.S. 44A-11. Otherwise (presumably), action on the part of the contractor will prejudice the rights of a subcontractor.
- C. The G.S. 44A-20(d) and G.S. 44A-23(c) Rule. According to G.S. 44A-20(d) and G.S. 44A-23(c), a lien waiver signed by a contractor before a subcontractor perfects its Claim of Lien on Real Property pursuant to G.S. 44A-11 is sufficient to waive the subcontractor's right to assert the contractor's claim of lien on real property by right of subrogation, but the contractor's lien waiver does *not* affect the subcontractor's right to a claim of lien upon funds or the subcontractor's right to assert a direct claim of lien on real property under the authority of G.S. 44A-20(d) when an owner/obligor improperly "pays over" the subcontractor's validly perfected claim of lien upon funds.

#### VI. Discharging a Claim of Lien on Real Property; Parties to a Lawsuit to Enforce a Claim of Lien on Real Property.

- A. Discharging a Claim of Lien on Real Property.<sup>64</sup> G.S. 44A-16 lists the six ways a Claim of Lien on Real Property can be discharged from public record, thereby freeing the real property from the claim of lien:
  1. The lien claimant or the lien claimant's agent or attorney can acknowledge to the Clerk of Superior Court the satisfaction of the indebtedness that gave rise to the Claim of Lien on Real Property. The Clerk of Court is required to enter an acknowledgment of satisfaction on the record of the Claim of Lien on Real Property. The acknowledgment of satisfaction must then be signed by the lien claimant or the lien claimant's agent or attorney, and witnessed by the Clerk of Superior Court.
  2. The owner can exhibit an instrument of satisfaction signed and acknowledged by the lien claimant. The instrument must state that indebtedness that gave rise to the Claim of Lien on Real Property has been paid or satisfied. The Clerk of Superior Court will then cancel the Claim of Lien on Real Property by entry of satisfaction on the record of the Claim of Lien on Real Property.
  3. By the lien claimant's failure to enforce the Claim of Lien on Real Property by commencing an action to enforce the claim of lien within 180 days after the last furnishing of labor or materials at the site of the improvement by the lien claimant.

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<sup>64</sup> G.S. 44A-20(e) and (f) and G.S. 20-19(e)(2) suggest that at least some of the methods described in G.S. 44A-16 may be sufficient to discharge a claim of lien upon funds.

4. By filing in the office of the Clerk of Superior Court the original or certified copy of a judgment or decree of a court of competent jurisdiction showing that the action by the claimant to enforce the Claim of Lien on Real Property has been dismissed or finally determined adversely to the claimant.
  5. By depositing with the Clerk of Superior Court a sum equal to the amount claimed in a Claim of Lien on Real Property, to be applied to the payment finally determined to be due in satisfaction of Claim of Lien on Real Property. The Clerk of Superior Court is then required to cancel of record the Claim of Lien on Real Property.
  6. By depositing with the Clerk of Superior Court a corporate surety bond in a sum equal to 1.25 times the amount claimed in a Claim of Lien on Real Property and conditioned upon the payment of the amount finally determined to be due in satisfaction of Claim of Lien on Real Property. The Clerk of Superior Court is then required to cancel of record the Claim of Lien on Real Property.
- B. Proper Parties to a Lawsuit to Enforce a Claim of Lien on Real Property. In an effort to "cover all bases," a lien claimant who brings an action to enforce a Claim of Lien on Real Property typically joins anyone who may have an interest in the property as a party to the litigation – including, for example, the current owner of the property, the former owner who sold the property to the current owner, and any lender who has or claims a lien on the real property.

Effective July 12, 2012 (the date Session Law 2012-175 was signed into law by Governor Perdue), certain owners, lenders, and title insurance companies are no longer necessary or proper parties to a lien enforcement action. Assuming there is no independent claim that is separate and distinct from the enforcement of the Claim of Lien on Real Property, G.S. 44A-13 now provides that a former owner of the property at the time the lien arose (*i.e.*, when construction was first commenced) is not a necessary party in a lien enforcement action if the former owner did not hold any ownership interest in the property at the time the lawsuit to enforce the claim of lien is commenced and if the lien claimant seeks no direct relief from the former owner. Similarly, a subsequent purchaser and a subsequent purchaser's lender are not necessary or proper parties to a lawsuit to enforce a claim of lien on real property once the lien on the real property has been discharged pursuant to G.S. 44A-19(a)(5) or (6) by the filing of a cash deposit or a surety bond with the Clerk of Superior Court.<sup>65</sup>

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<sup>65</sup> G.S. 44A-13(e) through (h) are important new provisions that will permit lenders to avoid the costs associated with mechanic's lien litigation once the mechanic's lien is discharged by the filing of a cash deposit or a surety bond with the Clerk of Superior Court. A prudent lender will consider including in the borrower's loan agreement a provision requiring the borrower to file a cash deposit or a surety bond with the Clerk of Superior Court sufficient to discharge the claim of lien on real property (i) when a Claim of Lien on Real Property is filed with the Clerk of Superior Court or, at a minimum, (ii) when an action is commenced by a lien claimant to enforce a Claim of Lien on Real Property.