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Lien--Necessity of Filing Statement of Labor and Materials Furnished or to Be Furnished Before Deed is Recorded by Purchaser

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deposited acceptance rule. Weighing the arguments with reference not to specific cases but to a rule of general application and recognizing the general and traditional acceptance of the rule as well as the modern changes in effective long-distance communication, it would seem that the balance tips whether heavily or near imperceptively, to continued adherence to the 'Rule in Adams v. Lindsell'."[14]

James L. Avritt

LIEN—NECESSITY OF FILING STATEMENT OF LABOR AND MATERIALS FURNISHED OR TO BE FURNISHED BEFORE DEED IS RECORDED BY PURCHASER.—The defendants and a building contractor signed a contract of sale on May 7, 1957, for the construction of a house on land then owned by the builder. Conveyance of title was to take place upon completion of construction, with defendants paying the balance of the purchase price at that time. The house was completed early in July and on July 8, 1957, the transaction was closed with conveyance by the builder and with complete payment by defendants. During the first week of October defendants contacted plaintiff, a plumbing contractor, and he proceeded to correct a substantial defect in the plumbing work he had done under contract with the builder. Plaintiff had not been paid by the builder for his original work. On December 11, 1957, plaintiff notified defendants of his intention to hold their property liable for his claim as required by Ky. Rev. Stat. 376.010(3) [Hereinafter referred to as KRS] and filed a statement of his lien claim in the county clerk's office as required by KRS 376.010(2). This was the first actual notice to defendants that plaintiff had not been paid.

In this action to enforce the lien the chancellor held that defendants, as equitable titleholders, had been "owners" of the property within the meaning of KRS 376.010(1) since May 7, 1957, and were not intervening bona fide purchasers for value and without notice. Therefore, he ruled that defendants were not entitled to protection under KRS 376.010(2); that the work done in October was the last work done under the plumbing contract; and that the notice given to defendants on December 11, 1957, complied with KRS 376.010(3). Accordingly, the chancellor sustained the lien. *Held:* Reversed. The Kentucky Court of Appeals held that when the balance of the purchase price was paid and the deed recorded on July 8, 1957, defendants became bona fide purchasers for value and without notice

[14] Morrison v. Thoelke, 155 So. 2d 889, 904 (1963).

entitled to priority over the lien since plaintiff had not filed the statement in the county clerk's office as required by KRS 376.010(2) showing that he had furnished or expected to furnish labor and materials before defendants recorded their deed. *Walker v. Valley Plumbing, Inc.*, 370 S.W.2d 136 (Ky. 1963).

This case raises the question of how the doctrine of equitable conversion should be applied in relation to Kentucky's mechanic and materialman lien laws. It turns primarily on the interpretation one gives the word "owner" in KRS 376.010(1). The chancellor held that "owner" meant legal or equitable owner; the Court of Appeals held that it meant only legal owner.

The chancellor's decision is not without merit. The whole vendor-purchaser relationship is based upon the doctrine of equitable conversion. The equity court regards the purchaser of realty, under a contract of sale, as the equitable owner even though legal title has not been transferred to him. The vendor is merely holding the title in trust for the purchaser's benefit and as a means of security for the payment of the balance of the purchase price.[1]

In instances where buildings are destroyed by fire before title has passed, this fiction of the law in the majority of jurisdictions places the burden or risk of loss on the purchaser on the theory that the purchaser is the equitable owner and should, therefore, bear the loss. A minority of jurisdictions, however, place the loss on the vendor because of a failure of consideration on the vendor's part allowing the purchaser to rescind the contract of sale and recover any down payment he has made. A third view prevails in states which have adopted the UNIFORM VENDOR AND PURCHASER RISK ACT. This statutory rule places the loss on the possessor of the property on the theory that the party in possession has a duty to guard against the loss with insurance.[2] Kentucky, with only slight deviation,[3] has firmly followed the majority viewpoint.[4]

Another application of this doctrine is seen in cases where one of the parties to the contract of sale dies before title has passed. Specific performance of the contract can be demanded by either party's heirs.[5]

If we interpret KRS 376.010(1) in the light of KRS 376.060, which provides for the personal liability of an "owner" who sells his property

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[1] De Funiak, Modern Equity § 87, at 207 (2d ed. 1956).
[2] *Id.* § 93, at 218.
[3] Johnston v. Jones, 51 Ky. 326 (1851).
[4] Godfrey v. Alcorn, 215 Ky. 465, 284 S.W. 1094 (1926); Cottingham v. Fireman's Fund Ins. Co., 90 Ky. 439, 14 S.W. 417 (1890); Marks v. Tichenor, 85 Ky. 536, 4 S.W. 225 (1887); Martin v. Carver's Admr., 8 Ky. L. Rep. 56, 1 S.W. 199 (1886); Calhoun v. Belden, 66 Ky. 674 (1868).
[5] De Funiak, Modern Equity § 87, at 208 (2d ed. 1956).

at a time when a lien might attach and within the time for filing a lien, we see that perhaps the legislature intended the meaning given "owner" by the chancellor in the case at bar. In part, KRS 376.060 provides:

> If the owner of any *legal or equitable* interest in land or improvements thereon contracts for labor or material used in the erection, repair or improvement of any structure thereon. . . . (Emphasis added.)

Harlan F. Stone, in a very exhaustive note,[6] exposes the doctrine of equitable conversion for what it is, a fiction in the law. In instances where the doctrine of equitable conversion has been heavily leaned on to reach a decision, he shows the same decision could have been reached by the proper application of the principles of equity. He further points out the relationship of the right of specific performance to equitable conversion:

> It is thus apparent that the theory of equitable ownership of land, subject to a contract of sale, is literally an incident of the right of specific performance, and cannot exist apart from it.[7]

True as this may be, in the principal case the defendants would have had the right of specific performance for the land before the house was built and the same right to the house and the land after the house was built. Thus, it seems the Kentucky Court of Appeals does not look with favor upon the doctrine of equitable conversion.

Today, one might ask what would be the effect of this decision as regards the development of large subdivisions with a substantial time interval between the completion of work by the subcontractor on the first house and his completion of work on the fiftieth house.

Under such circumstances our statutes seem to provide adequate protection for the subcontractor. Three possible approaches are available to the subcontractor with a non-severable contract for certain work on all the houses. One of the safest approaches would be for the subcontractor, immediately upon completion of each house, to file in the county clerk's office the statement of labor and materials furnished or to be furnished, as required by KRS 376.010(2), and if he had not contracted with the owner, to give notice of his intention to hold the property liable as required by KRS 376.010(3). This would insure the priority of his lien over any subsequent conveyance by the general contractor or subdivider in nearly all instances since such recordation would constitute constructive notice to a purchaser.

A second approach would be for the subcontractor to wait until he had finished the last house and then file one notice for the entire

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[6] Stone, *Equitable Conversion by Contract*, 13 Colum. L. Rev. 369 (1913).
[7] *Id.* at 386.

work in the county clerk's office and, if he had not contracted with the owner, give notice of his intention to claim a lien.[8] The third approach would be to file one notice in the county clerk's office pursuant to KRS 376.010(2) immediately after signing the subcontract. If the lien claimant had not contracted with the owner, he would then have up to seventy-five days after finishing his work on the last house to give notice as required by KRS 376.010(3).

James Avery Shuffett

SECURITIES—EXPANDED CONCEPT OF FRAUD—INVESTMENT ADVISERS ACT OF 1940.—The Securities and Exchange Commission brought this action against the defendant, a registered investment adviser. On several occasions defendant bought shares of stock for its own account. Shortly after each purchase it recommended the purchased security to clients for long term investments. Following a rise in the market price of the recommended security, defendant immediately sold its shares at a profit. The defendant failed to disclose these transactions to its clients. The Commission requested an injunction under the Investment Advisers Act of 1940[1] compelling defendant to disclose to its clients any dealings in recommended securities. The United States District Court of New York denied relief.[2] The United States Court of Appeals for the Second Circuit affirmed.[3] Certiorari was granted. *Held:* Reversed and remanded. The Commission may obtain an injunction compelling an investment adviser to disclose to clients

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[8] True, the houses which had been conveyed and their deeds recorded would escape his lien, as this case so holds, but KRS 376.060 provides a remedy:

> If the owner of . . . land or improvements thereon contracts for . . . material used in the erection . . . of any structure thereon under such circumstances that a lien for the payment thereof *may* attach to the property, and sells . . . the property *before* the expiration of the time provided for the filing and recording of a . . . materialman's lien, he shall, on receiving the consideration for the sale . . ., pay in full any sum owing for . . . materials, unless released in writing by the person furnishing the . . . materials. . . . (Emphasis added.)

The above statute entitles the subcontractor to a personal judgment for those amounts not covered by an enforceable lien. It provides for the personal judgment since all the houses sold were sold (1) at a time when a lien might attach, (2) before the expiration of the time for filing the lien, and (3) when the lien could not attach because of the provisions of KRS 376.010(2). This is true by virtue of the fact that we proceeded under one non-severable contract whereby the time limits of KRS 376.010(2) and KRS 376.010(3), needed to perfect the lien, did not begin running until the completion of the last house. Will B. Miller Co. v. Laval, 283 Ky. 55, 140 S.W.2d 376 (1940); Paterson v. Miller, 283 Ky. 60, 140 S.W.2d 379 (1940).

[1] 54 Stat. 847 (1940), as amended, 15 U.S.C. § 80b-1 (1960).
[2] 191 F. Supp. 897 (1961).
[3] 300 F.2d 745 (1961), *aff'd on rehearing* 306 F.2d 606 (1962).