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# Lien Rights and Construction Lending: Responsibilities and Liabilities in Florida

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# LIEN RIGHTS AND CONSTRUCTION LENDING: RESPONSIBILITIES AND LIABILITIES IN FLORIDA*

Originally mechanics' liens were devised to provide contractors with security interests in property they contracted to improve.[1] As an adjunct to contractual remedies, a mechanics' lien in its simplest form gives a builder a right to seek a judicial sale of property to satisfy his unpaid claims against the property owner for services or materials provided.[2] Underlying the mechanics' lien concept is the premise that the construction industry should have greater protection for extensions of credit than contract remedies provide.[3] Building tradesmen require large amounts of credit for long periods of time and potentially may commit all their capital to ongoing construction projects.[4] The inflated risks[5] and possible losses inherent in the industry were held to justify the mechanics' lien.[6]

As subcontracting became the standard mode of operation in the construction industry, mechanics' lien protection was extended to subcontractors and materialmen performing on contracts with the general contractor.[7] As a result, parties whose services and materials the owner had never directly sought obtained lien rights against his property.[8] To provide tradesmen with protection against nonpayment and yet minimize property owners' potential liability to lien claimants, legislatures developed comprehensive and complex schemes to provide uniformity and certainty of treatment to all parties. In an attempt to provide a balanced framework, the Mechanics' Lien Law in Florida has evolved into one of the largest and most complicated segments

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1. Mechanics' lien statutes were initially drafted during the 18th and 19th centuries when work on a construction project was completed by the employees of a single contractor hired by the property owner. *See* Comment, *Mechanics' Lien and Surety Bonds in the Building Trades*, 68 YALE L.J. 138, 138 (1958).

2. *Id.* at 141.

3. Dawson, *The Self-Serving Intermeddler*, 87 HARV. L. REV. 1409, 1451 (1974).

4. Stalling, *Mechanics' Lien Laws as They Exist Today*, 4 F.H.L.B. REV. 232 (1938).

5. *See generally* Comment, *supra* note 1, at 138-41.

6. *See* Stalling, *supra* note 4, at 232.

7. Modern mechanics' lien statutes give subcontractors and suppliers claims against an unknown owner inasmuch as they are parties to the owner's contract with the prime contractor. "The mechanic's lien statute telescopes these contracts and marshals them all as one," giving subcontractors and materialmen "a security that they did not contract for and probably could not have contracted for where they had not dealt directly with the owner." Dawson, *supra* note 3, at 1453.

8. *Id.* at 1446-52.

of the Florida Statutes.[9] Failure to heed the provisions of the Mechanics' Lien Law has led to considerable litigation and substantial losses that could have been avoided by compliance with the statutory provisions. Even if they have fully complied, lien claimants in many instances have forfeited their statutory rights because of the superiority of prior recorded mortgage liens. If the property owner defaults on the mortgage, a foreclosure action may declare mechanics' liens inferior to the prior recorded mortgage lien. If that occurs, foreclosure sale of the property will render mechanics' liens meaningless.

Recognizing the intent behind mechanics' lien legislation that one party not be unjustly enriched at the expense of another, Florida courts have granted equitable lien rights to lienors who failed to perfect statutory lien rights adequately or who lost priority to mortgage liens. Imposed against both owner's property and funds, equitable liens have been created from tradesmen's preferred rights in particular property and from general considerations of justice and equity.[10] The factual distinctions that have emerged from the body of judicial interpretations of equitable liens and after-the-fact equitable determinations have injected uncertainties into the construction lien area and have produced unpredictability under the lien statutes.

This note focuses on the mechanics' and equitable lien rights primarily in the construction lending context. It also traces the developing philosophy behind the Mechanics' Lien Law, emphasizing the expansion of protection for parties not in privity with the owner. The procedural requirements of the law are examined, with the focus upon the rights of those protected by and subjected to the law. The priority of the construction mortgage is discussed in the context of its interaction with the lien statutes. The priority problems are followed by an analysis of the fact situations that have led courts to impose equitable liens against property and funds. Suggestions for future alternatives which would protect all parties and seek to impose responsibilities on parties best able to minimize losses complete the scope of the note.

## DEVELOPMENT OF THE FLORIDA MECHANICS' LIEN LAW

A form of mechanics' lien appeared in Roman law[11] and in early maritime law.[12] Lien rights later developed in the civil law[13] and in the Code Napoleon.[14] English common law, however, did not recognize a mechanics'

9. The Florida Mechanics' Lien Law, FLA. STAT. §§713.01-.36 (1975), contains more than 7,000 words. S. RAKUSIN, FLORIDA MECHANICS' LIEN MANUAL i (1976).

10. *See, e.g.*, Crane Co. v. Fine, 221 So. 2d 145 (Fla. 1969); Jones v. Carpenter, 90 Fla. 407, 106 So. 127 (Fla. 1925). See text accompanying notes 119-167 *infra*.

11. MACKELDEY, HANDBOOK OF THE ROMAN LAW 274 (Dropsie's trans. 1883).

12. Comment, *California's Private Stop Notice Law: Due Process Requirements*, 25 HASTINGS L.J. 1043 (1974).

13. 1 DOMAT, CIVIL LAW §§1742, 1744 (1861). *See* Canal Co. v. Gordon, 73 U.S. (6 Wall.) 561, 571 (1867). The civil law gave very high consideration "to all who had, by their contributions, benefited, preserved, or enlarged the estate or property of another." Jones v. Great S. Fireproof Hotel Co., 86 F. 370, 386 (6th Cir. 1898), *rev'd*, 177 U.S. 449 (1900).

14. CODE NAPOLEON art. 2103, §2. The Code Napoleon accorded liens in France to masons, architects, contractors, and others employed in building houses. *See* Cushman, *The Proposed Uniform Mechanics' Lien Law*, 80 U. PA. L. REV. 1083, 1083 (1932).

lien right.[15] Under the common law, an artisan who had performed repair work on an article could retain it as security, pending payment of his bill for services,[16] but a laborer or materialman had no analogous security interest in real property enhanced by his services or materials.[17] He could only rely upon traditional contractual remedies to secure payment of his claim against the owner.[18] The mechanics' lien thus arose as a purely statutory remedy[19] benefitting parties in the building trades. Since the first mechanics' lien statute was adopted in 1791,[20] all states have adopted some form of mechanics' lien legislation,[21] and at least one state provides a constitutional mechanics' lien right.[22]

Florida first enacted mechanics' lien legislation in 1887,[23] giving to mechanics, artisans, laborers, and materialmen a lien right superior to the interests of all others.[24] The statutory mechanics' lien right was strengthened by a provision in the 1885 constitution directing the legislature to draft laws that would give mechanics and laborers liens on property which they had improved by either providing services or supplying materials.[25] Pursuant to this provision, Florida in 1935 became the only state to enact[26] the Uniform Mechanics' Lien Act,[27] which had been promulgated for the purpose of

15. *See* Canal Co. v. Gordon, 73 U.S. (6 Wall.) 561, 571 (1867). Because of its feudal character, the common law was reluctant to subject realty to payment of any claims other than feudal claims. Durling v. Gould, 83 Me. 134, 137, 21 A. 833, 833 (1890). *See* 4 AMERICAN LAW OF PROPERTY §16.106F (A.J. Casner ed. 1952).

16. *See* 10 THOMPSON, REAL PROPERTY §5186 (rev. ed. 1957).

17. *Id.*

18. An unpaid contractor or materialman could sue for breach of contract or for work performed and materials furnished. *See, e.g.*, Moore v. Crum, 68 So. 2d 379 (Fla. 1953).

19. *See, e.g.*, Sheffield-Briggs Steel Prods., Inc. v. Ace Concrete Serv. Co., 63 So. 2d 924 (Fla. 1953); Paxton-Pavey Lumber Co. v. Rehbaum, 100 Fla. 88, 129 So. 766 (1930); Harper Lumber & Mfg. Co. v. Teate, 98 Fla. 1055, 125 So. 21 (1929); Allardice & Allardice, Inc. v. Weatherlow, 98 Fla. 475, 124 So. 38 (1929). *See also* Delduca v. United States Fidelity and Guar. Co., 357 F.2d 204 (5th Cir. 1966).

20. 1791 Md. Laws, ch. 45, §10. Thomas Jefferson and James Madison proposed the Maryland legislation to provide parties involved in the construction of Washington, D.C., with security pending payment for their work. Moore-Mansfield Constr. Co. v. Indianapolis, N.C. & T. Ry. Co., 179 Ind. 356, 369, 101 N.E. 296, 301 (1913).

21. 4 AMERICAN LAW OF PROPERTY, *supra* note 15, §16.106F; G. OSBORNE, HANDBOOK OF THE LAW OF MORTGAGES §214 (2d ed. 1970).

22. CALIF. CONST. art. XX, §15. See note 25 *infra.*

23. 1887 Fla. Laws, ch. 3747.

24. The title of the bill read as follows: "An Act to Protect Mechanics, Artisans, Laborers and Material Men, and to Provide for the Speedy Collection of Moneys due them for Wages or Materials Furnished." *Id.*

25. FLA. CONST. art. XVI, §22 (1885) stated: "The Legislature shall provide for giving to mechanics and laborers an adequate lien on the subject matter of their labor." The 1968 Constitution omitted this provision.

26. 1935 Fla. Laws, ch. 17097.

27. Drafting of the Uniform Mechanics' Lien Act was undertaken in 1925 by the Standard Mechanics' Lien Act Committee of the Department of Commerce, at the request of Herbert Hoover, then Secretary of Commerce. The draft was promulgated by the Conference of Commissioners on Uniform Laws and approved by the American Bar Association in 1932. 2 R. BOYER, FLORIDA REAL ESTATE TRANSACTIONS §33.01, at 1067 (1976); Cushman, *supra* note 14, at 1085 n.6. The uniform act was withdrawn in 1943 after Florida alone

standardizing procedures for perfecting and enforcing liens.[28] Adoption of the uniform act in Florida was motivated by four goals: to place all lienors on a parity instead of giving priority to the first one to file a lien; to safeguard available funds from misapplication; to protect lienors from the filing of collusive prior mortgages; and to extend protection to owners against defaulting contractors.[29] The Legislature repealed the act in 1963,[30] but preserved its approach in the revised Mechanics' Lien Law enacted that year.[31] The revised law, renumbered in 1967 as Chapter 713, Florida Statutes,[32] remains in effect today.

### *Nonprivity Parties*

Instituted prior to the rise to prevalence of credit-basis subcontracting, the mechanics' lien historically has been based on privity of contract between the owner and the contractor.[33] Early mechanics' lien statutes conditioned the right to a mechanics' lien on a finding of strict contractual privity,[34] and the courts initially granted mechanics' lien rights only if a direct contractual relationship,[35] creating primary and direct liability,[36] existed between the owner and the lien claimant. In the view of the Supreme Court of Florida, a lien could not exist without a debt, and a debt could not exist without an express or implied contract.[37] The strict privity requirement precluded nonprivity subcontractors and materialmen from asserting lien rights under the statute.

Two judicial trends relaxed the requirement of strict contractual privity between owners and tradesmen. First, the concept of privity was gradually broadened by the courts to allow claimants to establish privity by means other than direct contractual relationships with owners. Special relationships

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among the states had adopted its provisions. One commentator suggests that the failure of the uniform act "reflected sufficient regional opposition, as contrasted with antagonistic interests of different groups affected by the statute." 4 AMERICAN LAW OF PROPERTY, *supra* note 15, §16.106F, at 228 n.11.

28. Drafters of the uniform act intended that it provide a uniform statutory scheme to replace diverse mechanics' lien statutes among the states, which had developed in piecemeal fashion. 2 R. BOYER, *supra* note 27, §33.01, at 1067.

29. *See* Lewis, *Fifth Anniversary of the Uniform Mechanics' Lien Act*, 15 FLA. L.J. 2, 3 (1941).

30. 1963 Fla. Laws, ch. 63-135.

31. FLA. STAT. §§84.011-.361 (1963) (renumbered 1967).

32. FLA. STAT. §§713.01-.36 (1967) (current version at FLA. STAT. §§731.01-.36 (1975)).

33. Spinney v. Sanford-Orlando Kennel Club, Inc., 123 Fla. 113, 166 So. 559 (1936); Hogue v. D.N. Morrison Constr. Co., 115 Fla. 293, 156 So. 377 (1934).

34. FLA. STAT. §85.25 (1927).

35. Since the mechanics' lien is a statutory creation in derogation of the common law, the terms of the applicable statutes have been strictly applied. Sheffield-Briggs Steel Prods., Inc. v. Ace Concrete Serv. Co., 63 So. 2d 924 (Fla. 1953); Shaw v. Del-Mar Cabinet Co., 63 So. 2d 264 (Fla. 1953); Rathburn v. Landess, 100 Fla. 507, 129 So. 738 (1930); Ft. Meade Hotel Co. v. Knoxville Iron Co., 99 Fla. 947, 127 So. 896 (1930); Ramsey v. Hawkins, 78 Fla. 189, 82 So. 823 (1919).

36. Harper Lumber & Mfg. Co. v. Teate, 98 Fla. 1055, 125 So. 21 (1929). *See* Stowers v. Wheat, 78 F.2d 25 (5th Cir. 1935).

37. Tallahassee Variety Works v. Brown, 106 Fla. 599, 609-10, 144 So. 848, 852 (1932).

between the parties, special knowledge on the part of the owner showing actual consent to be obligated to a nonprivity party,[38] and an express or implied assumption by an owner of a contractual obligation to pay the lienor's claim[39] were factors which were held to establish the broadened notion of privity. The owner's mere knowledge that a nonprivity materialman was furnishing materials, however, was insufficient to constitute statutory privity.[40] The second trend relaxing the strict privity requirement was the imposition of mechanics' liens based on cautionary notice[41] from the lien claimant to the owner as a substitute for actual privity.[42] The lienor's cautionary notice theoretically informed the owner of the services performed or materials supplied so that the owner could protect himself from a lien by setting aside a fund to pay the lienor's claim.[43] The courts, continuing to chip away at the notion of privity, allowed mechanics' liens in the absence of both notice and contractual privity if the owner waived notice.[44]

This imposition on a property owner of an obligation to parties with whom he never directly contracted has been justified by several theories. The prime contract arguably establishes an agency relationship, in which the contractor is authorized to make subordinate contracts pursuant to his prime contract with the owner. Were agency theory the only basis for the mechanics' lien, however, a lien right could exist under the common law of agency apart from statute, and the owner could be held personally liable[45] for the contracts made by the contractor as his agent. Since the mechanics' lien is purely statutory[46] and creates no personal liability,[47] agency theory offers an in-

38. Spinney v. Sanford-Orlando Kennel Club, Inc., 123 Fla. 113, 166 So. 559 (1936).

39. Foley Lumber Co. v. Koester, 61 So. 2d 634 (Fla. 1952).

40. First Nat'l Bank v. Southern Lumber & Supply Co., 106 Fla. 821, 145 So. 594 (1932); Tallahassee Variety Works v. Brown, 106 Fla. 599, 144 So. 848 (1932).

41. The term "cautionary notice" was coined by the Florida supreme court in All State Pipe Supply Co. v. McNair, 89 So. 2d 774 (Fla. 1956).

42. 1906 Fla. Laws, ch. 2211 (codified at FLA. STAT. §85.26 (1907)). *See* Tallahassee Variety Works v. Brown, 106 Fla. 599, 144 So. 848 (1932); Reed v. Southern Lumber & Supply Co., 73 Fla. 886, 75 So. 29 (1910).

43. Ramsey v. Hawkins, 78 Fla. 189, 82 So. 873 (1919).

44. Harper Lumber & Mfg. Co. v. Teate, 98 Fla. 1055, 125 So. 21 (1929).

45. There are four states which statutorily permit a mechanics' lienor whose claim is not satisfied by sale of the owner's property to seek a personal deficiency judgment against the owner: Pennsylvania, Illinois, Minnesota, and Idaho. *See* Dawson, *supra* note 3, at 1452 n.126; Comment, *supra* note 1, at 145 n.37.

46. *See* cases cited note 19 *supra*.

47. The Mechanics' Lien Law creates no statutory predicate for a personal judgment against a party outside a contract relationship. If a lienor fails to establish a lien for the full amount due to him, he may under the statute "recover in an action on a contract against any party to the action from whom such sums are due him." FLA. STAT. §713.28 (1975). This provision merely preserves a party's right to recover on a contract and creates no right to a personal judgment against a party not obligated by direct contract, in the absence of unjust enrichment, estoppel, fraud, or novation. Logan Constr. Co. v. Warren Bros. Constr. Co., 268 So. 2d 369 (Fla. 1972) (unpaid materialman of a subcontractor could not recover personal judgment against the general contractor since there was no amount due directly to him by the contractor). *See* King v. Ramsey, 66 Fla. 257, 63 So. 439 (Fla. 1913) (mechanics' lien statute held not to authorize personal judgment by materialman against sureties on a contractor's bond).

adequate explanation. Agency theory further may fail to account for the extension of mechanics' lien rights to sub-subcontractors and materialmen in privity with subcontractors.[48] Neither of these parties is in privity with either the owner or the contractor who could be deemed the owner's agent.

A traditional justification for protection of nonprivity parties is the prevention of unjust enrichment to the owner's property. Under this theory, the mechanics' lien provides the lienor with a method of recapturing his enrichment of the property.[49] To the extent that the purpose of mechanics' lien legislation is to hold the owner liable for the amount of the prime contract price, lien rights in his property will prevent unjust enrichment. Prevention of unjust enrichment, however, can only partially justify subjecting property to liens of parties who are outside a contractual relationship with the owner. Failure by the owner to observe the statutory scheme may

48. Prior to 1961, the Florida Mechanics' Lien Law did not protect sub-subcontractors and materialmen in privity with subcontractors. The law placed no burden on the owner for the payments of a defaulting subcontractor to his subcontractors and materialmen. Richard Store Co. v. Florida Bridge & Iron, Inc., 77 So. 2d 632 (Fla. 1954). A 1961 amendment expressed the intent of the legislature that sub-subcontractors and materialmen furnishing materials to a subcontractor were to be entitled to receive a lien under the Florida's Mechanics' Lien Law. FLA. STAT. §84.021 (1961) (repealed 1963). Construing this provision, the Florida supreme court held that the law did not envision extending the chain of protection one more link to cover sub-sub-subcontractors, these claimants being too remote in privity from the owner. Conway v. Sears, Roebuck & Co., 185 So. 2d 697 (Fla. 1966). Subsequently, the 1963 revisions of the Mechanics' Lien Law failed to re-enact the provision specifically applicable to sub-subcontractors and materialmen working for a subcontractor. One district court of appeal viewed the omission of the 1961 provision from the 1963 statute as precluding sub-subcontractors from a statutory mechanics' lien. J.P. Driver Co. v. Claxton, 193 So. 2d 440 (2d D.C.A.), *cert. denied*, 201 So. 2d 550 (Fla. 1967). The 1963 revision did not intend to alter the scope of parties entitled to mechanics' lien protection, but rather sought to correct procedural defects in the statute which had permitted "hidden liens," of which the owner was previously unaware, to attach to the property. Ceco v. Goldberg, 219 So. 2d 475 (3d D.C.A.), *cert. dismissed*, 230 So. 2d 149 (Fla. 1969), *aff'd on remand*, 252 So. 2d 849 (3d D.C.A. 1971). While the old statute had specifically protected contractors, subcontractors, and materialmen, the new statute divided potential claimants into those in privity with the owner, FLA. STAT. §713.05 (1975), and those not in privity with the owner. *Id.* §713.06. The law provided that all potential lienors not in privity with the owner should provide the owner with notice of having furnished labor or supplies to the construction project. Since this procedural change purported to protect the owner from hidden liens by giving him notice in all nonprivity situations, the *Ceco* court concluded that no reason remained to restrict the protections of the statute to parties in privity directly with the owner or contractor. The *Driver* court recently receded from its position, and followed the *Ceco* rationale, bringing an additional link in the chain, sub-sub-subcontractors, under the coverage of mechanics' lien protection. Hey Kiley Man, Inc. v. Azalea Gardens Apartments, 333 So. 2d 48 (2d D.C.A. Fla. 1976). The court concluded that no reason existed to draw an arbitrary line cutting off potential lienors, based on remoteness from privity, in light of the presently required protective notice to owner. This approach conceivably could provide a lien in an owner's property to any party who had supplied materials or provided labor so as to enhance the property and be justified on the basis of preventing unjust enrichment to the owner. To participate in a progress or final payment due from the owner, a party only in privity with a subcontractor must give notice to the owner of furnishing materials and services before the subcontractor has been paid in full.

49. *See* Dawson, *supra* note 3, at 1458.

subject his property to mechanics' liens after he has already paid the contractor for the work performed by the lienors, if the contractor fails to pay the lienors.[50] The possibility of such double payment suggests that the mechanics' lien cannot be fully understood in the light of an unjust enrichment theory. The mechanics' lien statutes, if they are to hold the owner liable for payment to subcontractors and materialmen even if he has already made payments to the prime contractor, can be justified only by a legislative determination that the subcontractor's and materialman's need for the extra protection overrides the owner's interest in limiting his liability.[51]

Reconciling the interests of the owner and the lienor often becomes a problem if the contractor has diverted funds disbursed by the owner rather than paying his subcontractors and materialmen. The owner has already paid for the work done by the lienors, who have not yet received the payments because of the contractor's misuse of the funds. If the funds cannot be collected from the contractor, who may have become insolvent, either the owner or the lienor must bear the loss. A lien against the owner's property for the full value of the lienor's contribution would satisfy the lienor's claim in full, but would subject the owner to double payment. Limitation of the lien to the unpaid amount of the prime contract would protect the owner from paying twice, but would provide the lienor only partial satisfaction for his claim.

### *Satisfaction of Lienors' Claims*

With an eye toward reconciling these conflicting interests, the Legislature adopted a two-fold purpose in enacting mechanics' lien legislation:[52] first, to ensure that lienors receive the full benefit of funds available for payment of their claims, and second, to limit the owner's liability[53] to the amount of the contract price.[54] The Legislature sought to accomplish this purpose in the 1963 revised Mechanics' Lien Law[55] by mandating the impoundment

50. FLA. STAT. §713.06(3)(h) (1975).

51. *See* Dawson, *supra* note 3, at 1453.

52. Alton Towers, Inc. v. Coplan Pipe & Supply Co., 262 So. 2d 671 (Fla. 1972); Bryan v. Owsley Lumber Co., 201 So. 2d 246 (1st D.C.A. Fla. 1967).

53. The lien right of a party in privity with the owner is based on a mutual contract between the parties and is thus logically limited in amount to the contract price. Even though lien rights of nonprivity parties originate from the prime contract, some states have adopted "Pennsylvania-type" statutes which give subcontractors and materialmen direct lien rights against the owner measured by the value of their contributions and not limited to the contract price. The Florida statute, a "New York-type" statute, grants derivative lien rights based on the contract between the owner and general contractor. The liability of the owner's property is thus limited to the amount of the contract price less payments properly made to the contractor. 4 AMERICAN LAW OF PROPERTY, *supra* note 15, §16.106F; Comment, *Mississippi Law Governing Private Construction Contracts: Some Problems and Proposals*, 47 MISS. L.J. 437, 461-62 (1976); Comment, *supra* note 1, at 142-46.

54. "Contract price" is defined by the Mechanics' Lien Law as the amount agreed upon by the contracting parties for performing the contract, as diminished by the cost of extras, change orders, or alterations to correct defects in workmanship, materials, or other breaches of contract. FLA. STAT. §713.01(3) (1975).

55. FLA. STAT. §§713.01-.36 (1967) (current version at FLA. STAT. §§713.01-.36 (1975)).

of funds initially due to a contractor and eventually due to subcontractors and materialmen, before they can be diverted from a project. The statute places on the lienor the obligation to notify the owner that he is furnishing services or materials to the project.[56] While the statutory notice to owner informs the owner of the lienor's claim, more importantly it directs the owner to impound money that would otherwise be paid to the general contractor in a progress payment.[57] Upon making any progress payment under the prime contract, the owner is obligated to make payment directly to lienors who have filed notice.[58] If the claims of lienors who have filed notice exceed the amount due on the progress payment, the owner is to prorate the amount due among the lienors.[59]

Prior to making the progress payment, the owner at his option[60] may require as a prerequisite to payment that the contractor furnish an affidavit stating the unpaid debts owed by the contractor to subcontractors and materialmen.[61] After all lienors who filed notices have been paid, the owner may use any remaining balance due on the progress payment to pay lienors whose claims appeared in the contractor's affidavit.[62] The owner has no obligation, however, to any lienor who did not file notice,[63] whether or not his bill appeared in the affidavit.[64]

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56. FLA. STAT. §713.06(2)(a) (1975).

57. Trowbridge v. Hathaway, 233 So. 2d 129 (Fla. 1970); Richard Store Co. v. Florida Bridge & Iron, Inc., 77 So. 2d 632 (Fla. 1954).

58. FLA. STAT. §713.06(3)(c)1 (1975).

59. *Id.* §713.06(3)(c)2.

60. "When any payment becomes due to the contractor on the direct contract, *except the final payment* . . . [t]he owner *may* require (and in such event, the contractor shall furnish as a prerequisite to requiring payment to himself) an affidavit as prescribed in paragraph (d)1. [FLA. STAT. §713.06(3)(d)1 (1975)], on any payment made or to be made on a direct contract . . . ." FLA. STAT. §713.06(3)(c)1 (1975) (emphasis added). Unless the owner requests that an affidavit be filed, disbursements made in the absence of the affidavit are not considered improper payments. The filing of an affidavit becomes a condition precedent to filing suit to enforce a contractor's lien prior to the time the final payment comes due only when the owner requests the affidavit. Connor v. Dreyer, 335 So. 2d 352 (2d D.C.A. Fla. 1976). When the owner does request that an affidavit be filed, it follows the form of the contractor's final affidavit, required by FLA. STAT. §713.06(3)(d)1 (1975). The statute mandates the furnishing of a contractor's affidavit before final payment may be made, however, and disbursement of the final payment in the absence of a contractor's affidavit is deemed improper and can subject the owner's property to the full value of lien claims against it. See text accompanying notes 66-69 *infra*.

61. FLA. STAT. §713.06(3)(c)1 (1975). See note 60 *supra* and text accompanying notes 66-69 *infra*.

62. *Id.* §713.06(3)(c)3. Any such payments may be deducted from the amount due the contractor. *Id.*

63. *Id.* §713.06(3)(c)1. Failure to provide statutory notice to the owner precludes a lienor from being a "priority lienor," but will not prevent participation in any balance remaining after proper payments are made from the owner to the contractor and payment is made to priority lienors. *See, e.g.*, Crane Co. v. Fine, 221 So. 2d 145 (Fla. 1969); Lopez Terrazzo & Tile, Inc. v. Cooper, 302 So. 2d 784 (3d D.C.A. Fla. 1974); Warren v. Bill Ray Constr. Co., 269 So. 2d 25 (3d D.C.A. Fla. 1972). However, the lien will be limited to the balance owing to the contractor. Bishop v. James A. Knowles, Inc., 292 So. 2d 415 (2d D.C.A. Fla. 1974).

64. The Florida supreme court held in Crane Co. v. Fine, 221 So. 2d 145 (Fla. 1969),

In addition to impounding funds due to notice-filing lien claimants, the owner must retain ten percent of the contract price or the amount of the last payment that will come due, whichever is larger.[65] The owner may not disburse this retainage fund until after receipt of a final affidavit from the contractor,[66] stating either that all lienors have been paid in full or that particular identified bills are still due.[67] Upon receipt of the affidavit, the owner may make direct payments to lienors[68] who filed notice and to lienors whose bills appeared in the contractor's affidavit.[69] If the balance due on the contract after payment to all laborers[70] is insufficient to pay these lienors' claims, and the contractor fails to furnish the difference,[71] the owner may make payments on a pro rata basis.[72]

Lienors also are forced to suffer losses when a contractor defaults and abandons a partially completed project. Applying the legislative intent to limit the amount of liens to the contract price if the owner has properly made payments[73] and retained funds,[74] the courts have permitted the amount

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that the Mechanics' Lien Law does not absolutely require notice, but rather gives lienors who have filed timely notice "priority liens," entitling them to first priority in the progress payment. Lienors who failed to file notice have the right to participate in progress payments if a balance remains after paying the claims of priority lienors. *See, e.g.*, Midway Shopping Mall, Inc. v. Corky Corp., 257 So. 2d 905 (3d D.C.A. Fla. 1972) (question whether funds remained after paying priority lienors created a genuine issue of material fact).

65. FLA. STAT. §713.06(3)(d)5 (1975).

66. *Id.* §713.06(3)(d)6.

67. *Id.* §713.06(3)(d)1.

68. *Id.* §713.06(3)(d)2.

69. See text accompanying note 87 *infra.*

70. Laborers have first priority to payment in determining lien amounts, and laborers as a class share in the final payment to the extent of their claims before other classes receive entitlement to payment. FLA. STAT. §713.06(4)(a), (b) (1975). For a general discussion of laborers' liens in Florida, see Note, *The Florida Laborers' Lien: An Unconstitutional Creditor's Remedy?*, 26 U. FLA. L. REV. 873 (1974).

71. If the balance is insufficient to pay all lienors' claims in full, the owner must withhold all payments until the contractor has had ten days to furnish the difference. FLA. STAT. §713.06(3)(d)3 (1975).

72. If the contractor has not furnished the difference within ten days from the time the contractor's affidavit was provided, the owner is to allocate funds in the same order in which all final payments are made. *Id.* Under that order, the owner is to pay, first, all laborers to the full amount of their bills, then all lienors other than the contractor to the full amount of their bills, and then the contractor. *Id.* §713.06(4)(a), (b).

73. FLA. STAT. §713.06(3)(h) (1975). The statute contains an exculpatory provision that deems an otherwise improper payment to be proper with respect to a particular lienor if it caused no detriment to the lienor. A payment which exhausted funds from which a lienor was to be paid was held to be detrimental and thus outside the scope of the exculpatory clause in Bill Ader, Inc. v. Maule Indus., Inc., 230 So. 2d 182 (4th D.C.A. Fla. 1969). The owner had failed to file a notice of commencement, and made payments to the contractor both before and after receiving lienor's notice to owner that he had furnished materials. Upon abandonment, diminution of the contract price by the cost of completion and the amount of funds previously paid to the contractor left no funds with which to pay the lienor's claims. The court allowed the lien claims to stand against the owner's property. Detriment was found to have resulted from the improper payments and not from the failure to file a notice of commencement.

74. FLA. STAT. §713.06(3)(d)6 (1975). *See* Landrum v. Marion Builders, 53 So. 2d

previously paid to the defaulting contractor to be deducted from the total contract price.[75] The reasonable cost of completing the project may also be deducted from the total contract price in computing the amount available for payment of lienors' claims.[76] Only that amount remaining after these deductions are made is available for pro rata distribution to lienors.[77] Costs of the delay and the resumption of construction may hike the cost of completion above the amount of the original contract price less payments already made to the contractor. The total amount of the contract price thereby expended, lienors retain no lien rights at all.

Under a statutory scheme aimed at simultaneously limiting the owner's lien liability to the contract price and ensuring that lienors receive the full benefit of funds properly available for payment of their claims,[78] one of the innocent parties must necessarily suffer the loss caused by diversion of funds or abandonment. Under the present statutory scheme, the owner who has made proper payments may offset payments made to the contractor and the projected cost of completion, giving him a prevailing position.[79] The only justification for this result appears to be the better capability of parties furnishing labor and materials to prevent the loss. The court in *Bryan v. Owsley Lumber Co.*[80] found that the lienor's position allowed him to determine the amount of credit to extend to the party obligated to him. That

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769 (Fla. 1951); Bryan v. Owsley Lumber Co., 201 So. 2d 246 (1st D.C.A. Fla. 1967).

75. Miller v. Duke, 155 So. 2d 627 (1st D.C.A. Fla. 1963).

76. Alton Towers, Inc. v. Coplan Pipe & Supply Co., 262 So. 2d 671 (Fla. 1972); Bryan v. Owsley Lumber Co., 201 So. 2d 246 (1st D.C.A. Fla. 1967). The owner possibly may lose the right to offset the cost of completion when he fails to pay all lienors in full or pro rata, FLA. STAT. §713.06(4) (1975), or file an affidavit stating his intention to recommence construction. *Id.* §713.07(4). Prior to the 1963 revision of the Mechanics' Lien Law, failure to record a notice of default, as required by former FLA. STAT. §84.071(4) (1963), prevented the owner from setting off the cost of completion against the fund available for payment of lienors' claims as of the date of abandonment. John T. Wood Homes, Inc. v. Air Control Prods., Inc., 177 So. 2d 709 (1st D.C.A. Fla. 1965). The requirement to file a notice of default was discontinued by the 1965 amendment, and the recommencement affidavit serves only to establish lien priority. However, failure to file the affidavit prevented the owner from offsetting his cost of completion in Melnick v. Reynolds Metals Co., 230 So. 2d 490 (4th D.C.A. Fla. 1970). *Melnick* may require filing of the affidavit or payment of the lienors before setoff will be allowed. *Melnick* may be limited, however, to situations in which the cause of the construction halt was something other than abandonment by the contractor. *See* S. RAKUSIN, *supra* note 9, at 273-74.

77. Bryan v. Owsley Lumber Co., 201 So. 2d 246 (1st D.C.A. Fla. 1967).

78. See text accompanying notes 52-57 *supra.*

79. An owner who does his own contracting also is entitled to limitation of his liability to the amount of the contract price. In Alton Towers, Inc. v. Coplan Pipe & Supply Co., 262 So. 2d 671 (Fla. 1972), *rev'g* 249 So. 2d 525 (3d D.C.A. 1971), a materialman who had given notice of his intention to claim a lien and had timely filed his notice of lien sought payment from funds held by the owner for completion of the abandoned project. Without asserting the validity of the rule that the owner is allowed to offset the cost of completion, the district court of appeal found that the rule did not apply in the case of abandonment by a subcontractor. The supreme court reversed, found that the owner/contractor's status as an owner took precedence over his status as a contractor, and allowed him to offset against the contract price the cost of completion.

80. 201 So. 2d 246 (1st D.C.A. Fla. 1967).

party's subsequent unwillingness or inability to pay was traceable to the lienor's misplaced confidence or bad judgment.[81] This result was based on the conclusion that the act of the lienor and not the act of the owner facilitated the loss, and thus the lienor should bear the loss.

*Limitation of Owner's Liability*

Compliance with the statutory scheme for making proper payments limits the owner's liability on any progress payment to the amount due on that payment and ensures that his liability for liens held by those furnishing materials and services will be limited to the amount of the contract price.[82] Thus upon disbursing the final payment in accordance with these statutory procedures, the owner is relieved of further responsibility under the direct contract with the general contractor.[83] Only when the owner fails to maintain the statutory retainage[84] or makes improper payments[85] to the detriment[86] of lienors will his property be subjected to the full amount of valid liens against it.

The preferential position given the complying owner under the statute has effectively reduced liens of nonprivity subcontractors and materialmen to a charge against unpaid funds. A lienor who fails to file notice not only loses the benefit of a priority position in progress payments, but also runs the risk of losing all lien rights if the contractor's final affidavit fails to include his claim.[87] The lienor himself perhaps justifiably could be held accountable if his failure to file notice resulted from his own neglect or ignorance. He may have deliberately failed to file notice, however, to avoid impoundment of a portion of the progress payment owing to the contractor. While impoundment earmarks funds for his own benefit, it also withholds funds from the contractor upon whom the lienor depends for payment and additional business. Fear of rescission by the contractor, who could be angered by the withholding of his funds because of the lienor's notice, might override the potential threat of nonpayment by the contractor and discourage the lienor from filing notice. Furthermore, even if he is entitled to share in the payments made by the owner, the claimant's lien is limited to a pro rata portion of the unpaid balance. If the owner has previously disbursed funds from which the lienor was to be paid, his lien is correspondingly diminished.

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81. *Id.* at 249.

82. FLA. STAT. §713.06(1) (1975) states: "The total amount of all liens allowed under this part for furnishing labor, services or material covered by any certain direct contract shall not exceed the amount of the contract price fixed by said direct contract except as provided in subsection (3) of this section." Under subsection (3), the owner's real property may be subjected to the full value of liens if the owner fails to maintain the statutory retainage or makes improper payments. *Id.* §713.06(3). See text accompanying notes 52-59 *supra.*

83. *Id.* §713.06(3)(d)4.

84. *Id.* §713.06(3)(d)6.

85. *Id.* §713.06(3)(h).

86. See note 73 *supra.*

87. *See* All State Pipe Supply Co. v. McNair, 89 So. 2d 774 (Fla. 1956).

MECHANICS' LIEN VERSUS CONSTRUCTION MORTGAGE

A mechanics' lien may provide a contractor, subcontractor, or materialman little if any real security if a construction lender holds a prior-recorded mortgage on the owner's property. When the owner defaults on the mortgage, the lender may institute foreclosure proceedings and attempt to have his mortgage lien declared superior to all other encumbrances. With a superior mortgage, the lender will be entitled to full satisfaction of his mortgage loan from the proceeds of the foreclosure sale, and he may obtain title to the property if he successfully bids at the foreclosure sale. Such a procedure effectively extinguishes subordinate mechanics' liens against the property.

*Priority of the Construction Mortgage*

Priority between the construction mortgage and mechanics' liens depends on the order of attachment.[88] A mortgage attaches to the property and takes priority when it is recorded.[89] A mechanics' lien of a contractor, subcontractor, or materialman,[90] though not perfected until a claim of lien is filed,[91] relates back[92] to the recordation of the owner's notice of commencement,[93] which sets the date of attachment and priority of the lien.[94] A mortgage recorded prior to the filing of the notice of commencement thus will prime subsequent mechanics' liens.[95] An examination of the public records by the prospective lender will reveal the notice of commencement if one has been filed. As a matter of policy, a lender will seldom take a mortgage potentially inferior to mechanics' liens that relate back to a prior-recorded notice of commencement. Thus in most instances, the mortgage lien will have been recorded prior to the filing of the notice of commencement, and will have priority over mechanics' liens against the property. Mechanics' liens, however, will be superior to a mortgage filed after the notice of commencement was filed.[96] The statute renders the notice ineffective against any person acquiring title

88. The common law rules for determining priority between claimants to the same land was that prior in time was prior in right. 2 J. POMEROY, EQUITY JURISPRUDENCE §679 (4th ed. 1918).

89. Though not specifically protected by the recording act, recorded mortgages have priority over later filed encumbrances and conveyances. 1 R. BOYER, *supra* note 27, §28.01.

90. Architects, landscape architects, engineers, and land surveyors who perform services beneficial to an owner's land and comply with the Mechanics' Lien Law also have lien rights. FLA. STAT. §713.03 (1975). Lienors who perform services or furnish materials to the property for the purpose of making it suitable as a site for construction of an improvement additionally are entitled to lien rights under the statute. *Id.* §713.04. In contrast to the liens of contractors, subcontractors, and materialmen, liens under §§713.03 and 713.04 do not attach until the time of recordation of the claim of lien, and thus do not take priority until that time. *Id.* §§713.03(3), .04, .07(1).

91. *Id.* §713.08.

92. *Id.* §713.07(2).

93. The owner files the notice of commencement pursuant to FLA. STAT. §713.13 (1975).

94. *But see id.* §713.13(5) (limiting the effective time of the notice of commencement). See note 99 *infra.*

95. *Id.* §713.07(3).

96. *Id.*

or any interest in the real property more than one year after the notice of commencement has been recorded unless the notice or a new or amended version provides otherwise.[97] A recent decision determined that under the statute, a mortgage is not "an interest in real property,"[98] indicating that the one-year limitation may not apply to defeat the priority of a mechanics' lien over a mortgage acquired later than one year after the recording of the notice of commencement.[99]

Use of the notice of commencement as the reference point for relation back of mechanics' liens was intended to eliminate the uncertainty and unreliability inherent in the pre-1963 law[100] which prescribed the time of visible commencement of work on the project as the point of attachment of mechanics' liens.[101] A lender could conceivably fail to observe that work had commenced on the project and file his mortgage lien, only to discover later that unobserved work had commenced prior to recordation of the mortgage. The notice of commencement test purportedly gives the lender justification for relying on the public records to be relatively certain of his priority.

Under the Florida Statutes, a mortgage on real property may secure both existing indebtedness and future advances, "whether such advances are obligatory or to be made at the option of the lender."[102] The lender with a prior-recorded mortgage takes priority under the statute for all advances secured by the mortgage, including amounts advanced subsequent to execution and recording. Historically, mortgages for future advances[103] have been

97. *Id.* §713.13(5).

98. United of Florida, Inc. v. Illini Fed. Sav. & Loan Ass'n, 341 So. 2d 793, 794 (2d D.C.A. Fla. 1977). A concurring opinion denied the necessity of reaching the question whether a mortgage is "an interest in real property" in the context of the Mechanics' Lien Law. *Id.* at 795 (Scheb, J., concurring specially).

99. The finding of the court in *United of Florida* that a mortgage is not "an interest in real property" would indicate that the one-year limitation of notices of commencement against subsequently acquired interests, under §713.13(5), would not be applicable to mortgages recorded after the one-year period, so that the priority of mechanics' liens would continue. The actual holding in *United of Florida*, however, may not state such a broad result, inasmuch as the rights acquired after the one-year period and declared inferior to the mechanics' lien claim were assignments of mortgages that had been acquired within one year of the notice of commencement. The court thus stated that even if a mortgage were accepted as an interest in real property, the assignees "stood in the shoes of their assignor," the mortgagee, and did not obtain any new interest in real property. *Id.* at 794. Since the mortgagee's claim had attached within the one-year period, the assignment could not subordinate the lienor's claim. If a subsequent court determined the court's finding that a mortgage is not an interest in real property to be dicta or an incorrect statement of the law, language within the court's assumption arguendo that a mortgage is an interest would support the priority of new mortgages acquired after the one-year period over mechanics' liens relating back to the notice of commencement. *Id.* at 795.

100. FLA. STAT. §84.03(1) (1959) (renumbered 1967).

101. *See generally* Silverstein, *Florida Mechanics' Lien Law — Visible Commencement*, 7 MIAMI L.Q. 477 (1953).

102. FLA. STAT. §697.04(1) (1975).

103. A mortgage for future advances secures an obligation by the single, binding promise of the mortgagor, made at the outset of the transaction, to pay back all sums

held superior to subsequent encumbrances to the extent of the amount advanced prior to the subsequent attachment.[104] If the lender were obligated to make future advances, the mortgage generally took priority over intervening encumbrances to the extent of all amounts advanced, whether initially or in the future.[105] Prior to the enactment of the current statutory language, however, Florida courts wavered on the question whether the mortgage was superior as to future advances that could be made at the lender's option.[106]

The current statute validates the properly recorded[107] mortgage as security for all advances made according to its terms, and abolishes the "optional-obligatory" test[108] that has plagued other jurisdictions.[109] Even in Florida, though, a valid claim of lien that is inferior to the initial mortgage will be superior to an increase in the mortgage indebtedness provided by a modification agreement recorded after the lien is recorded.[110]

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advanced at that time and all advances made at future times. G. OSBORNE, *supra* note 21, §114. Use of the mortgage for future advances permits the mortgagor to avoid paying higher interest on the total amount of the debt until he actually needs it. Both mortgagor and mortgagee are able to avoid the cost and inconvenience of refinancing. Note, *Mortgages for Future Advances in Florida*, 15 U. FLA. L. REV. 565, 565 (1963). The mortgagee has the further advantage of disbursing portions of the loan as the value of the secured property increases rather than making one initial payment for the full amount of the loan. G. OSBORNE, *supra* note 21, §113.

104. 4 AMERICAN LAW OF PROPERTY, *supra* note 15, §16.7.

105. Guaranty Title & Trust Co. v. Thompson, 93 Fla. 983, 113 So. 117 (1927).

106. *Compare* Bullard v. Fender, 140 Fla. 448, 192 So. 167 (1939) (failed to resolve issue of mortgagee's notice of intervening encumbrance), *with* Flynn-Harris-Bullard Co. v. Johnson, 90 Fla. 654, 107 So. 358 (1925) (priority of mortgage upheld where mortgagee had no actual notice of laborers' liens). *See* Note, *supra* note 103, at 574-77.

107. To attain priority over subsequently recorded encumbrances, the mortgage must be properly recorded. Air Flow Heating & Air Conditioning, Inc. v. Baker, 326 So. 2d 449 (4th D.C.A. Fla. 1976) (omission of legal description from mortgage caused loss of priority to mechanics' lien filed later the same day).

108. FLA. STAT. §697.04 (1975). *See, e.g.*, Silver Waters Corp. v. Murphy, 177 So. 2d 897 (2d D.C.A. Fla. 1965). Under the present statute, mortgagees "may, and when so expressed therein shall, secure not only existing indebtedness, but also such future advances." (emphasis added). FLA. STAT. §697.04(1) (1975). The language "and when no expression therein," added by a 1963 amendment, 1963 Fla. Laws, ch. 63-212, §3, might appear to impose a requirement that the mortgage state its status as a mortgage to secure future advances. Such an interpretation was not accepted by the court in Snead Constr. Corp. v. First Fed. Sav. & Loan Ass'n, 342 So. 2d 517 (1st D.C.A. Fla. 1976), which "decline[d] to attribute to the 1963 Legislature any purpose to require that such mortgages 'express' more particularly than before their purpose to secure 'future advances.'" *Id.* at 520. An earlier decision indicates that if no explicit future advances statement is made, the fact that subsequent lienors are on notice that the mortgage may cover advances not made at the execution will preserve the priority of the mortgage even as to future advances. Industrial Supply Corp. v. Bricker, 306 So. 2d 133 (2d D.C.A. Fla. 1975). The purpose of requiring the mortgage to state that it secures future advances, thus, is to give notice to parties searching the record for that fact.

109. *See* Kratovil & Werner, *Mortgages for Construction and the Lien Priorities Problem — The "Unobligatory Advance"*, 41 TENN. L. REV. 311 (1974).

110. Bowen v. American Arlington Bank, 325 So. 2d 31 (1st D.C.A. Fla. 1976).

*Loss of Lien Rights Upon Foreclosure*

Default by an owner/borrower may lead to the loss of a lienor's lien rights against property. Once the lender realizes default has occurred, he may institute foreclosure proceedings, enjoin all parties holding interests that encumber the property, and seek to have their lien claims judicially declared inferior to his prior-recorded mortgage.[111] Subsequent foreclosure sale either funnels full sale proceeds to the foreclosing mortgagee or vests in him encumbrance-free title if he successfully bids at the sale.[112] In either case, the lien claimant is left without statutory rights.

The lienor may find recourse if the court adjudicating the foreclosure finds that the mortgagee has acted to subordinate his mortgage lien to other liens. The assignee of a mortgage in *Blanchard v. Continental Mortgage Investors*[113] foreclosed a mortgage on land on which the lien claimant, under contract with the defaulting owner, had built a dam. The lienor produced evidence showing that he had been in privity not only with the owner but also with the assignee of the mortgage. The court found express and implied contracts obligating the assignee to pay for the work performed by the lienor. Additionally, the work performed on the land was found to have unjustly enriched the assignee. Under these circumstances, the assignee was held to be estopped to deny the priority of the contractor's lien to his own mortgage lien. The decision indicates that a party who has improved real property will not lose all lien rights against a lender if he has relied on the lender for payment of his debt.

THE EQUITABLE LIEN

Where statutory remedies have left parties who provided services or furnished materials with unvindicated rights, Florida courts in some cases have applied the equitable lien doctrine[114] espoused by the Supreme Court of Florida in *Jones v. Carpenter*[115] to grant lien rights apart from the statutory mechanics' lien. The state courts have imposed equitable liens upon both real property[116] and funds.[117]

111. FLA. STAT. §713.07(3) (1975). See text accompanying notes 88-110 *supra.*

112. Any surplus proceeds from the foreclosure sale over the foreclosure judgment are properly divided among successful lien claimants. Hemmerle v. First Fed. Sav. & Loan Ass'n, 338 So. 2d 82, 84 (2d D.C.A. Fla. 1976). The *Hemmerle* court held that foreclosure judgments should be based on the total of monies actually advanced on the loan and properly expended for construction, and not the total amount of loan commitments, thereby preventing the lender who unsuccessfully bids at the foreclosure sale from obtaining a windfall gain at the expense of the successful bidder, who would receive a project worth less than the bid he made high enough to exceed the foreclosure judgment, and lien claimants, who would likely have no surplus in which to share.

113. 217 So. 2d 586 (1st D.C.A. Fla. 1969).

114. *See generally* Boyer & Kutun, *The Equitable Lien in Florida*, 20 U. MIAMI L. REV. 731 (1966).

115. 90 Fla. 407, 106 So. 127 (1925).

116. *See, e.g.*, Jones v. Carpenter, 90 Fla. 407, 106 So. 127 (1925) (homestead property); Imler Earthmovers, Inc. v. Schatten, 240 So. 2d 76 (1st D.C.A. Fla. 1970) (specific improved land); Lake Sarasota, Inc. v. Pan Am. Sur. Co., 140 So. 2d 139 (2d D.C.A. Fla. 1962) (realty of shareholders of dissolved corporations).

117. *See, e.g.*, Crane Co. v. Fine, 221 So. 2d 145 (Fla. 1969) (fund owed to contractor);

The broad language used by the *Jones* court[118] has led to extremely flexible application of the equitable lien. Justified initially out of "a general consideration of right and justice,"[119] equitable liens have been imposed in cases involving fraud,[120] misrepresentation,[121] and estoppel.[122] Recent court decisions[123] have applied the "special and peculiar equities" test adopted by the Florida supreme court in *Crane Co. v. Fine*[124] as the basis for imposing equitable liens. Courts have extended the equitable lien doctrine to cases such as *Crane,* involving potential mechanics' lien claimants confronted with procedural bars to establishing statutory liens.[125] Courts have also employed the equitable lien to restore lien rights to claimants with liens subordinated to prior-recorded construction mortgages.[126] Numerous assertions of equitable lien rights in widely varying fact situations have engendered much confusion as to the requirements necessary to establish equitable lien rights. Such confusion has been particularly troublesome in cases in which equitable liens have been sought against funds, and specifically against undisbursed construction loan proceeds, rather than property.

Most claimants asserting equitable lien rights in Florida have relied, directly or indirectly, upon *Jones.* In *Jones,* the Florida supreme court recognized the equitable lien as an equitable "right of a special nature" over an item of property, entitling a party to proceeds from a judicial sale of the property.[127] The property owner in *Jones,* a former bank president, had made improvements on his privately owned property using embezzled bank funds. The bank subsequently went into bankruptcy. Unable to collect the unpaid funds from the insolvent former president, the trustee in bank-

Morgen-Oswood & Assocs., Inc. v. Continental Mortgage Invs., 323 So. 2d 684 (4th D.C.A. Fla. 1975) (construction loan proceeds).

118. See text accompanying notes 127-131 *infra.*

119. Jones v. Carpenter, 90 Fla. 407, 106 So. 127 (1925).

120. *See, e.g.,* Schraub v. Charest, 277 So. 2d 814 (3d D.C.A. Fla. 1973).

121. *See, e.g.,* Phelps v. T.O. Mahaffey, Inc., 156 So. 2d 900 (2d D.C.A. Fla. 1963) (owner's misrepresentations of ownership justified imposition of equitable lien).

122. *Cf.* Merritt v. Unkefer, 223 So. 2d 723 (Fla. 1969) (court failed to find chain of estoppel).

123. *See, e.g.,* Dykema v. Trans State Indus., Inc., 303 So. 2d 52 (2d D.C.A. Fla. 1974) (availability of adequate legal remedy plus absence of special and peculiar equities prevented imposition of equitable lien); Marshall v. Scott, 277 So. 2d 546 (2d D.C.A. Fla. 1973) (equitable lien denied in absence of special and peculiar equities).

124. 221 So. 2d 145 (Fla. 1969).

125. *See, e.g.,* Westinghouse Elec. Supply Co. v. Midway Shopping Mall, Inc., 277 So. 2d 809 (3d D.C.A. Fla. 1973) (failure to give timely notice did not preclude equitable lien); O.H. Thomason Builders' Supplies, Inc. v. Goodwin, 152 So. 2d 797 (1st D.C.A. Fla. 1963) (noncompliance with Mechanics' Lien Law not a bar to equitable lien).

126. *See, e.g.,* Morgen-Oswood & Assocs., Inc. v. Continental Mortgage Invs., 323 So. 2d 684 (4th D.C.A. Fla. 1975); Fred S. Conrad Constr. Co. v. Continental Assurance Co., 215 So. 2d 45 (1st D.C.A. Fla. 1968).

127. The *Jones* court said: "It is simply a right of a special nature over the thing, which constitutes a charge or incumbrance upon the thing, so that the very thing itself may be proceeded against in an equitable action, and either sold or sequestered under a judicial decree, and its proceeds in the one case, or its rents and profit in the other, applied upon the demand of the creditor in whose favor the lien exists." 90 Fla. at 412, 106 So. at 129.

ruptcy, a nonmaterialman with no statutory lien rights,[128] sought to obtain an equitable lien against the improved property.

The court traced the equitable lien to two alternative sources:[129] a written contract showing an intention to charge some particular property with a debt or obligation,[130] or a declaration by a court of equity out of a "general consideration of right and justice" as applied to the particular relationship of the parties and the circumstances of the case.[131] While no contract imposed a charge on the improved property in *Jones,* the court found that right and justice could justify an equitable lien in favor of the bank, the funds of which had been used to improve the encumbered property. Since the bank had involuntarily paid for the improvements incorporated into the property, the trustee as successor to the bank's interest was held to be entitled to a lien by which he could subject the property to sale to regain the bank's funds.

The equitable lien theory was applied to a potential mechanics' lien claimant in *Palmer v. Edwards.*[132] In contrast to the *Jones* trustee, the *Palmer* claimant had a statutory mechanics' lien right which he had failed to assert.[133] Upon sale of the property by the allegedly insolvent owner/debtors, the contractor sought to establish his rights to the sale proceeds. The court held that the contractor was entitled to an equitable lien and thus had rights under the sales contract. The court neglected to indicate whether its decision turned on the existence of a contract between the owner and the contractor or on a general consideration of right and justice.[134] Apparently the court was swayed by the argument that a decision adverse to the contractor would have permitted the owner/debtor to obtain the full proceeds of the sale, which represented in part compensation for the value added to the property by the contractor's improvements. The owner would have been unjustly enriched, and the contractor would have had no means of recovery since the property was no longer in the owner's possession.

Subsequent courts have relied on the *Palmer* precedent to grant equitable liens to a party who performs services or furnishes materials in the improve-

128. The parties who had furnished the materials had been paid from the embezzled funds. The trustee was not an unpaid materialman and thus had no lien right under the statute.

129. Jones v. Carpenter, 90 Fla. 407, 106 So. 127 (1925); *accord,* Carter v. Suggs, 190 So. 2d 784 (1st D.C.A. Fla. 1966). *See* 1 L. JONES, THE LAW OF LIENS §27, at 25 (3d ed. 1914).

130. 90 Fla. at 412, 106 So. at 129; *see* Wagner v. Roberts, 320 So. 2d 408 (2d D.C.A. Fla. 1975) (equitable lien granted to assignee of invalid mortgage where mortgage proceeds had benefited the property).

131. 90 Fla. at 412, 106 So. at 129. The "consideration of right and justice" half of the *Jones* equitable lien criteria has been interpreted to require circumstances such as fraud or misrepresentation of essential facts to validate the claim. Jennings v. Connecticut Gen. Life Ins. Co., 177 So. 2d 66 (2d D.C.A. Fla. 1965) (contractor not entitled to lien for materials and labor against lessor's interest in property, absent fraud or misrepresentation or any requirement in lease that lessee make improvements).

132. 51 So. 2d 495 (Fla. 1951).

133. The decision does not reveal the reason for the contractor's failure to assert his mechanics' lien right against the property. The court apparently believed imposition of an equitable lien in this instance to be correct regardless of the reason for the failure to assert a claim.

134. See note 131 *supra.*

ment of real property although he has not availed himself of the statutory mechanics' lien remedy.[135] In *Green v. Putnam*,[136] an alleged joint venturer sought a mechanics' lien against property owned by his co-venturer, or an equitable lien in the alternative. Without deciding whether the plaintiff was entitled to a mechanics' lien, the Florida supreme court imposed the equitable lien. The court found that imposition of the equitable lien would prevent unjust enrichment of the co-venturer at the expense of the plaintiff.[137] To subsequent courts, the line of reasoning used by *Jones, Palmer*, and *Green* established the right to an equitable lien as an additional remedy for the mechanics' lienor.[138]

### Crane Co. v. Fine: *The Special and Peculiar Equities Test*

Under the Florida mechanics' lien scheme of giving claimants a right against the retainage fund, held for the purpose of satisfying lien claims, the question arose whether an equitable lien could be imposed against that fund. In *Crane Co. v. Fine*, [139] the Florida supreme court affirmatively decided that question, utilizing the "special and peculiar equities" test, upon which courts have relied in applying the equitable lien doctrine. The complaining materialman in *Crane* had completed work on a construction project, entitling him to receive payment from a $15,000 fund held by the defendant general contractor for payment of the plumbing subcontractor, plaintiff's debtor. The subcontractor had abandoned the job before receiving payment for the work already performed. The court found that the materialman had "a right of a special nature" in particular property, *i.e.*, the $15,000 hold-back fund. Because the plumbing subcontract work had been fully performed, the contractor holding the fund was held to have no right to the fund other than as a security holder for unpaid materialmen. The court said: "We hold only that, because of the special and peculiar equities shown by the record in this particular case, the plaintiff should not be foreclosed from seeking an equitable lien merely because he was entitled to but failed to perfect his statutory materialman's lien."[140]

While the "special and peculiar equities" language, derived by the court from its earlier decision in *Wood v. Wilson*,[141] had potential for broad application, the *Crane* decision emphasized its inherent limitations in applying the

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135. *See* cases cited notes 136-138 *infra*.

136. 93 So. 2d 378 (Fla. 1957).

137. *Id.* at 380.

138. *See, e.g.*, Armstrong v. Blackadar, 118 So. 2d 854 (2d D.C.A. Fla. 1960) (court granted equitable lien even though claimant, had he complied with statute, would have been entitled to mechanics' lien); Dewing v. Davis, 117 So. 2d 747 (2d D.C.A. Fla. 1960) (grove caretaker who performed work on property of owner who consented to the performance was entitled to assert equitable lien as well as statutory lien); Tucker v. Prevatt Builders, Inc., 116 So. 2d 437 (1st D.C.A. Fla. 1959) (contractor who had completed paving and curb construction work for insolvent owner entitled to equitable lien against realty in hands of owner's creditors).

139. 221 So. 2d 145 (Fla. 1969).

140. *Id.* at 149.

141. 84 So. 2d 32 (Fla. 1955).

equitable lien doctrine. The existence of undisbursed funds[142] and the incorporation of the plaintiff's materials in the construction project were not the factors that constituted the basis for the imposition of the equitable lien in *Crane*.[143] Had these factors alone been sufficient justification, *Crane* would stand for the proposition that any contracting party or supplier could assert an equitable lien against property and undisbursed funds, permitting an infinite string of equitable liens.[144] *Crane* must be read in the context of its limited facts: separate funds had been set aside for work already completed, the plaintiff materialman had a clear entitlement to the fund, the general contractor had no remaining right to the fund, and the general contractor in no way would be paying twice for the same work if the equitable lien were awarded.

### *Applications of the "Special and Peculiar Equities" Test*

Subsequent decisions[145] emphasize the actions of the parties holding the property rather than those of the lien claimants. A materialman defrauded out of a mehcanics' lien in *Hall's Miscellaneous Ironworks, Inc. v. All-Southern Investment Co.*[146] was unable to obtain an equitable lien against encumbered property upon foreclosure by the lender because the lender had not perpetrated the fraud. The contractor had initially persuaded the materialman not to perfect his mechanics' lien right so that there would be no encumbrance on the property that might deter mortgage financing. The contractor/owner had represented to the materialman that he would pay him for materials supplied before obtaining the mortgage. Without making payment, the contractor/owner had executed a mortgage which took priority over any subsequently attaching liens. When the contractor/owner became insolvent, the materialman retained no means of recovery and sought an equitable lien against the property in his counterclaim to the lender's foreclosure action.

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142. Subsequent to *Crane*, the Florida supreme court denied the imposition of a mechanics' lien against undisbursed funds because the facts, in contrast to the *Crane* facts, failed to show the existence of an undisbursed surplus. Trowbridge, Inc. v. Hathaway, 233 So. 2d 129 (Fla. 1970); *accord*, W.W. Gay Mechanical Contractors, Inc. v. Case, 275 So. 2d 570 (1st D.C.A. Fla. 1973) (court declined to establish fictitious fund).

143. In imposing the equitable lien, the *Crane* court said: "We emphasize that this opinion is not to be interpreted as holding that a materialman is entitled to seek an equitable lien merely because his materials are incorporated in the improvement." 221 So. 2d at 149.

144. On the basis of the decisions in the Florida line of equitable lien cases culminating in *Crane*, one commentator has said that "the notion of preventing unjust enrichment of vendors and lessors, once released, ballooned away from the launching pad. It floats freely now through the Florida skies, taking the form of equitable liens independent of statute and based on 'right and justice.' It is impossible to predict where these wayward vehicles will land in Florida but so far, at least, their orbits have been confined within the sunshine state." Dawson, *supra* note 3, at 1455-56.

145. *See, e.g.*, Dykema v. Trans State Indus., Inc., 303 So. 2d 52 (2d D.C.A. Fla. 1974) (absence of special and peculiar equities prevented imposition of equitable lien in favor of architect who failed to file action on his claim of lien within the statutory time period).

146. 283 So. 2d 372 (1st D.C.A. Fla. 1973).

The court acknowledged that the contractor's deliberate fraud on the materialman[147] and his possible unjust enrichment established the basis for an equitable lien against the property, but denied an equitable lien with priority over the lender's mortgage. The court found insufficient participation by the lender in the fraud to establish overriding equities necessary for an equitable lien to prevail.[148] *Hall's* indicated, however, that the subcontractor might have a claim against excess proceeds from the foreclosure sale remaining after satisfaction of the lender's prior mortgage.

Misconduct by a lender, not present in *Hall's*, swayed the court to find an equitable lien against a loan fund balance in *Morgen-Oswood & Associates, Inc. v. Continental Mortgage Investors*.[149] The lender had set aside the amount contained in the fund as a retainage fund from which the contractor would be paid, but had refused to disburse the final payments and retainage under the construction loan agreement and had commingled the amount with other funds. A key to the *Morgen-Oswood* holding was the completion of the construction project, which gave the lender the full value of the security for which it had bargained. Had the equitable lien failed, the lender would have been unjustly enriched as the result of his own misconduct in refusing to disburse the final payments and retainage.[150]

Parties seeking equitable liens against undisbursed construction loan proceeds have relied on *Morgen-Oswood*[151] as an extension of the holding in *Fred S. Conrad Construction Co. v. Continental Assurance Co.*[152] that a surety and a contractor had a cause of action against a lender's undisbursed funds on which they had relied. Decided prior to *Crane*,[153] *Conrad* made no reference to equitable lien rights, but focused upon priority to the undisbursed funds. The owner of the construction property had defaulted on his obligation to the lender but the lender had permitted the contractor and surety to continue work on the project and had paid them additional sums. The lender instituted foreclosure proceedings and the contractor and surety alleged in counterclaims that the lender's failure to notify them of the default justified their claim of priority to the undisbursed loan fund. The court found a cause of

147. The court found that the mortgage had been executed for the purpose of defrauding Hall's of the benefit of the labor and materials it had furnished for incorporation in the partially completed building. *Id.* at 373.

148. The court stated in dictum that the allegations if substantiated by proof would establish the right to an equitable lien against the property. *Id.* at 374. Since the instant action, however, was against only the lender, the failure to establish overriding equities entitling the equitable lien to priority over the mortgage lien defeated a cause of action against the lender, on which the counterclaim was based.

149. 323 So. 2d 684 (4th D.C.A. Fla. 1975).

150. The court found that the equities were strong enough to defeat allegations that the mortgagee had been the victim of a kickback arrangement between the owner and the contractor. In the words of the court, "[i]f ever there was a case for imposition of an equitable lien on a particular property, it is this one." *Id.* at 684.

151. J.G. Plumbing Serv., Inc. v. Coastal Mortgage Co., 329 So. 2d 393 (2d D.C.A. Fla. 1976); Brief for Appellant at 11-13, Bastillion Dev. Co. v. Gilmer, 339 So. 2d 1163 (1st D.C.A. Fla. 1976).

152. 215 So. 2d 45 (1st D.C.A. Fla. 1968).

153. See text accompanying notes 139-144 *supra*.

action based on the lender's conduct as well as the contractor's and surety's right to rely on the loan fund.[154]

The equitable liens imposed in *Conrad* and *Morgen-Oswood* offer the subcontractor or materialman little real assurance of recovery. *Conrad* appears to support the imposition of an equitable lien if the lender has failed to notify parties working on a project of an owner's default. However, *Conrad* held only that counterclaims and crossclaims by the potential equitable lienors should not be dismissed and did not adjudicate the case on any fact findings. Moreover, the opinion stated no basis for a lender's duty to inform potential lienors of a default, if he does have such a duty. Direct payments made by the lender to the contractor and the surety arguably established a direct contractual relationship between them and may limit the holding to those facts.[155] A lender's failure to inform parties supplying materials and labor of the owner's default, however, does not conclusively establish the entitlement to an equitable lien.

In *J.G. Plumbing Service, Inc. v. Coastal Mortgage Co.*,[156] a plumbing subcontractor sought to impose an equitable lien on undisbursed construction loan proceeds held by the lender. The subcontractor, relying on *Crane*,[157] *Morgen-Oswood*,[158] and *Conrad*,[159] argued its entitlement to the lien based on the lender's failure to inform him of the default and pending foreclosure.[160] The court, focusing on the incomplete nature of the project, refused to impose an equitable lien on the fund. A completed project would have given the lender the security for which he bargained, as well as the undisbursed proceeds.[161] Retention of the excess would in that instance have resulted in the type of unjust enrichment found in *Morgen-Oswood*.[162] The mortgagee in *J.G. Plumbing* obtained only a partially completed project, the market value of which probably would be less than the total cost of labor and materials used in its construction.[163] Entitlement to the undisbursed funds thus was held necessary to protect the value of the lender's security, and the equitable lien was denied.

The interwoven aspects of justifiable reliance and unjust enrichment found in *J.G. Plumbing* render it a difficult guide for determining what

154. The court held that the parties had stated a cause of action for relief up to the remaining balance of undisbursed funds provided for in the mortgage loan agreement. 215 So. 2d at 47.

155. *Conrad* has been cited by only one court, which stated that the lienors' reliance on *Conrad* in that instance was misplaced, primarily because of the failure in *Conrad* to state additional relevant facts such as whether the construction was complete or not. J.G. Plumbing Serv., Inc. v. Coastal Mortgage Co., 329 So. 2d 393, 395 (2d D.C.A. Fla. 1976). The lack of judicial interpretation of *Conrad* limits its applicability for analysis purposes.

156. 329 So. 2d 393 (2d D.C.A. Fla. 1976).

157. See text accompanying notes 139-144 *supra*.

158. See text accompanying notes 149-150 *supra*.

159. See text accompanying notes 151-154 *supra*.

160. 329 So. 2d at 395.

161. *Id.*

162. "In essence, [*Morgen-Oswood*] was a case in which relief was granted in order to avoid an unjust enrichment." *Id.*

163. *Id.*

particular facts give rise to the imposition of an equitable lien. The court's emphasis on the incompleteness of the project suggests that unjust enrichment was the decisive factor. The court acknowledged that under facts similar to the *Morgen-Oswood* facts, in which construction had been completed prior to the default, an equitable lien would be justified to prevent unjust enrichment.[164] The additional finding in *J. G. Plumbing* that the lender had not affirmatively misled the subcontractor, however, suggests that an equitable lien on undisbursed loan proceeds could be created under alternative facts in which the lender's wrongful actions would entitle the lienor to rely on the fund.[165] This interpretation would be consistent with the court's distinction of *Morgen-Oswood,* which involved wrongful refusal to disburse funds as well as unjust enrichment. Reluctance to impose an equitable lien if the lender has committed no fraud or wrongful conduct is further supported by the court's reliance on *Hall's,* in which an equitable lien was denied priority because the lender had not been involved in the fraud perpetrated on the materialman.

While *J.G. Plumbing* provides a subcontractor or materialman with no assurance of equitable lien rights against a loan fund based solely on either completeness of the project or representations made by the lender, it suggests useful pleading considerations to a potential lienor. Since the case made no distinction between a fully completed project and a substantially completed one, a subcontractor or materialman could argue that a project was at least substantially complete, and that full entitlement to the lender of the loan proceeds would result in unjust enrichment. The potential lienor could further support his case for an equitable lien by arguing that various actions on the part of the lender affirmatively misled him into continuing to work on the project in reliance on the lender's representations to him.

*J.G. Plumbing* imposes no duty on the lender to advise subcontractors and materialmen of the status of the mortgages. The case suggests that such a duty might discourage the lender and mortgagee from working together to correct the default and complete the project.[166] False advice by the lender, however, might constitute fraud and misrepresentation[167] and subject the loan fund to subcontractors' and materialmen's equitable liens. A subcontractor or materialman might be well advised to inquire directly of the lender regarding the status of the mortgage. If the lender informed the lienor of the

164. *Id.*

165. *J.G. Plumbing* was cited in a decision in which an equitable lien was denied on property superior to a bank's mortgage lien because of the lack of material misrepresentation, fraud, mistake "or some factual circumstance tending to show that the bank (the lender) exercised 'affirmative deception' on the subcontractor to keep it on the job." Gancedo Lumber Co. v. Flagship First Nat'l Bank, 340 So. 2d 486 (3d D.C.A. Fla. 1976). *Accord,* Snead Constr. Corp. v. First Fed. Sav. & Loan Ass'n, 342 So. 2d 517, 520 (1st D.C.A. Fla. 1976).

166. 329 So. 2d at 395.

167. *See, e.g.,* Rood Co. v. Luber, 91 So. 2d 629 (Fla. 1956); Schraub v. Charest, 277 So. 2d 814 (3d D.C.A. Fla. 1973) (dealings between the parties disclosed fraud and misrepresentation necessary to establish equitable lien); *cf.* Merritt v. Unkefer, 223 So. 2d 723 (Fla. 1969) (absence of mistake or material misrepresentation led to denial of equitable lien).

default, the lienor could protect himself by discontinuing work on the project. If the lender, seeking to prevent a work stoppage, withheld the default information, the lienor could argue that the lender in so doing had assumed the contractual obligation or had misrepresented facts and was estopped from asserting the priority of his mortgage lien. A contractor could argue that the continued receipt of direct payments established the predicate for direct lien rights, even if the lender had been silent as to the default.

The lender can protect himself against potential lien liability by informing subcontractors, materialmen, and contractors of the owner's default when it occurs,[168] but he risks jeopardizing the completion of the project and the value of his security. The factual distinctions made in *J.G. Plumbing* give the lender no certain means of assuring retention of the undisbursed funds by following any particular course of action.

While expansion of the equitable lien doctrine has been justified by equitable considerations, one important side effect has been the partial replacement of the certainties imposed by the Mechanics' Lien Law procedures by the indefiniteness created by equitable lien factual distinctions. Strict application of the Mechanics' Lien Law might subject a party to an unjust loss, but the possibility of equitable lien imposition diminishes the guidance and predictability provided by the statutory provisions. Analysis of the leading cases that have formed the body of precedent for granting equitable liens when mechanics' liens have failed illustrates the trend toward broadening the equitable lien doctrine and the uncertainties such new breadth brings.

## ALTERNATIVES FOR THE FUTURE

Statutory and equitable liens in Florida have been used as effective tools for reconciling the interests of parties involved in construction projects, but the uncertainties and side effects created by their application have reduced the protection afforded lenders, owners, and lien claimants. The complexity of the Mechanics' Lien Law has caused unsuspecting lien claimants to lose lien rights and occasioned owners to lose the benefit of limited liability. The statutes have failed to provide for the exigencies of the modern construction industry, such as the reluctance of a potential lienor to file a notice that would cause building funds to be impounded. This restriction might place a strain on his continuing relationship with the contractor who needs the funds to complete the project. By following the statutory provisions, lienors preserve priority rights in undisbursed funds, but because the owner is favored by the limitation of his liability to the amount of the contract price, the full effect of any loss falls upon the lienors. Claimants must rely on a body of case law tenuously tied together by uncertain equitable principles. Lending institutions have no preventive means to protect themselves from equitable lien assertions and resultant proceedings. Consequently, the intent that rights under the Mechanics' Lien Law be based on statutorily prescribed factors has been eroded.

168. *Cf.* J.G. Plumbing Serv., Inc. v. Coastal Mortgage Co., 329 So. 2d 393 (2d D.C.A. Fla. 1976).

Assuming the continued desirability of the special protection accorded parties involved in construction projects,[169] a statutory scheme that provides greater certainty of protection for these parties is a proper goal. If the statute is to provide subcontractors and materialmen with actual security as it was designed to do, some protection should be given to counterbalance the inferiority of their claims to prior-recorded construction mortgages. Claimants should not be forced to rely on the uncertain equitable lien as the sole means of vindicating their rights. Contractors who properly perform their contracts should retain lien protection, but should bear the responsibility for improper use of funds. Owners should continue to be liable only for the amount of the contract price. Finally, lenders should retain priority for construction mortgages as security against subsequent lien claimants to ensure the continued availability of construction financing. As controller of the purse strings, however, the lender should have some power to manage the disposition of disbursed construction funds.

Adoption of a form of statutory stop notice is one means of attaining these objectives that merits legislative consideration in Florida. A stop notice is a lien on construction funds, in contrast to a mechanics' lien attaching to property.[170] Though wide variations distinguish the various stop notice type statutes enacted by other states,[171] the basic stop notice approach provides unpaid lien claimants with priority to undisbursed funds held by the lender or owner.[172] A lien claimant who has not received payment on his account files a stop notice with the lender or owner, providing notification that his account is overdue. The stop notice as adopted by the state of Washington "opens a new line of communication between lender and subcontractors, with the hope of 'red flagging' nonpayment of subcontractors and exposing potential mechanics' liens early in the project."[173]

In the sense that it provides information of lien claimant accounts, the stop notice is analogous to the notice to owner requirement in Florida. The stop notice, however, differs in two respects. First, it provides specific information as to amount of the claim and the fact of nonpayment. Second, this information could be provided to the lender as well as the owner.

The lender's responsibility upon receipt of a stop notice may take several

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169. Commentators have raised the question whether the special credit protection afforded the construction industry by mechanics' liens remains justified. *See, e.g.*, Comment, *California Mechanics' Liens*, 51 CAL. L. REV. 331, 360-62 (1963).

170. *See* Comment, *supra* note 12, at 1048.

171. Several states have adopted statutory stop notice. *See, e.g.*, ALA. CODE tit. 33, §37 (1975); CAL. CIV. CODE §§3156-3172 (West Supp. 1974); IND. CODE §32-8-3-9 (1975); WASH. REV. CODE §60.04.210(2)-(4) (Supp. 1975).

172. The stop notice is in this sense an extension to the lending situation of the Florida statutory requirement that the owner withhold funds due notice-filing lien claimants.

173. Note, *Mechanics' Liens: The "Stop Notice" Comes to Washington*, 49 WASH. L. REV. 685, 695 (1974) (citing G. Mooney, *Implementing the Law Relating to Liens, Including Mechanics' and Materialmen's Liens*, Mar. 28, 1973 (Bill Digest Form, H.B. No. 4), regarding enactment of 1973 Wash. Laws, ch. 47, §2 (codified at WASH. REV. CODE §60.04.210(2) (Supp. 1975))).

forms. California has the broadest stop notice statute,[174] construed to allow a stop notice claimant to freeze any unexpended construction funds held by the lender or owner.[175] The lenders and owners must withhold from the contractor amounts sufficient to pay stop notice claims filed, even though the amount of the claim may not be owed to the contractor when the notice is filed.[176] In contrast, under the Washington stop notice statute, the lender who complies with the statute and who receives a stop notice claim need withhold from the subsequent draw only a portion equal to the percentage of completion of the project that is attributable to the work performed by the stop notice claimant.[177] A lender who elects not to withhold funds, loses his construction mortgage priority to the extent of the filed claim.[178] Alternatively, he may immediately foreclose on the project.[179]

The Washington statute offers the most desirable approach to stop notice. The amount of a stop notice claim is limited to a portion of each progress payment, thus only requiring the lender to withhold a relatively small amount of the loan fund.[180] The undesirable result of a stop notice in which a very large claim freezes the entire construction fund and halts the flow of payments would be obviated. In addition, the lender's liability would be limited to amounts actually owing on the loan. Further, the amount withheld would be based only on work actually completed, as reflected in the contractor's most recent certification of job progress.[181]

The threat of work stoppage caused by the diminution of draws resulting from the withholding of large sums to meet stop notice claims must be ameliorated for a stop notice scheme to have a potential for success. A stoppage could result in two particular situations. First, a claimant could submit a large claim, to which the contractor objected, causing funds to be withheld and draws delayed until the claim is settled. Second, a nonpayment to some subcontractors might trigger a massive filing of stop notices by claimants fearful that draws to the contractors are being diminished and actually produce that result, tying up construction funds and halting the project. The statute could provide for summary judgments for quick adjudication of these claims. Alternatively, the statute could provide that the lender make full disbursement to the contractor, but transfer the stop notice claim to security by bonding it.

Under a stop notice statute, a lender who objected to the responsibilities placed on him to meet the claims of unpaid subcontractors and materialmen

174. CAL. CIV. CODE §§3156-3172 (West Supp. 1974).

175. Comment, *supra* note 12, at 1049.

176. A-1 Door & Materials Co. v. Fresno Guar. Sav. & Loan Ass'n, 61 Cal. 2d 728, 733-35, 394 P.2d 829, 834, 40 Cal. Rptr. 85, 89 (1964).

177. WASH. REV. CODE §60.04.210(4) (Supp. 1975). *See* Comment, *supra* note 12, at 1057.

178. WASH. REV. CODE §60.04.210(6) (Supp. 1975).

179. Note, *supra* note 173, at 696.

180. *Id.*

181. Under the Washington statute, "[d]raws against construction financing shall be made only after certification of job progress by the general contractor and the owner or his agent in such form as may be prescribed by the lender." WASH. REV. CODE §60.04.210(1) (Supp. 1975).

could avoid the stop notice requirements and in the alternative require at the outset of the project that the owner post a payment bond.[182] A bond for the full amount of the contract price would provide all parties with protection sought by the stop notice procedure. Parties not covered by the owner's bond could be protected by subordinate bonds. Thus, a sub-subcontractor, though not entitled to recover on the owner's bond, could recover against a bond put up by the contractor. In deciding whether to opt for the stop notice procedure or for bonding, the lender necessarily would be confronted with a trade-off situation. The stop notice procedure would avoid the difficulty and expense of obtaining bonding[183] and would reduce overall construction costs.[184] The bond procedure, however, would avoid the burdens of complying with the stop notice procedure and the construction delays that might result from late payments to stop notice claimants.

By providing potential lien claimants with a security interest in a portion of the loan fund, the application of the equitable lien and its inherent uncertainties could be eliminated. Traditional equitable factors such as fraud and material misrepresentation might still trigger the equitable lien, but the direct right against the loan fund would obviate equitable lien claims based on reliance on the fund. Upon abandonment, the lender would be entitled to use undisbursed funds to complete the project. Stop notice claimants would be entitled to funds remaining after completion of the project.

In revising the Florida Mechanics' Lien Law, legislators should seek to provide maximum protection to the parties involved in construction projects while at the same time preventing owners and lenders from being subject to double payment for the same work. Florida should approach the lien question in a manner analogous to the stop notice concept by seeking to resolve problems that arise from improper disbursement of funds early in the project rather than deferring final settlement until the project is either completed or abandoned. By imposing on the lender greater responsibility for individual progress payments, this goal of identifying nonpayment of subcontractors and materialmen before further disbursements are made should minimize losses and give lienors some protection. The very nature of lien law anticipates that losses will occur in the construction industry, but the law must impose responsibilities on all parties to ameliorate losses that do occur.

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182. Florida law currently exempts the owner from withholding the statutory retainage if he obtains a payment bond. FLA. STAT. §713.23 (1975).

183. Owners who have not established lines of credit often find bonding difficult if not impossible to obtain. The necessity to borrow money under a mortgage loan may indicate the lack of established credit necessary for a bond, leading him to resort to pledging the value of the completed building as security for the loan. A bond must protect the full amount of the contract price, and since the owner has pledged his value in the building on the mortgage, a bonding company will require that he have assets in addition to that building before bonding him.

184. The adoption of either of these statutory measures would increase the overall cost of construction lending and should be accompanied by an increase in the permissible rates of interest that may be charged under the Florida usury laws.