

NEW YORK CONSTRUCTION LAW UPDATE

This article is written and published by Vincent T. Pallaci, Esq. Mr. Pallaci is a construction attorney with the law firm of Kushnick & Associates, P.C. and he practices construction law in New York State. Mr. Pallaci is also the publisher and author of the New York Construction Law Update blog (<http://newyorkconstructionlawupdate.blogspot.com>) and the New York Mechanic's Liens blog (<http://nymechanicsliens.blogspot.com>)

THE MYSTERIOUS "BOND TO DISCHARGE ALL LIENS"

Odds are that if you have been in the construction industry for long enough then you probably know what a payment bond is and what a performance bond is. You probably have also come across a mechanic's lien discharge bond and perhaps even a bid bond or a maintenance bond. But the rarely used "bond to discharge all liens" likely will leave you with a blank look on your face. Don't worry, you wouldn't be alone. The bond to discharge all liens is rarely used and most in the industry do not even know it exists. But they should.

The bond to discharge all liens is created under Lien Law Section 37. Pursuant to Lien Law Section 37, the owner or general contractor may, either before or after work begins, obtain and file with the county clerk a bond that will prevent any lienor from attaching a mechanic's lien to the property even before that lienor does work. The bond to discharge all liens must be in at least the amount that is unpaid under the contract between the general contractor and the owner. In other words if you have a \$5,000,000.00 contract, and you are obtaining the bond to discharge all liens and a payment has not been made, then the bond must be in the amount of \$5,000,000.00. Likewise, if only \$2,500,000.00 remains due under the contract at the time that you seek the bond to discharge all liens, then the bond must be in at least the amount of \$2,500,000.00. A caveat with the bond to discharge all liens is that a judge must set the amount of the bond to prevent owners or general contractors from being less than truthful about the amount left due under the contract in an effort to reduce the bonding costs.

The bond must be issued by a fidelity or surety company authorized to do business within the State of New York and, in general, is the same type of surety that you would use to obtain a mechanic's lien discharge bond.

Once the bond is obtained and filed with the clerk, the project continues the same as any other project. However, in the event a subcontractor or supplier is not paid, rather than filing a mechanic's lien against the property, they simply go to the county clerk's office and file a claim against the lien to discharge all bonds. The notice of claim functions in much the same way as a mechanic's lien and must be filed in the same time frame as a mechanic's lien. The notice of claim must contain:

1) the name and residence of the claimant; and if the claimant is a partnership or a corporation, the business address of such firm, or corporation, the names of partners and principal place of business, and if a foreign corporation, its principal place of business within the state;

(2) the names of the owner, contractor and surety named in the bond;

(3) the name of the person by whom the claimant was employed or to whom he furnished or is to furnish materials;

(4) the labor performed or materials furnished, including also materials actually manufactured for but not delivered to the real property, and the agreed price or value thereof;

(5) the amount unpaid to the claimant for such labor or materials;

(6) a description of the real property such as is required for a notice of lien.

You may have noticed that this is essentially the same information you would have to put into a mechanic's lien.

The claim against the bond to discharge all liens is then enforced in a lawsuit much the same way that a mechanic's lien is foreclosed upon. The summons and complaint must be filed with the county clerk where the bond is filed and must name the owner, the surety that issued the bond and all other claimants that have made claims under the bond prior to the time the action is commenced. The bond enforcement claim must be brought within one year of the completion of the project or, if the project is abandoned, within two years of the time that the claimant last provided labor or materials to the project.

Contractors should be careful. If a bond to discharge all liens has been filed on a project you are working on, you cannot file a mechanic's lien against the property. If you go ahead and do so anyway, the owner or the general contractor can apply to the court for summary discharge of your mechanic's lien. This is especially important because if you file your mechanic's lien, and the owner or general contractor files a petition to discharge your lien after the time for you to file a new lien expires, then your mechanic's lien will be discharged and you will be out of time to submit a claim against the bond. As I said at the beginning, while you many don't know what the bond to discharge all liens is, you should!

There are obviously pros and cons of the bond to discharge all liens. On the pro side, it prevents liens from attaching to the property. The lender on your construction loan will undoubtedly appreciate that. It will also prevent the owner and the general contractor from having to continuously respond to various liens during the course of the project, especially if the lienor is far removed and the general contractor doesn't even know who the lienor is (i.e. in the case of a supplier to a sub-subcontractor). Another pro is the scenario I described above, if a mechanic's lien is improperly filed against the property, the owner and general contractor

through smart practice might be able to get the liens discharged and simultaneously prevent bond claims from being submitted.

The biggest con of the bond to discharge all liens is the costs. You have to make an application to the court in the beginning of the process to set the amount of the bond. You then have to put up the money to a surety to post the bond. If the contract is large, this could be a substantial amount of money. But if the surety will accept a letter of credit, the costs are minimized.

The bond to discharge all liens is not for every project. But it is a good option for the right project, maybe even yours.