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POP QUIZ FOR BUILDERS, REMODELERS & SUBS: LEGAL ISSUES IN RESIDENTIAL CONSTRUCTION

***Sales of Homes (For Builders)*:**

(1) Q: If a buyer who has executed a Purchase Agreement for a spec home notifies you, the builder and seller of the home, of one of the following, does the buyer have a valid reason for failing to close on the property?

a. Failure/inability to obtain financing for the purchase of the home.
b. Failure/inability of buyer to sell current home.
c. Newly discovered information regarding undesirable aspects of the neighborhood.
d. Defects founded during the inspection process.

A: Each of the answers depends upon the exact language used in the Purchase Agreement, but the following information should also be noted:

a. **It depends, but likely yes.** Failure/inability to obtain financing for the purchase of the home is generally included within a purchase agreement as a contingency that must be met, and if it is not, the buyer has a valid reason for not closing. However, a buyer must have used reasonable and good faith efforts to try to obtain financing, but despite such efforts, was unable to obtain financing.

b. **It depends.** Failure/inability of a buyer to sell his current home is a valid reason for not closing only if it is included as a contingency within the purchase agreement.

c. **Likely No.** Newly discovered information regarding undesirable aspects of the neighborhood will almost always not be valid excuse for a buyer to back out of a purchase agreement.

d. **It depends.** Defects founded during the inspection process may be provide a valid reason for a buyer not to close if the buyer timely and properly disclosed such defects, and depending upon the language of the purchase agreement, if the builder failed to timely remedy such defects. A good purchase agreement will state that defects not disclosed within the provided period (e.g., 10 days) are waived. Iowa courts have strictly upheld this type of language.

(2) Q: If a buyer who has executed a Purchase Agreement for a spec home fails to close on the property without a valid legal defense or excuse, can the builder/seller sue the buyer and ask the Court to force/compel the buyer to close?

A: No. However, the builder/seller can sue for monetary damages and is entitled to all available damages stemming from the buyer's breach of the purchase agreement, including (a) the eventual difference between the purchase price under the purchase agreement and ultimate purchase price of the property; (b) all of the seller's costs to hold, carry, and maintain the property after the closing date until the eventual resale and close date, including mortgage interest payments, utilities, insurance, property, taxes, etc.; (c) any additional consequential damages; and (d) all costs and reasonable attorney's fees per the language of the purchase agreement.

(3) Q: If a builder builds a house for Person A in 2001, and Person B buys the house in 2009, can Person B sue the builder for alleged defective construction (i.e., breach of the implied duty of good and workmanlike construction) in 2012?

A. Yes, Person B can sue the builder based upon a case law extension of the implied duty of good and workmanlike construction to subsequent purchasers and the 15-year statue of repose (which may be decreased down to 10 years with the current legislation).

Mechanic Lien Questions (For Builders, Remodelers and Subs)

(4) Q: Does or should a subcontractor. . .

a. Deliver any type of notice to the general or the owner at the commencement of the project? If so, to whom? If so, what are the consequences for failing to deliver such notice?
b. Deliver any notice to the eventual homeowner of a house being built under contract with the general contractor if the general contractor owes the house at commencement of the project?
c. Check the county assessor's records prior to the job? If so, for what purpose?

A: In the case of an owner-occupied dwelling, the subcontractor can only enforce the lien to the extent of the balance due the principal contractor at the time the written notice is served on the owner-occupant (including within the 90 days.[1] (No

notice to the general is required by the sub.) The notice given to the owner must inform the owner-occupant of the subcontractor's lien and rights, and advise the owner-occupant to withhold any further payments to the contractor until a waiver of the subcontractor's lien is provided.[2] **A subcontractor should provide this notice to the homeowner via hand-delivery or via certified mail (return receipt requested) immediately upon beginning his work on the project.** If in doubt as to whether the structure is owner-occupied, provide this notice. If an owner-occupant makes payment to the contractor after receipt of this notice, he does so at his own risk.[3]

Regarding (b), the safest route is for the sub to deliver a notice to both the homeowner and the builder (even when the builder owns the property throughout some or all of duration of the project). However, if the subcontractor does not have actual or constructive notice that the ownership of the property has changed hands at the time of the filing of the mechanic's lien, then some courts have held that no notice is or was required by the sub.[4] Other courts may hold otherwise in certain situations.

The safest route is for the sub, before starting a project, to check the county assessor's records for this very purpose if there is any doubt.

(5) Q: Can one enforce a mechanic's lien when the work is performed for, and contracted through, the tenant (and not the owner of the property)?

A: Generally, no, unless the work was "required" under the terms of the lease (and courts have interpreted this requirement element differently).

(6) Q: If a general/direct contractor (e.g., builder/remodeler) or sub fails to file the mechanic's lien within 90 days of the last furnished material or labor, are they out of luck?

A: Their recovery based upon an untimely filed lien depends on the circumstances. Though, in this event, the general contractor or sub should still file a lien.

For a general contractor, an extra notice must be served (not just mailed) upon the owner, along with the mechanic's lien, in this event.

For a sub, the lien can only be enforced to the extent of the balance due from the owner to the contractor at the time the lien is served (unless a bond was given by the contractor).Therefore, where the owner has already paid the full contract price to the contractor, the late-filing subcontractor is unable to secure any portion of the contract price (unless a bond exists). Also note that in this situation the sub must serve (not just mail) the mechanic's lien.

Suppliers/subs of subs also have a notification requirement, but such requirement does not apply to single-family or two-family dwellings occupied or intended to be used for residential purposes. The requirement does, however, apply to condominium projects, apartment houses, and commercial real estate.

(7) Q: Can one file an amended mechanic's lien to increase the amount of the lien?

A: No.[5]

(8) Q: How long does one have to sue on a mechanic's lien? Are there any exceptions?

A: Two years plus the 90 days. An exception applies when a homeowner sends you a 30-day notice demanding suit within 30 days; after such 30-day period, the lien cannot be enforced.

<u>Attorney's Fee Questions</u>

(9) Q: Can a direct/general contractor recover attorney's fees in a successful action to foreclose a mechanic's lien? Can a sub?

A: Yes (but fees are still within the court's discretion). No for a sub. Also, note that a successful defendant challenging a mechanic's lien an also recover attorney's fees.

(10) Q: Can a direct/general contractor recover attorney's fees in a successful action on a breach of contract claim against

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the owner of the home? Can a sub recover attorney's fees in a successful action on a breach of contract claim against the general?

A: Yes and yes, if and only if, a properly drafted attorney's fees provision is within the written contract.

Other Possible Topics to be Discussed

• Verbal modifications and changes when the effective contract has a provision barring amendments except in writing.
• Best practices regarding change orders.
• Best practices regarding written contracts.
• Acceptance of a counteroffer by silence or acquiescence with the commencement of work by the other contracting party.
• 2011 Mechanic's Lien Case: A sub was out of luck against a homeowner even when funds were available due to the sub's failure to file a mechanic's lien.
o Welte Insurance v. Big Red Lighting, Lumberman's Brick (Iowa App. 2011): Subcontractor was denied recovery.
- A homeowner's contractor, which was hired to contract a home, only paid some of the subs prior to disappearing. Certain funds were deposited in escrow at closing, pending the resolution of the disputes between the homeowner and various subcontractors
- Among other things, the appellate court found that a certain subcontractor (of a subcontractor) was not entitled to any of the available escrows to compensate the sub for the value of the work performed because the sub failed to timely file a mechanic's lien (and enforce that lien). **The court emphasized that the sub's only available method of payment other than from the general contractor (or subcontractor), with whom the sub (or sub-sub) contracted, was to promptly perfect/file and enforce a mechanic's lien. This conclusion remains true even if there may be money available to remedy the unjust enrichment claimed by the sub.** This was a reversal of the lower decision.

• Practice Pointers:
• Subs must file a mechanic's lien if they want to enforce any right to payment against the owner.

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The information contained herein is not intended to be an all-inclusive summary or discussion of Iowa construction law or mechanic's lien law. Further, this information is not intended to be legal advice and should not be relied upon in analyzing your specific issues or legal questions. Please consult an attorney for your specific legal needs.

1. I.C.A. § 572.14(2).
2. I.C.A. § 572.14(3).
3. I.C.A. § 572.16 ("nothing in this chapter shall . . . require the [owner-occupant] to pay a greater amount or at an earlier date [than in the principal contract] unless the owner pays a part or all of the contract price to the principal contractor after receipt of notice under section 572.14, subsection 2"); *see also* Conrad v. Coop. Grain, 488 N.W.2d 450, 452-453 (Iowa 1992)
4. Louie's Floor Covering, Inc. v. De Phillips Interests, Ltd. , 378 N.W.2d 923 (Iowa 1985).
5. Section 572.26 states the amount of the lien claim may not be amended. Presumably, this means the lien claim may not be increased, as there would appear to be no valid reason for refusing reductions in the lien demand.