

## Subcontractor's Lien Claim: Craft v. Stevenson Lumber Yard

In the case of Craft v. Stevenson Lumber Yard, Inc., 179 N.J. 56 (2004), the New Jersey Supreme Court considered the challenge of an Appellant property owner regarding a decision of the Superior Court, Appellate Division (New Jersey), which affirmed a trial court's order granting summary judgment to appellee subcontractors in the property owner's action to discharge the subcontractors' liens and the subcontractors' counter-actions to enforce the liens under the Construction Lien Law (CLL), N.J.S.A. 2A:44A-1 to -38.

The owner had retained third-party defendant contractor to construct a residence, and the subcontractor purchased supplies from the subcontractors. The owner paid the contractor when payments became due, and the owner, in turn, paid the subcontractors, but one subcontractor applied the payments to other debts owed by the contractor. The contractor eventually ceased construction.

Craft had paid \$166,980.00. Michael Aladich, the principal of Aladich, filed for personal bankruptcy and the corporation became insolvent by late summer of 1999.

On June 16, 1999, Stevenson filed a Construction Lien Claim against the real property owned by Craft in the amount of \$ 53,019.59. Dubell Lumber Company, a second supplier, also filed a construction lien claim against Craft in the amount of \$ 7,649.35. That matter was consolidated with



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Stevenson's. Craft filed a Complaint demanding a judgment dismissing the Construction Lien Claim. Stevenson filed a Third Party Complaint against Aladich for \$ 75,000, the amount owed Stevenson for all of the projects for which Stevenson had provided supplies. Following arbitration, in which the arbitrator determined that Craft was not liable, Stevenson moved for a trial de novo. The parties filed cross-motions for summary judgment and the trial court ruled in favor of Stevenson and Dubell.



Craft appealed, challenging the legitimacy of Stevenson's lien claim and the existence of a lien fund in connection with the claims of both Stevenson and Dubell. The Appellate Division affirmed the grant of summary judgment in favor of Stevenson and Dubell, holding that the innocent homeowner must bear the financial burden caused by a defaulting contractor, despite paying for his supplies in full and despite having no knowledge that the contractor had outstanding accounts with its supplier.

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## out of order

"I do not mind lying, but I hate inaccuracy."

- Samuel Butler

A liar should have a good memory."

- Quintilian

"All men are born truthful, and die liars."

- Vauvenargues

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The Supreme Court granted Craft's Petition for Certification. In addition, the Court granted amicus curiae status to the Building Contractors Association of New Jersey ("BCA/NJ") and to the Northern New Jersey Chapter, Inc., National Electrical Contractors Association ("NECA").

This appeal presented two issues under the Construction Lien Law (CLL), N.J.S.A. 2A: 44A-1, et seq.. First, Whether an innocent property owner is liable to a supplier where the owner has paid his general contractor for supplies, which payments were transferred to the supplier without being earmarked, and were not recognized by the supplier as satisfying that property owner's account balance. The second issue pertains to the lien fund: What is the measure of the amount that is available to a subcontractor or supplier with a lien claim where the contractor has abandoned the job at a point at which the property owner has made all of the progress payments to date?



The Court explained that the main purpose of the CLL - to help secure payment to contractors, subcontractors and suppliers who provide work, services, material or equipment pursuant to a written contract - is achieved by empowering them to file lien claims and thus protect the value of the work and materials they have provided. A second goal of the Act is to ensure the rights of property owners who have met their financial obligations and to preclude imposing upon them the burden of double payment for work and materials.

As a general proposition, a creditor who is owed more than one debt by a debtor may apply the payments to the debtor's account in any manner it chooses so long as the debtor has not issued specific directions to the contrary. That is known as the payment application rule. That rule, however, is not absolute. Where, as here, the creditor knows or should know that a debtor is under an obligation to a third party to devote a relevant payment to discharge a duty the debtor owes to the third party, the payment must be applied accordingly regardless of the debtor's instruction or lack thereof. Within the terms of the Restatement (Second) of Contracts 258, Stevenson knew or had reason to know that it was not free to apply Aladich's payments at will. Aladich could not have directed the application of Craft's payment to any but Craft's obligations without breaching its duty to Craft, and Stevenson was likewise obligated to ascertain the source of Aladich's payments and to apply them accordingly. Moreover, Stevenson had a statutory duty to allocate Aladich's payments to the accounts from which they were derived if it wished to file a lien claim.

Reversing, the court held that (1) with respect to the validity of one of the subcontractor's lien claim under N.J.S.A. 2A:44A-9, the subcontractor had a duty to determine which of the contractor's projects was the source of its payment and to allocate the payment accordingly, and, thus, because the subcontractor failed in that duty, it was unable to verify the existence of a debt as required under the CLL, and no lien claim against the owner's property could be advanced; and (2) regarding the lien fund, the measure of the amount available to the subcontractors was determined in accordance with N.J.S.A. 2A:44A-10 and -23, and, because the contractor walked off the job at a point at which he had been paid to date and was owed no money by the owner, there was no lien fund.



The court reversed the judgment of the appellate court and remanded for the entry of judgment in favor of the owner declaring that no lien fund existed.