

The Contractor's "Sledge Hammer" – The Sale of the Owner's Property (or Threat Thereof) Under North Carolina's Lien Law

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In North Carolina, like many states, the most effective tool in the contractor's tool bag to ensure payment for work is the ability to hold the land improved as security for amounts due. The mechanics, laborers and materialmen's lien has been recognized as so fundamental a tenet of North Carolina law that it is specifically provided for in the State's Constitution: "The General Assembly shall provide by proper legislation for giving to mechanics and laborers an adequate lien on the subject matter of their labor." N.C. Const., Art. X, Sec. 3. The North Carolina General Assembly fulfilled this constitutional mandate by adopting Chapter 44A of the General Statutes. It is Article 2 of Chapter 44A that deals specifically with liens arising out of the construction process.

The purpose of this article is to describe the "sledge hammer" of the lien law – the process by which a contractor or material supplier can actually force the sale of the owner's real property in satisfaction of its lien rights. An informal poll of construction lawyers and clerks of court confirms that this "sledge hammer" is almost never actually wielded. This is true because, practically speaking, the effect of the public record filing of the initial claim of lien or notice of claim of lien at the beginning of the process, or the sometimes lengthy litigation process to enforce the lien, is often enough to result in the discharge or resolution of the underlying claim before it reaches the lien judgment or foreclosure sale stage. Having said that, a construction lawyer should have a working understanding of the lien foreclosure sale process in North Carolina.

To get to the point of foreclosing on the real property improved, several fairly obvious preconditions must be met. First is the fact that the lien at issue must be of a type that entitles the claimant to a lien upon the improved real property. Broadly speaking, Chapter 44A provides for a lien

on the real property improved in three situations:

- Where the contractor or material supplier contract directly with the owner of the real property. *See* N.C. Gen. Stat. § 44A-8.
- Where a first through third tier subcontractor or supplier perfects its subrogation based lien rights on the real property (as opposed to a lien merely on funds). *See* N.C. Gen. Stat. § 44A-23.
- Where a subcontractor or material supplier of any tier acquires a direct lien on the real property due to the owner's unauthorized payment of funds after receipt of a notice of claim of lien under N.C. Gen. Stat. § 44A-20.

In each of the circumstances outlined above, the lien claim must be properly perfected according to the type of lien to be asserted by the claimant. While it is not within the scope of this article, strict adherence to all of the formal statutory requirements of Chapter 44A including service, required information in the lien form itself, and filing within the 120-day limitation period are an absolute must. *See* N.C. Gen. Stat. §§ 44A-10 through 44A-12, 44A-17 through 44A-19, and 44A-23.

Assuming a lien has been properly perfected, an action to enforce the lien must be commenced no later than 180 days after a claimant last provided labor or materials to the project. N.C. Gen. Stat. § 44A-13(a). While it is better practice to file the suit in the county where the real property is located, this is not a mandatory requirement. N.C. Gen. Stat. § 44A-13. There may be circumstances where the property extends into more than one county. There may be other circumstances where the property is located in a

different county from where the litigants reside. If the suit is filed in a different county from where the property is located, then a notice of *lis pendens* must be filed in the county where the property is located. *Id.* The *lis pendens* gives notice to title searchers that a lawsuit has been filed to enforce the lien, and that the lien has not expired. The *lis pendens*, like the lawsuit itself, must be filed within 180 days after the last furnishing of labor or materials to the site. *Id.* If the title to the property at issue, however, belongs to a receiver or trustee in bankruptcy, then the lien will be enforced by the court having jurisdiction over the real property. *Id.*; *RDC, Inc. v. Brookleigh Bldrs.*, 309 N.C. 182, 305 S.E.2d 722 (1983).

Assuming the lien claimant prevails on its claim, the court will then enter a judgment in the amount proven and will include a specific order that directs the sale of the real property subject to the lien. *Id.* One should note that under the statute, the judgment may not exceed the principal amount of the claim of lien that it is enforcing. N.C. Gen. Stat. § 44A-13(b).

Notice and Logistics of an Execution Sale

Once all of the above steps are satisfied, the procedure to compel the sale of property in satisfaction of a judgment enforcing the lien is governed by N.C. Gen. Stat. § 44A-14(a). This statute in turn incorporates by reference the judgment execution sales procedures set forth in N.C. Gen. Stat. §§ 1-339.41 through 1-339.76. These procedures differ from the familiar Chapter 45 procedures applicable to power of sale foreclosures in North Carolina in a number of important respects. Chief among the differences is the administration by the sheriff of the entire construction lien execution sale process, whereas the power of sale

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foreclosure process under Chapter 45 is administered through a trustee and the parties in interest.

The most crucial step in conducting a valid lien execution sale of real property is ensuring proper notice. The notice of a sale must reference the execution order and judgment that authorized the sale, state the date, hour, and place of sale, describe the real property, and state that the sale will be made to the highest bidder for cash. N.C. Gen. Stat. § 1-339.51, § 1-313. The notice must also be published in an area designated by the clerk of superior court for twenty (20) days preceding the sale, and be published once for at least two successive weeks in a newspaper qualified for legal advertising, or if no such paper exists in that county, then one with county-wide circulation. *Id.*

If the notice of sale is published in a newspaper, then the notice must be published for not less than seven (7) days and the date of the sale shall not be more than ten (10) days preceding the last publication of the notice. N.C. Gen. Stat. § 1-339.52. Moreover, if the lien affects real property in more than one county, the notice requirements must be met in each county. *Id.*

In addition to the general notice requirements to the public, notice must be provided to the judgment debtor at least ten (10) days before the sale of the property, and if the debtor is found in the county, then the sheriff must serve a copy of the notice on him personally. N.C. Gen. Stat. § 1-339.54. If the debtor is not found in the county, the sheriff must send a copy of notice by registered mail to his last known address and serve a copy on the debtor's agent in the county, if one exists. *Id.* While a number of the statutory requirements impose service and notice obligations on the sheriff to facilitate a smooth foreclosure sale process (*see* N.C. Gen. Stat. § 1-339.54), a lien judgment creditor is wise to provide the sheriff's department with all the necessary notices and forms and should oversee the process closely.

The sale itself must be scheduled in accordance with the prescribed statutes. A sale may be held on any day other than Sunday. N.C. Gen. Stat. § 1-339.43. Most notably, the sale of the real property must be at the courthouse door in the county in

which the property is located. N.C. Gen. Stat. § 1-339.44. The sale must not start before 10:00 a.m. or after 4:00 p.m. Moreover, sales cannot continue after 4:00 p.m. except in cities or town with populations greater than 5,000. N.C. Gen. Stat. § 1-339.60. Within five (5) days after the date of the sale, the sheriff must file a report of sale with the clerk of the superior court. N.C. Gen. Stat. § 1-339.63.

Returning to the venue issue, the practitioner should consider before he first files his lien that the foreclosure sale of the property subject to the lien may only be conducted in the county where the real property is located. Moreover, if he files a lien on real property that includes different parcels in multiple counties, then separate sales must be conducted in each county.

N.C. Gen. Stat. § 1-339.64 provides for a ten (10) day "upset bid" process, which provides a short period in which the bid price for the property resulting from the sale may be increased by post-sale upset bids which must exceed the original bid by at least five (5) percent and otherwise satisfy the other statutory requirements.

Disposition of Proceeds of the Sale

Once the sale is consummated and the upset bid period has expired, the sheriff is required to tender to the clerk all proceeds of the sale, minus the expenses incurred in administering the sale and caring for the property pending the sale. N.C. Gen. Stat. § 1-339.70. Finally, the clerk then applies the proceeds to the payment of the lien creditor's judgment, with any surplus payable to the owner of the real property or other person legally entitled to it. N.C. Gen. Stat. § 1-339.70. Assuming the proceeds of the sale are sufficient, the sale of the property satisfies the lien and passes all title and interest to the purchaser free and clear of all interests or other liens arising "after the first furnishing of labor or materials at the site of the improvement by the person claiming the lien." N.C. Gen. Stat. § 44A-14(a).

Sale of Property Upon Order Prior to Judgment

By way of an interesting side bar, N.C. Gen. Stat. § 44A-14(b) provides for an infrequently used process by which a construction lien claimant who has properly perfected its lien on real property and instituted an enforcement action may seek a *pre-judgment* sale of improved real

property. The procedure allows a Superior Court Judge, upon notice to all interested parties and a hearing, to order a *pre-judgment* sale. The moving party must first meet the high standard of demonstrating that sale prior to judgment is necessary to prevent "substantial waste, destruction, depreciation or other damage to said real property prior to the determination of said action. . . ." *Id.* Once this standard has been satisfied, the statute allows the judge to determine the method of sale of the property as long as it is commercially reasonable. *Id.* Likely due to the fact that this statute is not often invoked, there is no reported appellate court authority in North Carolina interpreting the statute.

Conclusion

Practically speaking, while it is uncommon for a construction or material supplier to have to continue the lien process to its bitter end and actually proceed to a sale of the improved real property, it is important for construction law practitioners to be familiar with the entire lien claim process, including the "sledge hammer" of the execution sale procedure. Doing so will allow us to best advise and serve our clients.

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