BUSINESS TOOLKIT

Mechanic's Lien Ruling a Mixed Bag

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A recurring problem in commercial leasing is a tenant-hired contractor coming after the landlord when the tenant fails to pay, typically with mechanic's lien foreclosure and unjust enrichment claims against the landlord. The landlord often has given the tenant funds to pay the contractor as part of a build-out allowance, which the tenant spent on something else.


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The recent decision *Wang Electric., Inc. v. Smoke Tree Resort, LLC*, 230 Ariz. 314, 283 P.3d 45 (App. 2012), resolved a number of open landlord-liability issues in this context.

In *Wang,* the tenant's general contractor failed to pay its subcontractors, who then recorded mechanic's liens against the landlord's property and filed suit to foreclose them. The lease required the tenant to make improvements approved by the landlord and the landlord gave the tenant an improvement allowance. The lease stated that "no mechanic's or other lien for any ... work or materials [furnished to tenant] shall attach to or affect [landlord's] interest in the [p]remises" and represented that the sole relationship between the parties was that of landlord and tenant.

The first issue was whether a self-serving lease provision inserted by the landlord disclaiming any mechanic's lien liability or agency relationship with the tenant could insulate the landlord from liability to a tenant-hired contractor on a mechanic's lien foreclosure claim. The general rule in Arizona is that the landlord is liable if the tenant was required under the lease to make the improvements on the theory that the tenant was acting as the landlord's agent in hiring the contractor. To thwart liability, landlords began putting such disclaimers in their leases, but it was unknown whether they were enforceable. *Wang* held no.

The court ruled that the landlord could not defeat the statutory agency relationship with its tenant by including self-serving language to that effect in the lease.

The only way for a landlord to avoid mechanic's lien liability is to clearly state in the lease that any improvements are done at the tenant's sole election and expense, but that leaves the landlord at risk when a tenant does not perform the approved build-out.

Where design compliance is an issue, the better approach is to a create a mechanism for ensuring that tenant improvement funds are used to pay contractors, such as requiring lien releases in exchange for the release of funds, or hiring a third-party administrator to undertake this supervisory role. If no tenant improvement funds are provided, another possibility is to require the tenant to buy a contractor payment bond.

The second issue in *Wang* was whether a landlord is liable for unjust enrichment simply because the contractor performed work increasing the value of the property even though the landlord did nothing wrong. The court held no. The landlord is *only* liable if it engaged in improper conduct, such as not paying a promised improvement allowance. However, this is little consolation given the landlord's simultaneous mechanic's lien foreclosure liability.

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prohibiting such discussions during work hours or prohibiting their appearance on Facebook pages.

If employees are permitted to discuss non-work-related topics on-the-clock, employees should also be allowed to exchange information relating to their working conditions, including benefits and pay. And it only takes two employees talking to obtain protection. If an employee wants to grouse about a supervisor on social media and the audience includes at least one co-employee, the protection prevails.

One way to avoid NLRB scrutiny, including having to defend against an NLRB charge or lawsuit, is for employers to avoid continued reliance on existing, outdated policies or drafting their own based on samples from the Internet or generic office software. Tiffany & Bosco can provide answers and help ensure compliance with NLRA or other employment-related laws.