

A RECENT CASE SIGNALS EXPANDED LIEN LAW PROTECTIONS FOR SUBCONTRACTORS IN NEW YORK CITY



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A recently-decided case in the State Supreme Court in New York City named *The Ideal Supply Co., Inc. v. Interstate Fire Protection, Inc.* appears to have opened the door for subcontractors who are not getting paid by their contractors to bring new claims under the New York Lien Law.

The Lien Law does many things for subcontractors. Of course, it allows subcontractors to file mechanics' liens, which critically protect the rights of unpaid subcontractors. However, the Lien Law does much more than that.

Under the Lien Law, all contract payments contractors receive from a project owner must be held "in trust" for the subcontractors' benefit. This means that the money has to be used to pay the subcontractors' invoices. Similarly, higher tier subcontractors hold payments from their contractors "in trust" for lower tier subcontractors and so on through the material suppliers and laborers. These funds are referred to as "Lien Law Trust Funds."

Under the Lien Law it is actually a crime — larceny — for a contractor to "divert" Lien Law Trust Funds. A contractor "diverts" trust funds when it uses trust funds for a purpose other than paying the subcontractors. The classic example of a "trust fund diversion" is a contractor using money that it received from an owner on Project A to buy materials for Project B.

Although the Lien Law makes trust fund diversion a crime, subject to criminal punishment, it says nothing about "civil" lawsuits for this behavior. That is, the Lien Law does not specifically say that a subcontractor can sue the contractor, or its officers, for money damages as a result of a trust fund diversion.

Although the facts of the *Ideal Supply* case are complicated, in this case the subcontractor said it was not getting paid by the general contractor, even though the general contractor had been paid by the owner. As a result, the subcontractor sued both the general contracting company and the general contractor's individual officers.

The general contractor tried to have the claims against its officers thrown out. Under well-known contract law, only the parties to the contract — usually contracting *companies* — can be held responsible for a breach of the contract. Usually, the officers of a contracting company cannot be held personally responsible for the company's obligations under the contract. But the subcontractor in the *Ideal Supply* case did not rely on its contract to make the claim. Instead, the subcontractor sued the contractor's officers under the New York Lien Law.

Generally speaking, the Lien Law is very particular. If something is not specifically provided for in the text of the law itself, then the right does not exist. Nonetheless, the Court in the *Ideal Supply* case did not throw out the subcontractor's lawsuit against the officers. The Court did so even though the Lien Law does not specifically say that a subcontractor could sue the individual officers and even though the Court could not find a case that allowed this type of claim from the appellate court that controls its decisions in New York City.

So what does this mean? The recent decision was a preliminary decision in the *Ideal Supply* case, so the case is not over. This decision does not mean that *Ideal Supply Co.* has already won or that it has even proved that Lien Law Trust Funds were "diverted." However, it does mean that *Ideal Supply Co.* will be allowed to try and prove its case — including against the general contractor's individual officers. That alone is important because it suggests that the Court in New York City recognizes and approves of an expanded view of the Lien Law's protections for subcontractors who are not getting paid. It also means that the individual officers of general contractors who don't properly pay their subcontractors may have to defend themselves (not just their companies) in court.