



## LEGAL UPDATES

# Remembering The Notice of Non-Responsibility

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For so long, a hot economy and commercial leasing market meant that concerns over unpaid tenant improvement construction and related mechanic's liens were closeted like winter clothes in the heat of the summer. In the current "pandemiconomy," many commercial businesses are planning their return to the office. Some tenants need to complete build-outs, while others must reconfigure their space to address the new requirement of doing business under state and local Shelter in Place orders. As a result, tenant improvement construction projects are on the rise. Unfortunately, confidence in the ability to fund those projects has softened. Landlords must be cognizant of mechanic's lien claims by contractors and suppliers who are not paid for their labor, services and/or materials on a tenant's project.

The mechanic's lien is the vehicle, created by California law, for general contractors, subcontractors, material suppliers and labor forces to receive payment from a property owner when the tenant who hired them fails to pay for their work. Payment for these professionals is so important that California's Constitution protects their right to be paid. Moreover, California courts have ruled that contract provisions which seek to waive or impair mechanic's lien rights are unenforceable.

To assert valid mechanic's lien claims, contractors and suppliers, generally, must serve a 20-day preliminary notice in the form prescribed by statute. This document puts the owner and tenant on notice that the party giving notice will provide labor and/or materials to the project, and that they will have the right to record a mechanic's lien if they are not paid.

Given the substantial rights afforded to ensure contractors and suppliers are paid for their work, it is essential for landlords to understand their exposure to liability when a tenant fails to pay for its construction work. At the same time, landlords must understand available protections from this liability. While the landlord has several tools to avoid being subject to mechanic's liens, each must be utilized in a timely and proper manner.

Landlords seeking to avoid mechanic's lien claims can post on the job site and record a "notice of non-responsibility." These notices must be posted and

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recorded within 10 days of the landlord's knowledge of the construction activity. A landlord who timely records and posts this notice, subject to the exceptions below, shields/protects its interest in the property from the mechanic's liens of contractors and suppliers working on a tenant improvement project. However, the notice is not a bulletproof shield for the landlord. If the landlord "participates" in the improvements, e.g., via lease provisions that require the tenant to make the improvements at issue, the notice will have no effect. In addition, some conduct by the landlord, such as review and approval of plans and specifications, approving the contractors and substantially benefiting from the improvements also may prevent the notice of non-responsibility from having any effect. Regardless of the potential limitations, as a general rule, landlords are well advised to timely post and record the notice of non-responsibility instead of presuming it will be later deemed ineffective.

Even if the notice of non-responsibility is ineffective, the landlord has other protections from mechanic's lien claims. For example, landlords should require that all contractors and suppliers (particularly those who have served preliminary 20 day notices) sign conditional and unconditional lien waivers in exchange for payment. That way, the landlord and tenant can be assured that all parties with potential lien rights are paid and relinquish their lien rights as they receive payment. Additionally, landlords can include lease provisions requiring deposits/additional deposits to satisfy potential mechanic's lien claims as part of tenant improvement or alterations authorizations. Leases also can include language, as they typically do, requiring that the tenant immediately remove mechanic's liens by paying the claim or obtaining a mechanic's lien release bond. Additional lease language requiring the tenant to defend and indemnify the landlord from mechanic's lien foreclosure lawsuits also would be helpful. While these are powerful tools, the landlord must be proactive and have them in place before any tenant improvement work begins.

As is evident from the discussion above, mechanic's lien claims on tenant improvement projects can be complicated and challenging to address. Should you have any specific questions regarding these issues, please contact any member of our Construction Practice team.