

**BALANCING COMPETING INTERESTS**

**HOW A CONTRACTOR GETS PAID FOR TENANT IMPROVEMENTS**

**VS.**

**HOW AN OWNER AVOIDS GETTING STUCK WHEN ITS TENANT DOES NOT  
PAY ITS CONTRACTOR FOR IMPROVING ITS SPACE**

**INTERNATIONAL COUNCIL OF SHOPPING CENTERS**

**LAW CONFERENCE**

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**SCOTTSDALE, AZ**

**STUART H. SOBEL**

**SIEGFRIED, RIVERA, LERNER,**

**DE LA TORRE & SOBEL, P.A.**

**201 ALHAMBRA CIRCLE**

**ELEVENTH FLOOR**

**CORAL GABLES, FLORIDA**

**33134-5108**

**305-442-3334**

**Fax 305-443-3292**

**[Ssobel@siegfriedlaw.com](mailto:Ssobel@siegfriedlaw.com)**

**<http://www.siegfriedlaw.com/articles/sobel/default.htm>**

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**INTRODUCTION**

Generally, a contractor's lien for improvement of a property attaches only to the interest of the person contracting for the improvement. Typically, the tenant owns only a leasehold interest in the property, which is extinguished at the termination of the

lease, by which the interest was created. Thus, special problems for both an unpaid contractor and a lessor wishing to avoid liens, may arise when a tenant contracts to improve a leasehold space.

A contractor performing an improvement to a tenant space may, under certain circumstances, be entitled to a lien for its unpaid balance, against the fee interest of the center where the space is located. Although the overwhelming majority of states allow a lien to reach only the interest of the party hiring the contractor, under various circumstances, acts or omissions of the owner of the center may render the fee interest of the entire center subject to the lien of the contractor improving a tenant space.

California, for example, exempts an owner's property from the lien of one improving it at the behest of a tenant, so long as the owner is unaware of the improvement. However, once the owner becomes aware that a tenant or other interested party has contracted for improvements to the owner's property, the contractor's lien will attach to the fee interest, unless the owner, within ten days of acquiring knowledge, posts and records a "Certificate of Nonresponsibility." See California Civil Code, §§3094, 3128 and 3129.

Florida, on the other hand, does not subject the owner's fee to the lien of a contractor improving a leasehold unless the improvement was required under the terms of the lease. Even under those circumstances, the lessor may prohibit the attachment of liens for such improvements in the lease and, by recording a short form of the lease provision, relegate the contractor's lien to the leasehold interest only. See §713.10, Florida Statutes.

A good source for pertinent cases, collected by type of property improved, appears at 46 A.L.R. 5<sup>th</sup> 1 (1997).

The purpose of our visit today is to discuss the various issues that arise, and suggest ways to analyze and resolve them. An outline of the issues follows. The materials conclude with a collection of statutes and case references.

## BALANCING COMPETING INTERESTS

I. General rule--lien attaches only to interest of party contracting for improvement

A. Exceptions

1. knowledge of fee owner

a) in some states, ie. California, knowledge alone is sufficient to render fee subject to lien

1) in such states, owner must affirmatively act to avoid attachment of lien, ie, record/post notice of

nonresponsibility

b) in other states, ie. Florida, owner's mere knowledge will not subject fee to lien

2. pith of lease

a) what's a "pith", anyway

1) improvements required by lease

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2) improvements contemplated, but not required by lease

b) how to prove "pith"

1) lease negotiations

2) cost of improvement reflected in rent

3. affirmative actions by owner subjecting

fee interest to lien

a) consent

1) more than merely allowing improvement to occur

b) estoppel

B. Making sure the Owner does not subject the fee to the contractor's lien

1. lease provisions prohibiting liens

2. recording short form of lease

3. conflicts---prohibiting liens and requiring that they be bonded (anticipating them)

II. Alternatives for the Contractor When Liens Won't Fly

A. Personal guarantees of tenant's principals

B. Irrevocable letters of credit

C. Alternative security (mortgages)

D. How bad do you want this job?

III. When the Contractor is Limited to Lien on Leasehold

A. Form of lien

B. Requisites of Notices to "Owner"

C. Lis Pendens

D. Foreclosure and sale nuances

1. arbitration of contract dispute between contractor and lessee, without joining lessor

2. enforcement of arbitration award

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re-litigating against lessor

3. nature of leasehold interest foreclosed

term, defenses

E. Purchase of leasehold interest

1. communication with lessor

F. What if the leasehold is terminated