Mississippi Construction Lien, Bond, Stop Notice, Open Account and Contractor Prompt Payment Claims

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I. CONTRACTOR AND SUBCONTRACTOR PAYMENT REMEDIES

MISSISSIPPI PROMPT PAYMENT LAWS AND STOPPING WORK

A. Prime Contractors' Statutory Claims for Interest

Mississippi has prompt payment laws applicable to both an owner's obligation to promptly pay the prime contractor on a private or public job, and, as noted below, applicable as well to the prime's obligations to promptly pay his subs.

The statutes dealing with owners state that if the owner fails to make a timely partial, progress or interim payment to the prime contractor (within 30 calendar days of the due date on a private job, within 45 days on a public job) the prime contractor is entitled to collect from the owner interest from the due dates at the rate of one percent (1%) per month until paid (12% APR). § 87-7-3(a) [private jobs]; § 31-5-25(a) [public jobs] *Miss. Code Ann.* Similarly, if the owner fails to make a final payment to the prime contractor, the prime contractor may claim statutory interest of one percent (1%) per month until paid (12% APR). § 87-7-3 [private jobs]; § 31-5-25 [public jobs] *Miss. Code Ann.* Note that the 12% APR interest allowed to prime contractors is a higher rate of interest than the general legal rate of interest of 8% provided for contract generally under § 75-17-1(1).

When, though, is a final payment considered due to the prime contractor so that the 1% per month interest charges can begin? In the case of private jobs, the interest statue provides that final payment is due upon the earliest of any of the following, provided that any surety for the contractor has first given consent in writing to the final payment:

(i) Completion of the project, or substantial completion in accordance with the terms of the contract;

(ii) Upon the owner's beneficial use or occupation of the premises (unless the owner's occupation continued during a renovation); or

(iii) When the project architect or engineer certifies the project is complete, **"whichever event shall first occur."** § 87-7-3(b) [private jobs] *Miss. Code Ann.*

In the case of public jobs, the events triggering the due date of a final payment are the same as the three listed above for private jobs, except that in addition a certification of completion by the State or municipal authority can also trigger the final payment due date if that is the earliest of the listed events to occur. § 31-5-25(a) [public jobs] *Miss. Code Ann.*

B. SubContractors' and Suppliers' Penalty Claims for Late Payment

Prime contractors, on both private and public jobs, can become liable to pay a penalty in Mississippi for late payment to their subs and suppliers. There is one exception to this rule: the late payment law does not apply on private jobs to payment of subs and suppliers for construction of single-family residences. §§ 87-7-5 [private jobs]; 31-5-27 [public jobs] *Miss. Code Ann.*

A payment to a prime's sub or supplier is considered late by statute if the payment is not made within fifteen (15) days of receipt of payment from the owner. If the prime receives only partial payment from the owner, the sub or materialman must still be paid, but *pro rata* for their part due from the owner's payment. The penalty for the prime's late payment sounds astoundingly large (1/2 of 1% *per day* from the time of the owner's

payment to the prime), but is capped at 15% of the outstanding balance due to the sub or supplier. §§ 87-7-5 [private jobs]; 31-5-27 [public jobs] *Miss. Code Ann.* Since the statute speaks in terms of the interest as a penalty, presumably the statutory penalty is in addition to any contractual claims for interest created by the late payment.

C. Right to Stop Work for Nonpayment under AIA Contracts

1. Prime Contractors' Right to Stop Work

An owner's failure to timely pay the prime contractor can lead to the prime's stopping work and, if nonpayment continues, to termination of the contract for breach under AIA contract provisions. However, the contractor must be careful to observe the notice requirements. The AIA General Conditions for Construction provide that the prime contractor can stop work until payment is made:

- If the architect does not issue a Certificate of Payment within 7 days of the Application for Payment through no fault of the contractor; or
- if the owner does not pay the contractor within 7 days of a due date under the contract; and
- the contractor gives 7 days additional written notice to the owner and architect of that the work will stop if payment is not made.

Article 9.7 (A201-2007).

2. Prime Contractors' Right to Terminate the AIA Contract

The prime contractor, after stopping work for nonpayment, can then terminate the contract and sue for payment and damages:

- If the work is stopped for nonpayment for 30 consecutive days through no

fault of the contractor or of a subcontractor or of a sub-sub contractor; and

- the contractor provides 7 additional days written notice of termination.

Articles 14.1.1, 14.1.3 (A201-2007).

3. Subcontractor's Right to Stop Work or Terminate AIA Contract

The subcontractor can stop work until payment is made after the contractor's failure to make timely payment for 7 days as called for by the agreement, and after provision of 7 days' additional written notice by the subcontractor to the contractor that work will stop until payment of the amount owed is received. Article 4.7 (A401-2007).

II. MISSISSIPPI PAYMENT BOND LAW CLAIMS:

A. PRIVATE CONSTRUCTION JOB PAYMENT BONDS

1. Bonding Around A Stop Notice: A General Contractor's Provision of a Payment Bond to an Owner Dissolves A Sub's Stop Notice Rights: Mississippi law does not require contractors on private projects to furnish performance or payment bonds. **However, the first inquiry one should make on a private job is whether there is a payment bond since payment bond rights, where they exist, are in lieu of statutory lien or stop notice rights.** In other words, a subcontractor's stop notices become legally ineffective where the general contractor provides to the owner a payment bond protecting subcontractors and suppliers. As a result, a general contractor, faced with a sub's stop notice claim that could delay the owner's closing with its lender (preventing final payment to the general, and by the general to all the other subs), can get rid of the sub's stop notice by "bonding around the lien". The general contractor can simply provide to

the owner a payment bond obtained from a surety/insurance company that will cover the amount of the stop notice claim. The contractor's provision of a payment bond dissolves the stop notice rights of the sub as a matter of law. *Dickson v. U.S.F.&G. Co.*, 117 So. 245, 248 (Miss. 1928):

> If the contractor does not give the bond provided by the statute, laborers and materialmen have an equity...in the funds due the contractor by the owner of the building. But where a bond is given as provided by the statute, such funds are released from such equity or trust in favor of materialmen and laborers and go into the hands of the contractor untrammeled. The purpose of the bond section of the statute was to provide for the protection of materialmen and laborers, the bond being in lieu of their equity in the funds arising out of the building contract.".

Also, the prime contractor can achieve the same protection from stop notices at the start of the project by providing the owner a payment bond. *Ewin Engineering Corp. v. Deposit Guaranty Bank and Trust*, 216 Miss. 410, 62 So. 2d 572, 574 (1953), citing *Dickson v. U.S.F.&G. Co.*, 117 So. 245, 248 (Miss. 1928). Accord., *Redd v. L & A Contracting Co.*, 151 So. 2d 205, 207, 246 Miss. 548 (Miss. 1963). See also, *Jesco, Inc. v. Jeffreys Steel Co.*, Inc., 571 F. Supp. 801 (N.D. Miss. 1983) ("Under *Dickson v. USF & G*...where the contractor has given bond, as here...*no* lien, either at law or equity, may be asserted against monies due a contractor under a construction contract or purchase order." Emphasis original.).

One hastens to add that if the prime contractor posts a performance bond instead of a payment bond, Mississippi law automatically writes into the performance bond a payment provision protecting subcontractors, laborers and materialmen of the general contractor at § 85-7-185. Therefore, the private bond statute requires protection of tier 1

contractors and materialmen below the bonded contractor but, unlike the Little Miller Act which protects also the next tier upon their giving timely notice of claims, the private bond statute does not require that the bond protect tier 2 sub-subs and materialmen of subs.

2. Motion to Expunge Stop Notice and Lis Pendens Filing Given the Presence of a Payment Bond: What, though, if the subcontractor stubbornly refuses to remove a stop notice and accompanying lis pendens notice even in the face of the contractor's providing him a copy of a bond? In that case the contractor, preferably joined by the owner (to ensure standing), should apply to the County or Chancery Court to have the lis pendens notice immediately enjoined and expunged under the authority of § 85-7-201 *Miss. Code Ann.* That section, the false notice statute, allows application to the County or Chancery Court on two day's notice to expunge the inappropriate lis pendens filing from the land records, to enjoin the further filing of such notices, and for an award to the injured party a penalty in the full amount of the wrongful filing if filed "falsely and knowingly."

The Mississippi Court of Appeals has noted a chancellor's right to examine whether a recorded materialmen's lien is void and of no effect, and whether the lien should be enjoined, in *Cummings v. Davis*, 751 So. 2d 1055, 1058 (Miss. App. 1999).

Although a more cumbersome claim, it also possible for an owner to assert an action for slander of title where the false filing of a lien is malicious. *Walley v. Hunt*, 54 So.2d 393, 212 Miss. 294 (Miss. 1951).

3. Remote Materialmen: The Mississippi Supreme Court has held that the

private bond statute for private projects (§ 85-7-185) requires that the bond provide protection only to persons furnishing labor or materials to the contractor who provided the bond to the owner; it does not protect remote materialmen having no direct contract with the contractor who gave the bond. *United States Fidelity & Guaranty Co. v. Maryland Casualty Co.*, 191 Miss. 103, 199 So. 278, 282 (1940); *Alabama Marble Co. v. United States Fidelity & Guaranty*, 146 Miss. 414, 111 So. 573, 574 (1927) . For example, the Court held in the *Alabama Marble Co.* case that a bond provided by the prime contractor for the construction of the Lamar Life Building in Jackson did not cover the claim of a provider of marble to a subcontractor on the job. *Id.* The law, though, does not preclude the general contractor's bond from affording greater protection to remote materialmen than the statute requires, so one must read the bond to learn if its scope is broader than the statute requires. Further, if the prime contractor requires a subcontractor to provide a bond, the private bond statute then requires that materialman who have dealt with the bonded subcontractor be protected under the bond.

4. Equipment: Finding coverage under a private bond for equipment rentals or repairs can be problematic unless the bond specifically covers "equipment" as well as "labor and materials". However, modern bond forms do usually cover equipment as well as "labor and materials". In the case of *Western Casualty & Surety Company v. Stribling Brothers Machinery Company*, 162 Miss. 581, 139 So. 838, 840-841 (1962), the Mississippi Supreme Court strictly interpreted the terms "labor and materials" under the private bond statute to hold that the surety was not liable for the claims of intervenors for unpaid equipment rentals and transportation costs of equipment. The Court did recognize

coverage claims for gas and oil and necessary repairs to the equipment used in the work. *Id.* The Court in a subsequent case, based on the terms of the indemnity bond in that action, broadly disallowed bond claims for equipment rentals, transportation, repairs and parts, stating that "all persons furnishing labor or material under said contract" did not include lessors of equipment. *Great American Insurance Company v. Busby*, 247 Miss. 39, 150 So. 2d 131, 135, 137 (1963). See also, *Carruth v. Standard Accident Insurance Co.*, 329 F. 2d 690, 692-93 (5th Cir. 1964), reaching the same conclusion. However, the Mississippi Court did find coverage for equipment repairs (as well as fuel and oil consumed) in *Seaboard Surety Co. v. Bosarge,* 226 Miss. 482, 84 So. 2d 517, 519 (1956), where the private performance bond specifically covered the contractor's obligation to provide "equipment", as well as labor, supervision and tools, to complete a housing project. The *Bosarge* and *Busby* cases are compared in *Coatings Manufacturers, Inc. v. DPI, Inc.*, 926 F. 2d 474, 477 (5th Cir. 1991). And again, the bond at issue by its terms may very well explicitly cover equipment rentals.

5. Commencement of Suit and Joinder In Suit on Bond: The Mississippi private project bond statutes provide that if the prime contractor provides only a Performance Bond to guarantee his performance to the Owner (the bond Obligee), then in that case the Performance Bond by statute also acts as payment bond securing payment to the subcontractors providing labor or materials to the contractor providing the bond. § 85-7-185. The statute also provides that if a claimant brings suit on the private project bond, other persons furnishing labor or materials under the contract may intervene in the action to have their rights determined under the bond. However, unlike the public project

bond requirements under the Little Miller Act, the private bond statute does not require that the bond be sufficient to cover the full amount of the prime's or subcontractor's contract. Therefore, the statute provides that the owner or prime to whom a Performance Bond was given (the Obligee) has the first priority in the bond proceeds for the satisfaction of his claim for damages ahead of subcontractors. § 85-7-193. Remaining payment claimants on the Performance Bond are left to share in the available bond proceeds on a pro rata basis after the owner/obligee's claims are satisfied. §85-7-193. If the prime contractor provided a payment bond in addition to a performance bond, presumably the unpaid subcontractor-claimant would look first to the payment bond and its terms to make a claim.

If the contractor on a private project provided only a performance bond (rather than a performance bond accompanied by a payment bond), only the owner or the prime to whom the bond was given (the Obligee) on a private project can bring suit within the first six months following either notice of abandonment or completion and final settlement of the contract. Thereafter if the bond obligee has not brought suit, and if the bond has not been exhausted by the Obligee, any third party supplying labor or materials can initiate suit on the performance bond for payment. §85-7-187.

Once suit is brought by a party eligible to relief under the performance bond, any other party entitled to bond relief may intervene in the action and be made a party to the suit since by statute only one action can be brought on the performance bond for performance and payment claims. §85-7-191. Similarly, if a private project payment bond was provided, Mississippi law provides that there can be only one action on the

payment bond into which other payment claimants may intervene. § 85-7-191. However, while §85-7-191 states there can be only one action on the private project bond, the Supreme Court has refused to uphold the one action rule on constitutional grounds against a claimant who had no notice of the suit. *American Fidelity Fire Insurance Company v. Athens Stove Works, Inc*., 481 So. 2d 292, 295 (Miss. 1985).

6. Statute of Limitations for Payment Claims on Private Jobs: The Mississippi legislature reworked the private job bond limitations statute (§85-7-189) in 1995 to more nearly match the limitations periods contained in the public bond limitations statute (§31-5-53). The statute of limitations for suit on a private job payment bond (§85-7-189(2)) remains a relatively short period of one (1) year. However, whereas before suit on a payment bond could not be commenced before a notice of abandonment or the complete performance and final settlement of the general contractor's contract, now the limitations period requires that suit **"be commenced within one (1) year after the day on which the last of labor was performed or material was supplied by the person bringing the action and not later."** (Emphasis). Thus, for a subcontractor suing on a payment bond the limitations period runs from its own last supply of labor or materials to the job. The one year does not run, say, from the general contractor's completion of the entire project, or from the owner's occupancy. The legislature made the same change a year earlier in 2004 to the payment bond section of the public bond statute, running the limitations period in from the last supply of materials or labor by the party bringing the action.

By contrast, the limitations period under the statute on an owner's suit on a

performance bond (§85-7-189(1)) still runs from final completion or occupancy. Also compare the one-year limitations period on a payment bond (running from the last supply of labor or materials) with the limitations period on a statutory lien which runs one-year after the date the money claimed, "*became due and payable, and not after*". (Emphasis added). § 85-7-141. The limitations on a lien therefore runs from the date the last invoice became due, as opposed to a payment bond claim which runs from the last supply of labor or materials.

It may be of some note that there is a Fifth Circuit Court of Appeals case, applying Mississippi law, that has held that where the bonding company takes over a defaulting contractor's contract and supplies a substitute contractor whose work turns out to be defective, the bonding company can subject itself to the normal six year statute of repose for deficiencies (§ 15-1-41), rather than the one year bond statute of limitations (§ 85-7-189), if it elected to serve as the contractor. *Cooper Industries, Inc. v. Tarmac Roofing Systems*, Inc., 276 F. 3rd 704, 712-713 (C.A. (Miss.) 2002). However, the bonding company would not have a liability for the substitute contractor's deficiencies if it chose to re-bid the contract, supplying a new contract to the owner, rather than simply appointing the substitute contractor to complete the contract in default. *Id.* The one year bond statute of limitations applies only to laborers and materialmen to the job, and owners who themselves have supplied labor or materials. *Id.*, 276 F. 3d at 714.

7. Priorities in Recovery; Attorney's Fees: As noted previously, where only a payment bond is provided, if the recovery on the bond turns out to be inadequate to satisfy all parties to the action, the bond obligee is to be satisfied first as to all claims

and damages before judgment is given for remaining parties on a pro rata basis. § 85-7-193; § 85-7-185. Section 85-7-193 also authorizes the award of reasonable attorneys' fees in an action on a private job performance bond in an amount to be set by the judge, but the attorneys fees must be authorized in the bond contract or by separate statute. *Sentinel Industrial Contracting Corp. v. Kimmins Industrial Service Corp.,* 743 So.2d 954, 971 (Miss.1999).

8. **Interest:** Prime contractors and subcontractors on private projects who do not received timely payment will be able to charge interest/penalty as permitted by the Mississippi Prompt Payment Act. See the descriptions of § 87-7-3 and § 87-7-5 in Section I above.

9. **Bonding Under Alter Ego Entity:** In *Beco Inc. v. American Fidelity Fire Ins. Co.,* 370 So.2d 1343,1346 (Miss.1979), the Supreme Court found that a prime contractor and his surety could not evade responsibility where a private bond was with Bob Wolfe Electric Co., a d/b/a name for Bob Wolfe, individually, but the assertion was made the work was done by his family's corporation, Wolfe Electric Company, Inc. Under the circumstances the Court found that the individual and corporate identities were mere alter egos and "the fiction of separate corporate identity" would be disregarded.

B. MISSISSIPPI PUBLIC JOB PAYMENT BONDS

1. **Bid Bonds:** A bid bond provides relief to the owner in the event the contractor whose bid has been accepted refuses to proceed with signing the contract and construction (a performance bond, by contrast, covers construction performance). Public authorities in Mississippi in their discretion may require contractors to post bid bonds

with bids on public construction contracts. Cities, for example, may impose the requirement of a bid bond pursuant to § 21-17-5 *Miss. Code Ann.* (1972), which gives cities control over management of their finances. AG Opinion, 1990 WL 547943; AG Opinion, 1990 WL 548140. Generally, there is no statutory requirement that the public authority require a bid bond from contractors. However, the private financing and construction of dorm facilities for the Institutions of Higher Learning requires that bids be accompanied by a check or "bid-bond payable to said board in a sum not less than five percent of the gross construction cost of the facility to be constructed as estimated by said board.... The said bid security...shall be forfeited if the successful bidder fails to enter into the lease contract and commence construction within the time limitation set forth in the notice." § 37-101-43 *Miss Code Ann*. Further, where the public authority chooses to require a bid bond, it may accept cash or its equivalent, including a personal check or irrevocable letter of credit, in lieu of the bid bond. AG Opinion, 1996 WL 508568 at p. 3; AG Opinion, 1995 WL 526173.

2. Performance and Payment Bonds Required For Public works – The Mississippi Little Miller Act:

The Mississippi Legislature in 1980 enacted the Little Miller Act which follows closely the model of the Federal Miller Act (40 U.S.C. §§ 3131-33). Mississippi's Little Miller Act appears at §§ 31-5-51 to -57 *Miss. Code Ann.* (Supp.).

Mississippi requires general contractors on public projects to provide bonds covering performance and payment because a claimant could have no lien rights against the property of the state. The state, as sovereign, is not subject to private liens or stop notices. *Key Constructors, Inc. v. H&M Gas Company*, 537 So. 2d 1318, 1321 (Miss.

1989). Thus, §31-5-51(1)-(2) provide that for projects exceeding a cost of $25,000, anyone entering a contract with the state, any county, city or other public authority must furnish a **performance bond** "in favor of or for the protection of such public body, as owner" and "in an amount not less than the amount of the contract". The statute further requires that the contractor provide a **payment bond** "in an amount not less than the amount of the contract". *Id.*

(i) Payment Bond Claimants Covered: Mississippi Little Miller Act states:

> (2) **Every Person who has furnished labor or material** used in the prosecution of the work provided for in such contract, in respect of which a **payment bond** is furnished **and who has not been paid in full therefor** before the expiration of a period of ninety (90) days after the date on which the last of the labor was performed by him or the last of the materials was furnished by him and for which such claim is made…shall have the right to sue on such payment bond for the amount, or the balance thereof that is due and payable, but unpaid at the time of institution of such suit and to prosecute such action to final execution and judgment.

(Emphasis added). § 31-5-51 (2) Miss. Code Ann.

Justice Jimmy Robertson in *Key Constructors, Inc.* noted especially that, "Section 31-5-51(3), appears to have been taken verbatim from that portion of the Miller Act addressing the rights of persons furnishing labor or material to subcontractors engaged in public works projects." *Id.* That provision of the Mississippi Little Miller Act provides:

> (3) **Any person having direct contractual relationship with a subcontractor** but no contractual relationship express or implied with the contractor furnishing said payment bond shall have a right of action upon the said payment bond **upon giving written notice to said contractor within ninety (90) days from the date on which such person did or performed the last of the**

> **labor or furnished or supplied the last of the material for which such claim is made**,…. Such notice shall be given in writing by the claimant **to the contractor or surety…."**

(Emphasis added). § 31-5-51 (3) Miss. Code Ann.

The Little Miller Act at Subsection (4) then goes on to provide that the "only persons" protected by the payment bond required under the Act are: (a) first tier subcontractors and material suppliers below the prime contractor; (b) second tier sub-subcontractors and material suppliers below subcontractors who give notice within 90 days of their last addition of labor or materials (see sec. v below); and (c) laborers who have performed work on the project site. § 31-5-51(4). The Little Miller Act leaves out of its requirements protection for materialmen of materialmen (see section ii below), and for subs below the sub-sub level, although the bond can be written more expansively since the parties are always free to contract to provide greater protection.

Still, though, the Little Miller Act's protections are fairly broad, certainly more so than the Mississippi lien and stop notice statutory schemes they are in lieu of. The Mississippi Court of Appeals in a 2004 case, citing *Key Constructors, Inc.,* stated:

> Since Mississippi's Little Miller Act is modeled after the Federal Miller Act, 40 U.S.C.A. §§ 270a-d (redesignated as 40 U.S.C. §§ 3131-33), the Mississippi Supreme Court has found federal court decisions interpreting the Federal Miller Act instructive and persuasive when interpreting Mississippi's Little Miller Act. *Key Constructors, Inc. v. H & M Gas,* 537 So.2d 1318, 1321 (Miss.1989).

Younge Mechanical v. Max Foote Construction Co., 869 So.2d 1079, 1082 Ct.App.2004). Therefore the larger body of law available concerning the Federal Miller Act may be consulted in the analysis of Mississippi Little Miller Act cases. For example, a Federal

Miller Act case discussing the reach of compensation claims a supplier of labor can make would be relevant. In *United States v. Carter*, 353 U.S.210, 77 S.Ct. 793, 1 L.Ed.2d 776 (U.S. 1957), a case construing the analogous Miller Act, the U.S. Supreme Court noted:

> The Act, however, does not limit recovery on the statutory bond to 'wages.' The parties have stipulated that contributions to the [employee health and welfare trust] fund were part of the consideration Carter agreed to pay for the services of laborers on his construction jobs. The unpaid contributions were a part of the compensation for the work to be done by Carter's employees. The relation of the contributions to the work done is emphasized by the fact that their amount was measured by the exact number of hours each employee performed services for Carter. Not until the required contributions have been made will Carter's employees have been 'paid in full' for their labor in accordance with the collective-bargaining agreements."
>
> ….In fact, the surety's obligations extended to some persons who had no contractual relationship with Carter. For example, persons who contributed labor and material to Carter's subcontractors were entitled to the Act's protection. [Citations omitted]. As long as Carter's obligations relating to compensation for labor have not been satisfied, his employees will not have been 'paid in full' and the Miller Act will not have served its purpose.

353 U.S. at 217-218, 77 S.Ct. at 797.

(ii) Materialmen: An issue can thus arise whether a materialman is a supplier to a subcontractor within the protection of the Little Miller Act bond or merely a material supplier to another materialman outside the protection of the bond. In *U.S. for Use and Benefit of Clark v. Lloyd T. Moon*, 698 F.Supp. 665, 668 (S.D.Miss.1988) for example, the District Court determined that the plaintiff fabricator of steel joists and decking had supplied his products to another steel material supplier of the prime contractor, not to a "subcontractor" of the prime contractor for the Project, thus rendering

the plaintiff materialman a third tier "materialman to a materialman" outside the scope of the protection of the bond. Among the factors considered was indicating the middleman the materialman supplied to was just another materialman was whether the entity "did no on-site work, either installing its products or supervising their installation", gave no performance bond to the prime, did not receive progress payments, included sales tax in its price, and supplied prefabricated, standard items rather than a complex, integrated system. 698 F.Supp. at 667. Custom manufacturing alone is not determinative. *Id.*

(iii) Equipment: Mississippi has followed the traditional rule that only materials or the portion of equipment (i.e. rentals) actually used or consumed in the construction of the project are reimbursable under a public works bond. In *Houston General Insurance Company v. Maples*, 375 So. 2d 1012, 1015-1016 (Miss. 1979), the Court upheld the liability of the bond surety to reimburse a fuel supplier, "since the fuel was necessary for the equipment's operation which was essential to the construction." However, the Court held that a supplier of tires for heavy equipment could not seek reimbursement for the entire price of tires. *Id*. at 1016. The Court remanded for further testimony on portion of the tires' useful life consumed on the project. *Id*. The Court did uphold a claim under the bond for heavy equipment rental payments, noting the equipment was essential to the project, "just as laborers would have been had the equipment not been used." *Id* at 1016. The key in is proof that the specific materials were intended for the use or consumption in the construction of the public project. See also an analogous Miller Act case, *U.S. for and on Behalf of Mississippi Road Supply Co. v. H.R. Morgan, Inc.,* 542 F.2d 262, 267 (5th Cir.1976) ("The amount of such [equipment] rents…represent the approximate value

of the equipment's useful life which is dedicated to construction of the project.").

(iv) Diversion of Materials: However, the Mississippi Supreme Court, in an opinion by Justice Jimmy Robertson, has recognized also that a supplier of material to a contractor may have no control over the contractor's diversion of materials from the intended public project to another project not covered by the bond. In *Key Constructors, Inc. v. H&M Gas Company*, 537 So. 2d 1318, 1321 (Miss. 1989), a supplier of fuel to a subcontractor brought suit under the Little Miller Act on the bond. The prime contractor and obligee on the bond attempted to defend against the claim by stating that the subcontractor had diverted the fuel to other unbonded projects that he was working on. The Court held that the claim of diversion was immaterial to the action on the debt to the materialman, citing opinions noting that a materialman's claims should not be denied where the materialman supplied materials in good faith to a subcontractor for the prosecution of the contemplated public work. *Id*. at 1323-24.

The Supreme Court in *Key Constructors* also held that the prime contractor could not defend against bond liability to the materialman of the subcontractor by asserting that he also had a claim against the subcontractor and was owed a set off. The Court stated: "The right of a materialman to make a demand on the contractor and/or his surety was legislatively created so that the supplier could distance itself from contractor/subcontractor disputes, thus assuring its prompt payment." *Id*. at 1324.

(v) Notice Requirement: The Little Miller Act imposes no notice requirement on tier one subcontractors, laborers or materialmen having a direct contractual relationship with the prime contractor as a condition precedent to suit on the bond.

However, second tier sub-subcontractors and materialmen of subs not having a direct contractual relationship with the prime can not proceed against a surety bond under the Little Miller Act without first meeting the Act's rather difficult 90 day notice requirement. § 31-5-51(3). The Act requires sub-subs and materialmen of subs to the general contractor to give written notice of the claim to the prime contractor within 90 days of the claimant's last furnishing of labor or material for which claim is made. The notice must state "with substantial accuracy" the specific amount claimed, and the specific subcontractor to whom the material was furnished or for whom the labor was done, and who has not made payment. The notice may be delivered in person or by prepaid certified mail, return receipt requested. In addition, the claimant may give notice to the surety, but the critical notice is the notice to be given to the general contractor. See *United States for the Use and Benefit of Jinks Lumber Company, Inc. v. Federal Ins. Co.,* 452 F.2d 485, 487 (5th Cir. 1971) ("The purpose of the notice requirement of the Miller Act is to alert a general contractor that payment will be expected directly from him, rather than from the subcontractor with whom the materialman dealt directly. Without a statutory period, materialmen might delay claims unreasonably, thus frustrating the general contractor's need to be able to commit his funds to other activities."). See also *Younge Mechanical, Inc. v. Max Foote Construction Co., Inc.,* 869 So.2d 1079, 1082 (Miss.Ct.App.2004) which cites the *Jinks* case as authority in its analysis of the Mississippi Little Miller Act.

Nonetheless, a Mississippi federal District Court stated it was willing to overlook the certified mail/return receipt requirement for mailing where, "the only failure

to comply with the statute was the failure to send notice by certified mail, and where there is no dispute but that actual notice was received by the proper party". *Brothers In Christ, Inc. v. American Fidelity Fire Insurance*, 692 F. Supp. 701, 703 (S.D. Miss. 1988).

Also, notice that the strict 90 day notice requirement may not be applicable if the subcontractor was required to give a separate payment bond. In that case, the subcontractor becomes the principal on the subcontractor bond, and the direct suppliers to the sub providing the subcontractor bond should be able to make claims on the subcontractor payment bond without having first sent a notice of nonpayment within 90 days of the last transaction. However, note further in that case that even though the General Contractor may have given a Little Miller Act bond, the subcontractor's bond is a private bond on a private subcontract (even on a public building), meaning the subcontractor bond's reach is governed by the Mississippi private bond statute (which limits relief to those supplying directly to the subcontractor providing the subcontractor bond, not further tiers down).

(vi) Commencement of Suit and Statute of Limitations: The Act provides that public project bond claimants within the protection of the Act who have remained unpaid for at least 90 days following their last furnishing of labor or materials for the public project "shall have the right to sue" on the payment bond. §31-5-51(2). Thus claimants must go unpaid at least 90 days from the due date to sue on the bond. The Legislature amended the Act in 2004 to create a statute of limitations for suit on a payment bond that runs from the same date that is from the last performance of labor or supply of material.

The Act now provides that, "[w]hen suit is instituted on a payment bond... it shall be commenced within one (1) year after the day on which the last of the labor was performed or material was supplied by the person bringing the action and not later." §31-5-53 (b).

Prior to July 2004 the one year for suit on a payment bond began from performance and final settlement of the contract. Further, the Mississippi Supreme Court had stated that, "a suit instituted on a payment or performance bond may not be commenced until notice of the final settlement or abandonment by the primary obligee has been published." *Stanton & Associates v. Bryant Construction Co.*, 464 So. 2d 499, 503 (Miss. 1985). However, the 2004 amendment appears to have changed all that as to payment bonds. Thus, while the right to sue for nonpayment does not accrue until the 91st day following the last supply of materials and labor for which the claim is made (§31-5-51(2)), it appears that the litigation on the bond can now commence prior to the performance and final settlement of the contract, and indeed must commence within one (1) year after the day on which, "the last of the labor was performed or material was supplied by the person bringing the action". §31-5-53 (b). [Also, compare the limitations period of the lien statute, § 85-7-141, which runs one year from the time the claim, "became due and payable", with the limitations of the public bond statute, running one year after, "the last of the labor was performed or material was supplied" by the claimant, §31-5-53 (b).].

The Little Miller Act does not follow the old rule that there can only be one suit brought on a payment bond, with all claimants required to intervene. The Act permits

multiple suits against the payment bond on state and local projects.

(vii) Venue: The Act provides that venue for a suit on a public performance or payment bond is available in the county in which the contract or part of the contract was performed, or in a county where service of process may be obtained on the prime contractor or surety on the bond. §31-5-53 (c).

(viii) Right to Examine The Bond: The prime contractor can not stonewall a potential claimant's request to examine the bond and its coverage provisions. The Little Miller Act provides that the prime contractor shall furnish a certified copy of the contract and bonds on the project upon request to, "[a]ny person supplying labor or materials for the prosecution of the work". §31-5-55.

(ix) Attorney's Fees: The Little Miller Act authorizes the judge to impose an award of reasonable attorney's fees against either the payment bond defendant or the bond claimant if either party proceeds in the action on the defense or claim unreasonably for mere delay, or without just cause, or in bad faith. § 31-5-57. The Mississippi Supreme Court recently upheld a substantial award of attorney's fees under § 31-5-57 together with the Mississippi Litigation Accountability Act (§ 11-55-5), in *Tupelo Redevelopment Agency v. Gray Corp., Inc.,* 2006-CA-00218-101807 at ¶71 (Miss.2007), for example, where the prime contractor delayed payment to the subcontractor on a public job "for no apparent reason", and the prime knew the sub "was entitled to the money, but withheld the money and has continued to do so." Also, the prime induced the sub "to believe that it would get its money when in fact [the prime contractor] Gray had already assigned the entire retainage to its bank." *Id.* at ¶71. Further, the prime in the

subsequent litigation requested payment from the public owner of the amount it owed to the sub but continued to refuse to pay the sub the amount it admitted owing the sub throughout the proceeding "'without substantial justification.'" Therefore the Supreme Court found that an award of attorney's fees under the statute was within the discretion of the lower court. *Id.* at ¶72.

In an earlier case, *Key Constructors*, Inc. v. H &M Gas Co., 537 So.2d 1318, 1324-25 (Miss.1989), the Mississippi Supreme Court recognized that § 31-5-57 allows the award of attorney's fees upon the provision of appropriate evidence (See *Tupelo Redevelopment Agency* at ¶71), but nonetheless threw out the portion of the judgment entered below awarding attorneys fees against the bond defendants where the plaintiff failed to show what a reasonable legal fee would be on the basis of the expert testimony of another attorney. The Court stated of attorney's fees that one, "may not merely pull a figure out of the thin air." *Key Constructors, Inc. v. H & M Gas Company*, 537 So. 2d at 1325. One should check first, of course, to see if there is an attorney's fees provision in the construction contract that one can cite in addition to the statute.

(x) Interest: Prejudgment interest is awardable on liquidated, fixed amounts sought under the Little Miller Act as in other cases since the bond is to insure "prompt payment". In addition, §31-5-27 provides that if a prime contractor on a public construction contract without reasonable cause fails to make payment to his subcontractors and material suppliers within 15 days of his receipt of payment under the contract with the public agency, an interest penalty shall accrue on the principal due at the rate of ½ of 1% per day of the delinquency, not to exceed 15% of the balance due.

See *Stanton & Associates v. Bryant Construction Co.*, 464 So. 2d 499, 502 (Miss. 1985). However, if the prime contractor terminates his contract with a supplier, even wrongfully, by breaching it, the contract is at an end, and the statutory penalty does apply because it applies only to payment for work that is ongoing. *G.B. 'Boots' Smith Corp. v. Cobb,* 2003 WL 22455653 (Miss.2003) ("When Smith [prime] breached the contract, the contract was terminated, and the Cobbs [materials supplier] were no longer entitled to the benefits under the Contract. ...Therefore, after the breach the Cobbs were no longer material suppliers under the public construction contract, and § 31-5-27 no longer applied to them.").

(xi) Subcontractor Bonds: If the prime requires the sub to put up a bond, the sub's bond falls under the private bond statutes rather than the procedures of the Little Miller Act. *U.S.F.&G. v. Dedeaux*, 152 So. 274 (Miss. 1934).

(xii) Failure to Require Bond: If a Board of Supervisors fails to require a bond for a public project, the Board members are not individually liable for their negligence. *Pidgeon Thomas Iron Co. v. Leflore County*, 135 Miss. 155, 99 So. 677 (Miss. 1924).

C. HIGHWAY CONSTRUCTION PROJECT PAYMENT BONDS

1. Bond Coverage: Mississippi has a specific statute setting forth bonding requirements for State Transportation Commission construction contracts, § 65-1-85. The statute, rewritten in 2003 and 2004, requires bonds for, "[a]ll contracts by or on behalf of the commission for construction, reconstruction or other public work...except maintenance....". § 65-1-85 (1). Bonds for construction must be in an amount equal to the contract price, meaning, "the entire cost of the particular contract let.". § 65-1-85

(1)(f). If change orders increase the price after the contract is signed, the statute authorizes the Transportation Commission to require additional bonding. *Id.* The bonds must cover the contractor's performance and payment "of all persons furnishing labor, material, equipment and supplies". *Id.*

2. Equipment: Since heavy equipment plays a major role in highway construction, the legislature since 1968 has provided in the Transportation contracts statute specific definitions for "equipment" as well as "labor" and "materials" as they relate to equipment. The statute states "equipment" includes, "the reasonable value of the use of all equipment ... which are reasonably necessary to be used and which are used in carrying out the performance of the contract, and the reasonable value of the use thereof, during the period of time the same are used in carrying out the performance of the contract". Equipment therefore includes equipment rentals or the value the use of owned equipment during the contract period. § 65-1-85 (2).

The statute states that "labor" includes all reasonably necessary repair work on equipment used in the construction. It defines "materials" and "supplies" as including repair parts reasonably necessary to the efficient operation of equipment used on the job. § 65-1-85 (2).

3. Materialmen: As is true in the case of the Little Miller Act, an issue can arise as to whether a supplier on a highway construction project is a materialman or subcontractor within the protection of the bond, or merely a materialman to a materialman outside the bond's protection. In *Webb v. Blue Lightning Service Company*, 237 Miss. 862, 116 So. 2d 753 (1960), for example, the Court held that a supplier of

gasoline and diesel fuel to a gravel company for use in the mining of gravel which in turn sold the mined gravel to the bonded contractor was not eligible for reimbursement under the bond. The claim was simply for material sold to another materialman. By contrast, in *Mississippi Road Supply Company v. Western Casualty & Surety Company*, 246 Miss. 510, 150 So. 2d 847, 851 (1963), the Court upheld the claim of a materialman who had furnished supplies directly to a subcontractor on a highway construction.

4. Procedures and Notice: Since the procedural provisions of the former public works statutes had been held to apply to highway bonds, one would assume that the procedural provisions of the Little Miller Act supplement § 65-1-85 and should be followed in highway bond actions. See *Dixie Contractors, Inc. v. Ballard*, 249 So. 2d 653 (Miss. 1971). Thus, for example, the Little Miller Act should be consulted for the time for bringing suit and notice of suit.

5. Special Notice Requirement for Equipment Providers: Providers of equipment to subcontractors for road construction should take special note of the strict notice of nonpayment requirement in § 31-5-31. Section 31-5-31 provides that any person who leases, rents or sells to a subcontractor equipment to be used in a road construction contract where the general contractor must be bonded, must: (1) notify the general contractor that credit is being extended to the sub and stating the terms; and (2), if the sub defaults, notify the general of the nonpayment within 30 days after payment is due. Failure of the equipment provider extending creditor to comply with the nonpayment notice provision of the statute abrogates any right to proceed against the bond for the equipment leased, rented or sold. § 31-5-31.

III. MISSISSIPPI LIEN LAW CLAIMS

1. Construction Claimants Covered:

Section 85-7-131 provides that, "[e]very house, building, water well or structure of any kind" is subject to the lien of the statute "for labor done or materials furnished, or architectural engineers' and surveyors' or contractors' service rendered" in construction or repairs.

However, it is important to note at the outset that Mississippi law limits the availability of a statutory construction lien to prime contractors and suppliers having a direct contract with the owner as opposed to a subcontract with another contractor. The statute limits the creation of lien rights to a contract made, "by the owner, or by his agent, representative, guardian or tenant authorized, either expressly or impliedly, by the owner." § 85-7-135. Subcontracts do not fit those categories. Thus, a prime contractor would have a lien against the owner for unpaid payments since the prime has a direct contract with the owner. However, subcontractors, laborers and materialmen who have no contract with the owner, but only a contract with the general contractor or with a lower tier contractor, generally have no statutory right to a lien in Mississippi. Miss. Code Ann. § 85-7-135; *Brown v. Gravlee Lumber Co., Inc.*, 341 So. 2d 907, 909 (1977).

That is not to say subcontractors are without a remedy. Subcontractors and subsuppliers may look to either the remedies of the stop notice statute or to any available payment bond for relief from unpaid claims (as we will see in greater detail below). However, the lien remedy is limited to primes since, "[n]o privity [of contract] exists between a subcontractor and an owner." *Timms v. Pearson,* 876 So.2d 1083, 1086

(Miss.App.2004).

One should also note that the State of Mississippi and its county and city subdivisions, as the sovereign, are not subject to private liens. *Key Constructors, Inc. v. H&M Gas Company*, 537 So. 2d 1318, 1321 (Miss. 1989). One should therefore not attempt to file a lien against the State, counties or municipalities. Presumably, though, the State and its subdivisions backed by the power to tax their citizens, will not go broke. So while a prime contractor hired by the State or municipalities may be limited to the rights of a general creditor against the sovereign, at least the general contractor in theory does not run a credit risk doing business with the State or municipalities. Therefore, while the prime contractor will not have a lien against the sovereign, it should not have a credit risk either. Of course the risk a prime contractor runs in performing work for private owners is quite different: a prime contractor or a construction manager who has a direct contract with a private owner must have a right to lien the owner's property as security for construction fees.

Justice Jimmy Robertson has noted that, "[t]here is no natural law of materialman's liens" and that claimants can have lien rights, "only to the extent that they have brought themselves within the terms of the statute" governing liens, § 85-7-131. *Riley Building Supplies, Inc. v. First Citizens National Bank*, 510 So. 2d 506, 508 (1987). So a prime contractor must read the construction lien statute (§ 85-7-131 *Miss. Code Ann.*) carefully to find his rights and obligations.

2. Tenants: Further, if the work is initiated without the written consent of the land owner by a tenant or guardian, only the structure, or some part thereof, or the

estate of the tenant in the land, and not the lot, is subject to the lien. § 85-7-137. *Brown v. Gravlee Lumber Co., Inc.*, 341 So. 2d 907, 909 (1977). This statute limiting lien rights involving improvements initiated solely by the tenant dovetails also with the § 85-7-135 limiting full lien rights to a contract made, "by the owner, or by his agent…or tenant authorized, either expressly or impliedly, by the owner." A landlord may therefore prevent his tenant from taking any action that would impose a lien by making it clear he the Landlord has not given the tenant any permission to create a lien. Thus, for example, a lease may say: "Tenant shall have no authority to permit or create a lien against Landlord's interest in the property."

3. Structures and Land Covered: Section 85-7-131 spells out the extent of the lien, depending on whether the structure is in a city, town or village (extending to the lot and curtilage); outside of any city, town or village (extending up to one acre on which the structure stands as selected by the lien holder); is a water well, oil or gas well, railroad or railroad embankment. If the services have been rendered upon the whole of a subdivision, the lien extends the entire subdivision, or to upon the portion of the property for which the services were required or were furnished. § 85-7-131.

4. Materials: The statute also creates a presumption that material shown to have been delivered to the job was used in the job. § 85-7-131. The presumption created by proof of delivery can be overcome only by specific proof that the delivered material was later diverted and not incorporated into the project subject to the lien.

5. Lien Notice Requirements: A lienholder must take steps set forth in the lien statutes to perfect the lien by filing notice of the lien if the lien is to have priority

over the interests of subsequent innocent purchasers, or over subsequent lenders taking deeds of trust (e.g., a subsequent second mortgage holder). *Riley Building Supplies, Inc. v. First Citizens National Bank*, 510 So. 2d 506, 509 (1987). Indeed, a lien is ineffective and nothing more than an inchoate right until notice of the lien is filed as required by the statute, rendering the holder of an unperfected lien nothing more than a common creditor. *Wortman & Mann, Inc. v. Frierson Bldg. Supply Co.*, 184 So. 2d 857, 859-860 (Miss. 1966).

The Chancery Clerk in each county of Mississippi maintains a book entitled "Notice of Construction Liens" as a part of the land records where lien holders may file and record their liens. § 85-7-133. The statute states the lien "shall not take effect unless and until some notation thereof shall be filed and recorded" in the Notice of Construction Liens book. *Id.* Thus, the lien must be recorded in the Notice of Construction Liens book to be effective under the statute.

In addition, the potential claimant *may*, but is not required to, record the construction contract under which he is proceeding in the land records with the Chancery Clerk. § 85-7-139. If the claimant files the contract before filing the notice of lien, the lien will be held to have been perfected at the time of the earlier filing of the contract. § 85-7-131. A prime contractor therefore may find it useful to file a copy of his contract early on, even before the work starts, to establish his priority position should he later have to file a lien. The filing of the contract is useful because an owner is less likely to be offended by the early filing of a contract, as opposed to the filing of a lien. The filing of the lien notice, if it follows the filing of the contract, can wait until a payment issue

arises, while at the same time the early filing of the contract reserves to the contractor an earlier priority date since by statute the lien notice date is made retroactive for priority purposes to the date that the contract had been filed. § 85-7-131.

The claimant, as a further protection, may also file a notice of lien in the lis pendens book maintained by the Chancery Clerk, in which case he must notify the owner of the filing. § 85-7-197. However, in any event, the essential filing to establish a lien is the filing in the Notice of Construction Liens book. § 85-7-133.

As to priority, the claimant's lien, "shall take effect as to purchasers or encumbrancers for a valuable consideration without notice thereof, only from the time of commencing suit to enforce the lien, or from the time of filing the contract under which the lien arose, or notice thereof, in the office of the clerk of the chancery court". § 85-7-131. Therefore, timely filing of the notice of lien or, as is also permitted in addition, of the contract, is essential to establish priority over later innocent purchasers and mortgage holders.

6. A Construction Lender Who Is Negligent May Lose Priority To A Materialman Who Has Perfected His Lien: A lender who finances the purchase of land is entitled to a preference for the mortgage securing the loan, "over all judgments and other debts of the mortgagor". § 89-1-45. Mortgage holders who have lent money to finance construction similarly may hold priority over the liens of contractors (or subcontractors and materialmen who subsequently perfect their liens by a stop notice and *lis pendens* filing)during or following the actual construction. However, the construction lender, if it is to maintain priority over the subsequent lien of a contractor, must be

prepared to show that it was reasonably diligent to see that advances of the construction loan went into the project instead of becoming diverted by the borrower to other projects or toward payment of unrelated debts. *Peoples Bank and Trust Co. and Bank of Mississippi v. L & T Developers, Inc.*, (Miss. 1983). A construction lender can show it was reasonably diligent by showing that it required the owner to obtain from the prime contractor an affidavit that he did not owe for materials and labor each time the contractor received an advance. *Wortman & Mann, Inc. v. Frierson Bldg. Supply Co.,* 184 So.2d 857, 861 (Miss. 1966). In addition, the lender can show that it checked the land records each time it advanced funds to see that if contractors or subcontractors had perfected lien rights. *Id.* However, even a negligent lender who fails even to require an affidavit of the owner or contractor will maintain the priority of his lien against a contractor who has failed to perfect his lien by filing the notice of construction lien required by the statute. *Riley Bldg. Supplies, Inc. v. First Citizens Nat. Bank,* 510 So.2d 506, 508 (Miss. 1987).

7. Commencement of Suit on a Lien and Statute of Limitations: The lien statutes provide a relatively short statute of limitations for suit. A claimant must initiate suit on the lien within twelve (12) months after the date the money claimed, **"*became due and payable, and not after*"**. (Emphasis added). § 85-7-141. <u>Notice that the 12 months runs from the payment due date, not the date of the filing of the lien notice.</u>

Thus,

one must file both the notice of lien and suit within the 12 months. However, "where there has been a continuous delivery of material, and the time of payment is not fixed by

contract, the statute begins to run against the lien from the delivery of the last lot of material." *Billups v. Becker's Welding & Machine Co.*, 186 Miss. 41, 189 So. 526, 528-529 (1939). See also *Inerarity v. A.S. Wade & Co.*, 106 So.828, 829 (Miss.1926) (lien barred where suit not brought until more than a year after default in monthly installments for materials).

The statute provides that a suit to enforce a lien is to be filed in the **circuit court** of the county in which the property is located. § 85-7-141. The statute does not mention county courts. However, while it is the safe choice to file in circuit court, do not be surprised if the circuit court by order refers the matter to county court if the amount involved is not large. The statute that should be amended to include county courts.

8. Joinder: The lien statutes require that any other parties claiming liens on the property be summoned and made parties to the suit or be allowed to intervene. §§ 85-7-143; 85-7-145. The statutes provide specific requirements as to what must be included in the claimant's complaint. § 85-7-141.

9. Attorney's Fees: If the lienholder is successful in reducing his lien to judgment, the lien statutes authorize the claimant to ask the judge to add the cost of attorney's fees for the prosecution and collection of the claim. § 85-7-151. Once the judgment is entered, the claimant may proceed to execute on the lien against the property as set forth in the statutes at §§ 85-7-153 to -157.

10. Application to Expunge A False Lien: An owner may file an Application

to have a County Court or Chancery Court expunge a false lien on two day's notice under

§ 85-7-201. A false lien is a lien filed by a contractor or supplier without just cause or just purpose to which he is not entitled under the lien statute. *Id.; Manderson v. Ceco Corp.,* 587 F. Supp. 445, 447 (N.D. Miss. 1984). The suit must be brought within one year of the filing of the false lien. § 85-7-201. Since the statute speaks to one who "falsely and knowingly" files the wrongful lien, one should first send a written demand that the lien be voluntarily removed and then move for the removal when the demand is not met. Also, as a matter of due process, one should take the precaution of having the Court issue a Summons to accompany the Application to be served on the defendant specifying the time, date and place for the hearing on the Application (see e.g. Form 1DD, Rule 81 Summons).

Subcontractors who fail to understand that they have no lien rights in Mississippi are often the filers of false liens. See § 85-7-135; and *Wenger v. First Nat. Bank of Biloxi*, 164 So.229, 230-231, 174 Miss. 311 (Miss. 1935). The sub may not understand that its remedy falls under the Stop Notice statute (§ 85-7-181) rather than the construction lien statutes. The general contractor may have a duty to the owner under its contract to keep the record clear of liens filed by subs. In that case the general contractor may need to initiate the Application, but should have the Owner join with him as a Plaintiff in the Application to expunge a sub's false lien in order to assure standing for the Application.

The false lien statute of § 85-7-201 provides a penalty for the filing of a false lien by the award to the complainant of "the full amount" of the false lien against the filer. The statute is penal in nature, and the penalty is based on its deterrent value, not on

attorneys' fees expended or other remedial measure of damages. However, the bar to obtaining the penalty is a high one, for it must be shown that the filer filed the false lien "falsely, knowingly, and without just cause" or "willfully". *Manderson v. Ceco Corp.,* 587 F. Supp. 445, 447 (N.D. Miss. 1984). Filing the lien on the advice of counsel may be a defense. *Id.* The filing of a release of the lien prior to the filing of the suit or hearing on the false lien may also be a defense. *Id.* at 446.

However, the owner may find it more convenient to arrange with the closing attorney and title insurer to bond around the lien rather than to go to the trouble and expense of incurring the legal expense to remove it.

The owner may also be able to state an action for slander of title. "A false statement which constitutes 'slander of title' may consist of an assertion that ...defendant has an interest in or lien on the property." *Walley v. Hunt*, 54 So.2d 393, 212 Miss. 294 (Miss. 1951). However, "[w]hatever be the statement, in order for it to form the basis of a right of action for slander of title, must have been made not only falsely, but maliciously." *Id.*

Of course one may also ask for the removal and discharge of a lien simply because the contractor, although acting in good faith, was mistaken in believing he was in compliance with his contract in all particulars, or mistaken that he is owed money by the owner. See e.g., *New Bellum Homes, Inc. v. Swain*, 806 So.2d 301, 304 (Miss.App.2001). One can ask the court to declare the lien invalid as a declaratory judgment action. See R. 57 MRCP; *Simmons v. Jaggers*, 914 So.2d 693, 694 (Miss.2005).

11. The Owner Can Create Lien or Stop Notice Rights Through an Agent: Under Section 85-7-135 Mississippi construction lien rights may be created, "when the contract or employment is made by the owner, or by his agent, representative, guardian or tenant authorized" by the owner. Thus, it is true that under some facts a realtor or developer may be found to have been an implied agent for the owner, placing the persons with whom he contracts in privity with the owner, and thus entitling persons who might usually be considered subcontractors to a direct lien, or those under them to the stop notice rights of a direct subcontractor. See *Bailey v. Worton*, 752 So.2d 470 (Miss.App. 1999). However, the facts in *Worton* are a bit unusual: there a subdivision developer granted permission to a realtor at the realtor's suggestion to design and build a house on a vacant back lot in order to render the lot more suitable for sale by the realtor, and allowed the realtor to advertise as the seller, making the subdivision owner an undisclosed principal, while the owner's actions cloaked the realtor with the apparent authority of an owner to control all aspects of the design, construction and sale. *Worton* must considered under its facts which not the usual case where an owner supplies a design to a general contractor to build to suit the owner's own needs and the owner's existence is known to all parties.

Nonetheless, the *Worton* case points out the risk an owner may take if he allows a potential developer/purchaser to jump the gun and start construction before closing on a contemplated sale property to the developer: the owner may find the potential developer/purchaser was his agent for the construction as to affected third parties during the period the owner still had the property before the sale, creating lien or stop notice

rights in the affected suppliers. The owner may find out he, even unwittingly, "had delegated ultimate authority, either intentionally or through his own negligence, to [the developer] for the construction of the house." *Bailey v. Worton,* 752 So.2d at 474. The developer can thus become the owner's agent with "the apparent authority from [the owner] in their dealings with" the construction contractor, "to bind [the owner]," providing lien or stop notice rights to contractors and suppliers. Id.

12. No Equitable Liens: Liens are the creations of statutes passed by the legislature. A chancellor has no authority to use his equitable powers to create a so-called "equitable lien" where none exists by statute. *Chic Creations of Bonita Lakes Mall v. Doleac Elec. Co., Inc.,* 791 So.2d 254, 259 (Miss.App.2000).

13. Mississippi Construction Liens and Arbitration: The question can arise how one can pursue arbitration rights while also asserting lien rights. The enforcement of a Mississippi construction lien, after all, calls for the filing of suit in the Circuit Court within one year, for a declaration of the right to foreclose on the property. See Section 85-7-141 (one must sue in Circuit Court to enforce a lien within one year of the time the money became "due and payable" and not after). The answer is that a contractual agreement to arbitrate construction disputes, as one would find in an AIA contract, does not preclude one's right to file a statutory construction lien. The AIA General Conditions address the matter. (See, e.g., AIA A141 – 2004 Terms and Conditions § A.4.2.5: "If a Claim relates to or is the subject of a mechanic's lien, the party asserting such Claim may proceed in accordance with applicable law to comply with the lien notice or filing deadlines prior to initial resolution of the Claim."). Also,

see, e.g., *Harris v. Dyer*, 50 Or.App.223, 623 P.2d 662, 665 (Or.1981). One may have to file the action within the one year statute of limitations to enforce a lien while requesting the court to stay the action pending the conclusion of an arbitration. Indeed:

> As a general rule, if parties have agreed to arbitrate all disputes arising out of their construction agreement, then arbitration will be considered a predcondition to any foreclosure action. The procedure most often followed is to stay the foreclosure action pending arbitration. While the arbitration does not substitute for foreclosing the lien, which under most mechanics' lien statutes may proceed only in a court of competent jurisdiction, the arbitration will decide many of the underlying contractual issues, including the amount to which the lien claimant is entitled.

6 Bruner & O'Connor *Construction Law* § 20:53 (2008). See also, 73 A.L.R.3d 1066, Maurice T. Bruner, "Filing of Mechanic's Lien or Proceeding for Its Enforcement as Affecting Right to Arbitration" (1976) § 3(b) ("Merely filing a mechanic's lien petition is not inconsistent with an intent to arbitrate the underlying contractual dispute and hence is not a refusal to arbitrate;….").

14. Mechanic's Liens for Vehicles and Articles: Mechanics have a possessory lien over the vehicles they repair for the repair charges so long as they retain possession. § 85-7-107 *Miss. Code Ann.* However, notice this twist: the lien is only for labor and materials; it does not cover storage costs. *Allstate Ins. Co. v. Green,* 794 So.2d 170 (Miss.2001). Further, the lien over automobiles does not extend to vehicles titled outside of Mississippi. *Id.* Moreover, in a very broad fashion, a mechanic of "any article" created or repaired at the request of another person has a statutory lien on the item for the cost of construction, repair or manufacture under § 85-7-101 and § 85-7-105 *Miss. Code Ann.* So a mechanic's lien can extend far beyond automobiles to "any item"

created or repaired at the request of another. Further, the mechanic's lien in the article can continue after the parting of possession by the mechanic if the appropriate notice of the amount due for labor and materials is unpaid is given to the owner. § 85-7-105 *Miss. Code Ann.* The mechanic's lien covers only articles which can be held or detached and seized for sale by the sheriff, and should not be confused with construction lien or stop notice rights.

15. Landlord's Lien: A landlord, by Mississippi statute, has a lien in personal property of his tenant located in the leased premises to secure the rent, "whether or not then due." § 89-7-51 (2) *Miss. Code Ann.* However, the landlord's lien is, "subject to all prior liens or other security interests perfected according to law." *Id.* For example, a lending institution that has taken an automatically perfected purchase money security interest in a mobile home (under § 75-9-302(1)(d)), which the law considers a consumer good, trumps a trailer park landlord's lien on a tenant's personal property which attached when the tenant placed the items in the mobile home. *Mullen v. Green Tree Financial Corporation-Mississippi*, 730 So.2d 9, 14 (Miss.1998). The landlord's lien, though, will trump any later perfected lien. *Id.* The priority of a landlord's lien in personal property over later perfected liens is recognized also by statute at § 89-7-1, requiring that a creditor acting on a writ of execution not take away goods from leased premises without first satisfying a landlord for any rent outstanding under a lease protected by his lien up to one year's rent. However, the landlord's lien must be prior in time. *Mullen,* supra, 730 So.2d at 14.

16. Condominium Liens: A condominium association can file an assessment

of condo fees against the owner as a lien by recording the charges with the Chancery Clerk. § 89-9-21. However, there is, "a legislative limit on the priority of the condominium assessment lien." *Tally Arms Condominium Ass'n, Inc. v. Breland*, 854 So.2d 28, 35 (Miss.App.2003). The condominium lien has no force beyond two years from filing, and has effect the second year only if the condo management files a renewal notice. *Id.*

17. Attorney's Lien: "Under Mississippi law…an attorney has a lien on all writings, documents and money of his client which come into his possession in the course of his professional employment. This lien entitles the attorney to retain possession of those papers, writings or money until all his fees are paid." *Brothers in Christ, Inc. v. American Fidelity Fire Insurance Company,* 680 F.Supp. 815, 818 (S.D.Miss.1987) (citing *Webster v. Sweat,* 65 F.2d 109 (5th Cir.1933). Further, "Mississippi law also recognizes a 'special' or 'charging' lien which entitles an attorney who, by his services, recovers a judgment, to have his fee satisfied out of that judgment." *Id.* The attorney must retain possession of the funds to enforce the charging lien, and "must have procured a judgment or decree in favor of his client." *Id.*

IV. MISSISSIPPI SUBCONTRACTOR'S AND MATERIALMEN'S STOP NOTICE LAW CLAIMS

1. Claimants Covered: The Mississippi Stop Notice statute, known also as the Stop Payment statute, states that an unpaid subcontractor or laborer of the prime contractor can give notice in writing to the owner of the amount due, claim the benefit of

the statute, and from that time on bind an amount sufficient to cover his claim in the hands of the owner until the claim is resolved. § 85-7-181.

As we saw in the section on construction liens, only prime contractors and others having a direct contract with the owner have the right to file a Notice of Construction Lien under the Mississippi construction lien statute set forth at § 85-7-131 (see §85-7-135, "Persons favored by lien"). A subcontractor cannot lien the property of the owner since, "[n]o privity [of contract] exists between a subcontractor and an owner." *Timms v. Pearson,* 876 So.2d 1083, 1086 (Miss.App.2004). Lien rights are thus reserved in the first instance to the prime who has a contractual relationship with the owner. Indeed, "[t]he [lien] remedy does not extend to subcontractors, who, according to the statutory scheme, must pursue a separate remedy under § 85-7-181 [the stop notice statute]." *Noble House, Inc. v. W&W Plumbing & Heating, Inc*. 881 So.2d 377, 386 (Miss.App. 2004).

Therefore the separate remedy for unpaid subcontractors, materialmen and laborers who have a contract with the general prime contractor, and no direct contract with the owner, is the Mississippi Stop Notice statute set forth at § 85-7-181. *Timms v. Pearson,* 876 So.2d 1083, 1086 (Miss.App.2004); *Chic Creations of Bonita Lakes Mall v. Doleac Elec. Co., Inc.,* 791 So.2d 254, 258 (Miss.App.2000); *Cummings v. Davis*, 751 So. 2d 1055, 1058 (Miss.App.1999). The Stop Notice statute is necessary to provide a remedy to an unpaid subcontractor because, "[a]t common law, materialmen and laborers who have dealt only with the prime contractor are general creditors of the prime contractor and have no right to recovery from the project owner." *Service Electric*

Supply Co., Inc. v. Hazelhurst Lumber Co., Inc., 932 So.2d 863, 868, ¶ 15 (Miss.App.2006). See also *Timms,* 876 So.2d at 1086, ¶8.

However, a subcontractor's stop notice rights, even where exercised, are limited. Thus, for example, a subcontractor or supplier must first check to see if the general contractor provided a payment bond to the owner for the project before giving a stop notice. As we have seen, bond rights are in lieu of stop notice rights, and a stop notice that ignores the presence of a bond is ineffective and may be expunged. *Ewin Engineering Corp. v. Deposit Guaranty Bank and Trust*, 216 Miss. 410, 62 So. 2d 572, 574 (1953), citing *Dickson v. U.S.F.&G. Co.*, 117 So. 245, 248 (Miss. 1928).

2. Sub-Sub Contractors Excluded: The protection afforded by the Stop Notice statute does not extend beyond those with subcontracts with the prime contractor. "Subcontractors or materialmen to another subcontractor are not entitled to recovery under this statutory provision." *Associated Dealers Supply, Inc. v. Mississippi Roofing Supply, Inc*., 589 So. 2d 1245, 1247 (Miss. 1991); *Chic Creations of Bonita Lakes Mall v. Doleac Elec. Co., Inc.,* 791 So.2d 254, 258 (Miss.App.2000). Such remote contractors and materialmen are mere "general creditors" of the parties with whom they have dealt. *Associated Dealers Supply, Inc. v. Mississippi Roofing Supply, Inc*., 589 So. 2d at 1247-1248. Accord., *Amerihost Development, Inc. v. Bromanco*, 2000 WL 137129 (Ms. Ct. App. 2/8/2000); *Cummings v. Davis*, 751 So. 2d 1055, 1058 (Miss.App.1999).

3. *Quantum Meruit* Claims Against the Owner Excluded: A subcontractor may be tempted to argue that its supply of materials for the owner's

ultimate benefit should give him common law rights against the owner for the value of his contribution to the project in the form of a *quantum meruit* claim. An owner, though, is not obligated to the subcontractor in *quantum meruit* even if the subcontractor remains unpaid and even if the subcontractor's work bestows great value on the owner's project. *Service Electric Supply Co.,Inc.,* 932 So.2d at870, ¶ 22. After all, an implied contract liability in *quantum meruit* could exist only in the absence of an express contract covering the work. That is not the case where a subcontract exists for the claimant's work. *Id.* Thus:

> …the owner's] implied liability that would arise generally from his receiving value from the party furnishing [materials], is taken away by the special contract [the owner] has made [with the prime contractor], and especially by the special contract which [the material supplier] has made with the person with whom the owner of the property has contracted to complete the work').

Id. Further, the subcontractor has an adequate remedy available under the stop notice statute. If the subcontractor has bound project funds in the owner's hands by a stop notice before the owner's payment of the funds to the prime, providing a sub a separate claim against the owner in *quantum meruit* would be duplicative of the stop notice remedy provided by statute (§ 85-7-181). And if the subcontractor has failed to avail itself of the stop notice remedy, the owner could hardly be held responsible in *quantum meruit* despite the sub's failure to proceed under the stop notice statute. See also *Timms v. Pearson,* 876 So.2d at 1086 ("Absent such [stop] notice, an owner has no obligation to a subcontractor who has provided materials or services pursuant to an agreement with a

contractor.”).[1]

4. Funds Frozen: However, to be effective and enforceable, the claimant must give the stop notice while the owner still owes money to the prime contractor. If the owner has already made final payment to the prime contractor when he receives the stop notice, the stop notice is ineffective and the owner has no liability to the subcontractor. *Timms v. Pearson,* 876 So.2d 1083, 1086 (Miss.App.2004); *Chic Creations of Bonita Lakes Mall v. Doleac Elec. Co., Inc.,* 791 So.2d 254, 259 (Miss.App.2000) (quoting *Williams v. Taylor,* 216 Miss.563, 569, 62 So.2d 883, 885 (1953)); *Corrugated Industries v. Chattanooga Glass Company*, 317 So.2d 43 (Miss.1975). An owner’s payments to the prime prior to receiving a stop notice “extinguish” the owner’s debt for the amounts paid, precluding liability of the owner under the stop notice statute to the extent of the payments made before receipt of the notice. *Amerihost Development, Inc. v. Bromanco, Inc.*, 786 So.2d 362, 367 (Miss. 2001) (citing *Engle Acoustic & Tile, Inc. v. Grenfell,* 223 So.2d 613,619 (Miss.1969)).

Further, the stop notice only requires the owner to withhold payment from the prime of, “the amount claimed in *that notice*.” (Emphasis original). *Amerihost Development,* 786 So.2d 362, 365 (Miss. 2001) (quoting *McNair v. M.L. Virden Lumber Co.*, 193 Miss. 232, 4 So. 2d 684, 689 (1941)). Therefore, “the filing of a stop-notice under § 85-7-181 benefits only the subcontractor(s) giving actual notice prior to the time the owner pays the prime contractor.” *Id.* A subcontractor failing to timely issue a stop

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1 But an unpaid prime, by contrast, could elect to proceed either in contract or on *quantum meruit* as a basis for payment as long as the contractor has reached substantial performance, and a recission or cancellation of the contract would be warranted due to the owner’s breach. *Sumrall Church of Lord Jesus Christ v. Johnson,* 757 So.2d 311, 313-314 (Miss.App.2000).

notice could not claim the benefit of another subcontractor's stop notice that was timely issued. Further, the subcontractor giving the stop notice is not required to notify other subcontractors of the stop notice (although the sub must give notice of any subsequent suit by summons at that time to any other interested parties "so far as known" by him). *Amerihost Development,* 786 So.2d at 366; § 85-7-181. In short, a sub who has not issued a stop notice while the owner still retains funds owed the prime cannot, "ride the coat-tails of those subcontractors and materialmen who actually asserted their rights" under the stop notice statute." *Amerihost Development,* 786 So.2d at 367.

Nor may a stop notice reach an amount owed by a third party to the owner since the statute does not cover funds, "in the possession of someone entirely outside the owner-contractor-subcontractor hierarchy." *Chic Creations of Bonita Lakes Mall v. Doleac Elec. Co., Inc.,* 791 So.2d at 258.

As noted, the stop notice cannot reach funds previously paid by the owner to the prime contractor in good faith prior to his receiving the stop notice. Such prior payments, "extinguish the right pro tanto of a subcontractor, materialman, or laborer to a lien on the property for the claim." 53 Am.Jur.2d *Mechanics' Liens* § 322 (1996); *Service Electric Supply Co., Inc. v. Hazelhurst Lumber Co., Inc.*, 932 So.2d 863,869, ¶ 15 (Miss.App.2006). However, the stop notice does reach and freeze for the benefit of the unpaid subcontractor or materialman whatever funds are still in the hands of the owner that are due the prime contractor, "as of the date the notice is served." *Noble House, Inc. v. W & W Plumbing & Heating, Inc.*, 881 So.2d 377, 385 (Miss.App. 2004). Therefore, the owner should give priority to stop notices according to the date of their

receipt where multiple stop notices are received from subcontractors on the project.

5. Lis Pendens Notice Filing to Back Up Stop Notice: If the subcontractor or materialman wants to give teeth to his stop notice to prevent its being ignored by the owner, it can file a lis pendens notice on the land records with the Chancery Clerk as permitted by § 85-7-197 *Miss. Code Ann.* The lis pendens is not a lien, but like a lien will be of concern to lenders of the project. A lis pendens notes a subcontractor has not been paid for its work on the project; if the owner ignores the stop notice and pays the contractor over the stop notice the stop notice can turn into a lien. Therefore the lis pendens notice preserves the sub's or materialman's priority position should it have to make a later claim on the property because the owner disregarded the stop notice by paying the general contractor. At the very least, the provision of the stop notice and the filing of the lis pendens notice along with it will get the owner's attention. Further, the lis pendens may cause the owner to require the general contractor to provide a payment bond for the claimant's potential benefit to the owner in order to clear the land record of the lis pendens filing.

The subcontractor must provide the lis pendens notice to the owner by certified mail as well as file it with the Chancery Clerk, all as called for by § 85-7-197.

6. Determining the Status of Party as the Prime Contractor or Construction Manager-Agent of the Owner: Since the protection of the stop notice statute is limited to subcontractors dealing directly with the prime, the question can arise as to who is the prime contractor for the job. In *Associated Dealers Supply, Inc. v. Mississippi Roofing Supply, Inc.*, 589 So. 2d 1245 (Miss. 1991), one of the corporate co-

owners of a Red Apple Inn project maintained on its payroll an employee who supervised the construction of the Inn and who hired the electricians, plumbers, framers, roofers and others to do all the actual construction. The Supreme Court found the co-owner was the prime contractor and that the co-owner's ownership status was irrelevant to determination of its status as the prime. The Court accepted the dictionary definition of prime as, "'the party to a building contract who is charged with the total construction and who enters into sub-contracts for such work as electrical, plumbing and the like.'" *Id.* at 1247-8 (quoting Black's Law Dictionary). Further, "[a]n owner is not excluded from this definition." *Id* at 1248. Thus, the Court found the whether a party is the prime should turn on the party's "activities isolated from its ownership". *Id.* Moreover, the Court found that since the supplier in that case supplied to a contractor who had contracted with the co-owner/prime contractor of the Inn, the supplier was a sub-sub not eligible to assert stop notice rights under the stop notice statute. *Id.*

A similar issue can arise for stop notice analysis whether a party should be characterized as a prime contractor or as construction manager-agent of the owner. A construction manager is, "a mere agent for a project's owner and …engages 'trade contractors' in his principal's name to perform most or all of the actual work.'" *Aladdin Const. Co., Inc. v. John Hancock Life Ins. Co.*, 914 So.2d 169, 176 (Miss.2005). By contrast, "a general contractor is 'in the chain of liability and…hires 'subcontractors' in his own name to perform work.'" *Id.* One indicator would be whether the party hired by the owner was to receive part of the construction cost as compensation in the manner of a contractor or was only to receive a professional fee for management. *Id.* at 177. If the

party hired by the owner is found to be a general contractor, then parties it dealt with are subs whose protection is to be found in the stop notice statute. However, if the party hired by the owner was the owner's direct agent, then the parties it dealt with would have lien rights against the owner. *Id.* at 180. Generally, "'the existence of a distinction between 'general contractor' and 'construction manager' is a question of fact for trial on the merits'" rather than a question of law that can be disposed of by summary judgment. *Id.* at 175, 180.

Prime contractors need to pay attention to the rights that subcontractors and materialmen can have under the Mississippi Stop Notice statute, and the limitations on those rights, since the owner may require that the prime contractor keep the project clear of materialmen's stop notices and lis pendens filings, and may need to move with the owner to clear any invalid stop notices given by sub-subcontractors having no such rights (as where a payment bond exists to protect the subs' interests in lieu of stop notice rights).

7. Resolution of the Stop Notice Claims by the Owner: Once the owner has received a stop notice the owner should be able resolve it by paying the subcontractor directly while providing a notice of the payment to the prime contractor. After all, once the stop notice is given, "…the subcontractor becomes entitled to payment **from the owner** up to the amount in which the owner is indebted to the general contactor as of the date the notice is served." *Timms v. Pearson,* 876 So.2d 1083, 1086 (Miss.App.2004) (Emphasis added). See also *Noble House, Inc. v. W & W Plumbing & Heating, Inc.*, 881 So.2d 377, 385 (Miss.App. 2004) ("Once a subcontractor who has not received payment

for his work by a contractor provides the property owner with written notice, he is entitled to payment **from the owner** up to the amount the owner is indebted the general contractor as of the date the notice is served. Miss. Code Ann. § 85-7-181 (Rev.1999).") (Emphasis added).

However, another way for an owner to resolve a stop notice if he receives one while still owing money to the contractor is to obtain the agreement of the subcontractor to make out a joint check to the prime contractor and the subcontractor of the funds due. See, S.R. Barrett, Jr., "Joint Check arrangements: A Release for the General Contractor and Its Surety", *The Construction Lawyer* Vol. 8, No. 2 (April 1988) at p. 7:

> By making the payment check payable jointly to two parties, the maker give each party the right to control the subsequent negotiation of the check. A bank or other holder of the check must require the signature of both payees before negotiating the check. Thus, either payee may block the other from negotiating the check simply by withholding its endorsement. This arrangement theoretically gives each payee the bargaining power necessary to insure that it will receive its proper portion of the proceeds.

See also UCC Section 3-116(b). But as to enforceability of joint checking see ft.n.[2]

Also, the owner has the option under of the statute of paying the amount due by him under the contract with the contractor into the court by interpleader, summon all known claimants against the contract funds into court to make their claims, and thereby escape any potential liability for costs and attorney's fees that would exist if he unjustly

2 But note an owner's **agreement to joint check** the prime and subcontractor **may not create an enforceable obligation** in certain circumstances. Contractual consideration may be lacking for the owner's agreement to issue a joint check. The owner may have no contractual relationship or rights against the subcontractor and vice versa. See *Service Elec. Supply Co., Inc. v. Hazelhurst Lumber Co., Inc.*, 932 So.2d at 869-870, ¶¶17-21 (Miss.App.2006).

denied the existence of the debt to the prime when the notice was received. Indeed, if the owner can establish it has acted as a mere "disinterested stakeholder", it will be entitled to attorney's fees for the cost of the interpleader action against the interplead fund. However, the award of attorney's fees to the owner who interpleads, "is a discretionary matter lying with the trial court." *Amerihost Development, Inc. v. Bromanco, Inc.*, 786 So.2d 362, 367-368 (Miss.2001). An owner's repeated ignoring requests to pay over the frozen funds before interpleading them could count against him on the issue of fees.

If the subcontractor initiates the suit, the owner retains the option of paying into court the amount due on the contract or, the amount "sufficient to pay the sums claimed", and again avoid any claim for costs and attorney's fees. However, if the owner, once sued with the prime contractor, without cause denies the indebtedness sufficient to cover the claims, the court "shall" give judgment to the issuer of the stop notice and award costs and reasonable attorney's fees to the unpaid subcontractor. *Id*. Once judgment on the stop notice is entered against the owner, it becomes a lien from the date of service of the original stop notice, enforceable against the owner's property on which the work was done. § 85-7-181. See *Service Electric Supply Co., Inc. v. Hazelhurst Lumber Co., Inc.*, 932 So.2d at 869, §15 (Miss.App.2006) ("A judgment against the owner under section 85-7-181 operates as a lien commencing on the date the stop notice was served."). Thus, a stop notice can turn into a lien against the owner's property if the owner forces the issuer of the stop notice to go all the way and take a judgment against him on the stop notice.

8. Owner's Offset Against Frozen Funds for Incomplete or Defective

Performance Under The Prime Contract: The Owner has a right to deduct from the amount owed the prime contractor, that would otherwise be reached by a stop-notice, the amount required to complete incomplete or defective work by the prime contractor and his subs. "...[T]he right of the owner to deduct damages because of the default of the contractor as against the claims of subcontractors, laborers, and materialmen has been recognized". 56 C.J.S. *Mechanics' Liens* § 322 at p. 374. After all, the stop notice statute reaches only any funds the prime contractor "...holds that *otherwise* would be paid to the contractor." (Emph. added). *Chic Creations of Bonita Lakes Mall v. Doleac. Elec. Co., Inc.,* 791 So.2d 254, 257 (Miss.App. 2000). Thus, the stop notice reaches funds owed the prime, "after subtracting any completion costs or other performance generated setoffs or backcharges", that the unpaid suppliers and subs are entitled to the remaining funds held on the date of the receipt of the notice. E.G. Gallagher, "Upaid Subcontractor's or Supplier's Right to Payment out of Contract Funds", *The Construction Lawyer,* Vol. 10, No. 1 (January 1990) at p. 9.

The Owner certainly has the right to first determine and make offsets for defects in performance in Mississippi where our stop notice statute is, "by subrogation to the rights of the independent contractor. The materialmen or laborers under such a statute are entitled to a lien only when the contractor is entitled to one, and there is something due or to become due to the principal contractor from the owner." *Chancellor v. Melvin,* 52 So.2d 360, 365, 211 Miss. 590, (Miss.1951). Indeed, such offsets would be appropriate where substantial completion has not been reached. "In the absence of substantial performance, the right to a lien may be denied." 53 Am.Jur.2d *Mechanics'*

Liens § 247 (1996). Again, in the absence of lien rights by the prime, stop notice rights are diminished accordingly.

The owner must be careful, after receipt of a stop notice, not to pay over to the prime contractor additional monies to repair the prime contractor's defective work that otherwise would not be owed by the owner. Otherwise, such misspent funds become chargeable against the owner in the subcontractor's action. *McNair v. M.L. Virden Lumber Co.,* 193 Miss. 232, 4 So.2d 684 (Miss.1941).

More generally, when considering an owner's retaining funds against the prime for defects, an owner has a right in both contract and in common law to retain (or recover) funds to cover the cost of repairing defects; the contractor after all has a legal obligation to perform in a workmanlike manner. *New Bellum Homes, Inc. v. Swain*, 806 So.2d301, 307-308 (Miss.App.2001) (residential construction defects); *Gerodetti v. Broadacres, Inc.*, 363 So.2d 265, 268 (Miss.1978) (commercial construction defects). A contractor is in material breach of his duty to perform construction in a workmanlike manner where there is a, "'failure to perform a substantial part of the contract or one or more of its essential terms or conditions, or if there is such a breach as substantially defeats its purpose.'" *McCoy v. Gibson*, 863 So.2d 978, 980 (Miss.App.2003) (residential construction defects). However, where the defects cannot be repaired at a reasonable cost or without economic waste, or the repairs would be impractical, the court should only award the diminished value of the property determined by an appraiser as opposed to the repair cost. *Geordetti*, 363 So.2d at 268. The jury should be instructed on the cost rule and the diminished value rule as appropriate. *Id.* Application of the

diminished value rule can result in a greatly reduced damages figure compared to the cost of repair. See, e.g., *Johnson v. Black Brothers, Inc.*, 879 So.2d 525, 529 (Miss.App.2004) (diminished value of a house due to an uneven floor was $25,000 as determined by an appraisal; the cost of repairing the floor was $228,000, or more than ten times as much, so the Chancellor correctly chose to award the owner only the diminished value of his residence).

9. Joinder: The claimant filing suit must summon all other known interested parties into the action "so far as known" by him, and other claimants may intervene if not summoned by the claimant. § 85-7-181.

10. Equipment Claims Excluded: The federal Fifth Circuit Court of Appeals has held that the term "materials" in the stop notice statute (§ 85-7-181) does not include equipment, just as the same term "material" in the private bond statute (§ 85-7-185) has been held not to include equipment unless the parties to the bond write coverage in for equipment. *Coatings Manufacturers, Inc. v. DPI, Inc.*, 926 F. 2d 474, 478-79 (5th Cir. (Miss.) 1991). Rather, the stop notice statute, "applies only to services or supplies actually incorporated into the structure and cannot be invoked by a supplier of rental equipment." *Id.* at 475, 478-479. An equipment dealer should check, though, to see if the prime contractor was required to give the owner a payment bond that is broad enough to cover the equipment claim. If the owner is a public entity, there should be a payment bond in place covering equipment rentals and fuel as noted in the bond sections above.

11. Assignments by the Prime: § 85-7-183 provides that no prime contractor can assign, transfer or otherwise seek to defeat the stop notice or other rights

of its subcontractors, laborers and materialmen, and that all such assignments, transfers and other dispositions are subordinate to the rights of the subcontractors, laborers and materialmen, as well as of the owner, except where the prime contractor protects such parties by entering into a performance bond subject to the private bond statute of § 85-7-185.

V. MISSISSIPPI OPEN ACCOUNT CLAIMS

1. Open Account Claims: If all other relief is unavailable under the bond, lien and stop notice statutes, and there is no formal written contract such as a credit application but only an open account based on invoices, a claimant should consider the Mississippi Open Account Statute (§ 11-53-81). The Mississippi Open Account Statute provides a means for the Court to add attorney's fees for collection to the debt when rendering a judgment for the Plaintiff despite the absence of a formal written contract providing for attorney's fees.

An open account is an unwritten contract under which a seller agrees in advance to extend credit to a buyer for purchases. *McArthur v. Acme Mechanical Contractors, Inc.,* 336 So.2d 1306, 1308 (Miss.1976). An open account is therefore, "'an account based on continuing transactions between the parties which have not closed or been settled.'" *Douglas Parker Electric, Inc. v. Mississippi Design and Development Corporation*, ¶8, No. 2006-CA-00285-COA (Miss.Ct.App. 02/20/2007) (quoting *Franklin Collection Serv. V. Stewart,* 863 So.2d925,930 ¶4 (Miss.1978). That is, a suit on an open account is "an action to collect on a debt created by a series of credit transactions'", albeit the agreement was unwritten. *Allen v. Mac Tools, Inc.,* 671 So.2d

636, 644 (Miss.1996).

A remote supplier (a sub-sub or below), for example, would use the open account statute where the supplier without a written contract provided supplies and issued invoices that remain unpaid. The Open Account Statute provides authority for the judge to add attorney's fees to the debt where the debtor fails to pay 30 days after claimant has made a written demand correctly setting forth the amount owed with an itemized statement of the account. § 11-53-81.

However, the court will **not** permit the use of the open account statute as authority

to add attorney's fees to the debt if the claim is based on a written contract rather than an open account, and the written contract fails to contain an attorney's fees provision. See *C.R. Daniels, Inc. v. Yazoo Manufacturing Co.*, 641 F. Supp. 205, 210 (S.D. Miss 1986), involving a contract created by the purchaser's written purchase orders accepted by the seller. "Daniels [the seller] is not entitled to attorney's fees under this section [11-53-81] because his claim against Yazoo [the buyer] is based on contract rather than open account." *Id.* Therefore, "…the federal court has stated that attorney's fees are not available under section 11-53-81 when the claim is based on contract." *H&E Equipment Services, LLC v. Floyd,* 959 So.2d 578, 583 (Miss.App. 2007) (citing *Daniels).*

Indeed, since, "[a]n open account is an unwritten contract", the open account statute has no application and is not available where there is a written purchase order, written credit agreement or other signed contract that is the basis of the plaintiff's claim. *McArthur v. Acme Mechanical Contractors, Inc.,* 336 So.2d 1306, 1308 (Miss.1976);

C.R. Daniels, Inc. v. Yazoo Manufacturing Co., 641 F.Supp. 205, 210 (S.D. Miss.1986) (citing *Westinghouse v. Moore & McCalib, Inc.,* 361 So.2d 990, 992 (Miss.1978)). Therefore where there is a written credit application or other written contract one can look only to the terms of the written agreement for a right to add attorney's fees for collection to the debt, and not to the open account statute.

Also, to recover attorney's fees under the open account statute, the plaintiff must succeed in recovering a judgment for the amount sued for, or at least within "a few dollars" of the claim. Attorney's fees will not be granted where the court finds liability on some invoices but not others. *Id.* Similarly, the Court will not award attorney's fees where the judgment is "partially in favor of both parties" with liability found on only potion of invoices sued on since in such a case the open account claimant is not the "prevailing party." *Barnes, Broom, Dalls and McLeod, PLLC v. Estate of Cappaert, Deceased,* 2007-CA-0276-SCT at ¶21-22 (Miss.2007).

However, "while courts must strictly construe the attorney's fees on the open accounts statute", the cases require only that the amounts stated in the demand letter and in the complaint be "a correct amount". The amount demanded in the complaint can vary from the amount stated earlier in the demand letter to reflect credits for payments received between the time of the demand letter and the later filing of the complaint. *Gulf City Seafoods, Inc. v. Oriental Foods, Inc.* 2006-CA-00987 at ¶16 (Miss.App.2007).

Further, "once a prima facie case is made on open account, the burden of proof shifts to the account debtor to prove that the amount claimed is incorrect." *Natchez Electric and Supply Co., Inc. v. Johnson,* 968 So.2d 358, 360 (Miss.2007).

Moreover, an open account claimant should be cautioned that if it brings suit under the statute, but fails to prove any of the invoices are owed so that the defendant prevails, the statute entitles the defendant to attorney's fees to be set by the judge. § 11-53-81. So, the statute can cut either way! Thus, where a defendant prevails on the plaintiff's claims and, in addition, wins on a counterclaim establishing an open account debt against the plaintiff, for which the defendant made demand before filing the counterclaim, the defendant is entitled to attorney's fees as the prevailing party under the statute. *Par Indust. v. Target Container Co.*, 708 So. 2d 44 (Miss. 1998).

Recently the Mississippi Court of Appeals held that the Open Account Statute is not applicable to add attorney's fees in favor of the defendant if the open account claim concludes in the pretrial stage by either the plaintiff's voluntary dismissal of the claim, or by a successful summary judgment granted to the defendant to preclude the open account claim, and where the parties thereafter go on to litigate the Plaintiff's claims on the Plaintiff's alternative theory of contract. See *H & E Equipment Services, LLC v. Floyd*, 959 So.2d 578, 583 at ¶ 18 (Miss.App. 2007) (citing *Hughes Equipment Co. v. Fife*, 482 So.2d 1144, 1145 (Miss.1986) and *C.R. Daniels, Inc. v. Yazoo Mfg. Co.,* 641 F.Supp. 205, 210 (S.D.Miss.1986)).

Further, the Mississippi Court has refused to recognize an open account claim where the account listed dates and hours worked, but there was no agreement as to the hourly rate. The open account claim must be for a liquidated amount or sum certain. *Stanton & Associates v. Bryant Construction Co.*, 464 So. 2d 499, 502-03 (Miss. 1985). That is, an open account, "must contain a 'final and certain agreement on price.'"

Douglas Parker Electric, Inc. v. Mississippi Design and Development Corporation, ¶8, No. 2006-CA-00285-COA (Miss.Ct.App. February 20, 2007) (quoting *Motive Parts Warehouse, Inc. v. D & H Auto Parts Co.,* 464 So.2d 1162,1166 (Miss.1985).

In *H & E Equipment Services, LLC v. Floyd*, 959 So.2d 578, 581 at ¶11 (Miss.App. 2007), the Court addressed what is necessary to prove in court to have invoices entered into evidence under the business records exception to the hearsay rule of MRCP 803(6). The Court affirmed the exclusion of invoices where the witness only testified that he was the custodian of the records and that the invoices, many of which were computer generated reprints, were generated in the ordinary course of the business. The witness failed to explain how the documents were created using the company's information or to state that the invoices were originally created at or near the time the charges were incurred and that the reprints of the invoices contained the same information as the originals without alteration as to the amounts due.

Although a fine point, while an open account is specific "form of oral contract", an open account claim may be distinguishable from other forms of oral contract claims. *Id.* at ft.n.1. An open account, "'results where the parties intend that…the account shall be kept open and subject to a shifting balance as additional related entries of debits or credits are made, until it shall suit the convenience of either party to settle and close the account…." *Id.* By contrast a claim based on only an oral contract may set a specific contingency to occur that will trigger the payment obligation other than completion of the work and invoicing. In *Douglas Parker Electric*, noted above, a fact issue for trial was whether an oral agreement set the payment obligation for electrical work to a barge to

occur upon the sale of the barge or upon the payment to the owner of insurance. Either way payment would not become due upon the mere completion of the work and the presentation of an invoice. *Id.* at ¶¶ 12-14. Bear in mind, though, that oral understandings are irrelevant if there was a written agreement or contract meant to embrace the whole of the parties' agreement.

2. Reasonableness of Attorney's Fees Claimed: "In collection suits, there is a rebuttable presumption that one-third of the judgment obtained is reasonable, where the fee is calculated to be no more than $5,000." *Gulf City Seafoods, Inc. v. Oriental Foods, Inc.,* 2007 WL 4111418, 2006-CA-00987 at ¶19 (Miss.App.2007) (citing *Dynasteel Corp. v. Aztec Insus., Inc.,* 611 So.2d 977,986 (Miss.1992)). The case also notes a list of other factors that can be taken into account, e.g. time and labor required and preclusion of other employment to the attorney by the time involved.

3. Statute of Limitations: The statute of limitations for claims on unwritten contracts in Mississippi, including Mississippi open account claims, is three (3) years after the accrual of the cause of action. § 15-1-29 *Miss. Code Ann.* However, there is an exception to consider. The accruing of the cause of action can be extended by new assurances or promises of payment. *Harrison Enters., Inc. v. Trilogy Commc'ns, Inc.,* 818 So.2d 1088,1096 (¶¶35-37)(Miss.2002). Indeed, the doctrine of equitable estoppel tolls the running of the statute of limitations where a debtor knows or has reason to know that its assurances and promises of later payment cause a party to delay filing suit based on the assurances. *Douglas Parker Electric, Inc. v. Mississippi Design and Development Corporation*, ¶¶18-19, No. 2006-CA-00285-COA (Miss.Ct.App. 02/20/2007) (citing

PMZ Oil Co. v. Lucroy, 449 So.2d 201,206 (Miss.1984). In *Douglas Parker Electric* the debtor's alleged promises to pay for electrical work upon the later sale of the barge or payment of to him of insurance proceeds created a material issue of fact as to the start date for the running of the statute of limitations for payment.[3]

4. Affidavit to Account Statute Repealed: The old Affidavit to Open Account Statute (formerly § 13-1-141) that allowed a creditor to plead an affidavit to open account and thereby require the defendant to file a counter-affidavit showing where the account was wrong, or have judgment entered against him for the account, was repealed in 1991. The current statute on open account, §11-53-81, conforms to modern pleading rules in that it does not require the defendant to swear to the answer. Rather, the current statute and rules of procedure allow for the presentation to the Judge of a motion for summary judgment on the account accompanied by an affidavit, or a trial, following an exchange of pleadings and the opportunity for both sides to engage in discovery.

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[3] In the construction context the "statute of limitations" applicable to contractors' contractual claims for payment may be contrasted with the "statute of repose" applicable to owners' claims for construction defects. An owner has six (6) years to sue the contractor for construction defects. § 15-1-41 *Miss.Code Ann.* Further, unlike the exception noted above for the statute of limitations on payment claims, "No action may be brought" for defects "more than six (6) years after the written acceptance or actual occupancy or use, whichever occurs first" on a project, no matter what. Not even fraudulent concealment (which can toll application of a statute of limitations per §15-1-67) provides an exception tolling a "statute of repose." *Steve Windham v. Latco of Mississippi, Inc.*, No. 2005-CA-02086-COA ¶¶6-8 (Ct.App.2007). The statute of repose "incorporates a policy judgment" by the legislature that at the end of the six (6) years following actual occupancy without a suit being filed, "contractors…are entitled to close their books" on their projects, defective or not. *Id.* at ¶6.