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BILL ANALYSIS

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Senate Bill 405 (as introduced 4-21-05)

Sponsor: Senator Valde Garcia

Committee: Economic Development, Small Business and Regulatory Reform

Date Completed: 6-29-05

## **CONTENT**

**The bill would amend the Construction Lien Act to do the following:**

- Allow a person to bring an action to discharge a lien on a residential structure that had been recorded by an unlicensed person.**
- Require licensed contractors to pay a \$10 fee upon initial licensure and a \$10 fee for each year of license renewal, rather than a \$50 fee upon initial licensure, for deposit in the Homeowner Construction Lien Recovery Fund.**
- Require laborers and other lien claimants to pay a \$50 fee every three years.**
- Require the Department of Labor and Economic Growth (DLEG) to mail notice of renewal fees.**
- Delete the authority of the DLEG Director to require additional assessments when the Fund balance is below \$1.0 million.**
- Revise the calculation of the limit on Fund expenditures for administration.**
- Revise provisions concerning recovery from the Fund.**
- Prohibit the payment of interest from the Fund.**
- Increase the maximum amount that may be paid to subcontractors, suppliers, and laborers per residential structure from \$75,000 to \$100,000.**

### Overview of the Act

The Construction Lien Act provides for the creation and enforcement of liens to protect the rights of people who perform labor or supply material or equipment for the improvement of real property. Under the Act, a contractor, subcontractor, supplier, or laborer has a construction lien on the interest of the owner or lessee who contracted for the property improvement. The Act prescribes procedures for claiming and enforcing a construction lien, with specific provisions for residential structures.

The Homeowner Construction Lien Recovery Fund, created under the Act, is used to pay claims of subcontractors, suppliers, and laborers, if the owner or lessee of residential property can demonstrate that he or she paid for the contracted services. The Fund is funded by assessments against licensed contractors, a fee charged to laborers who recover from the Fund, and a fee charged to other lien claimants who choose to become members of the Fund.

### Licensure Requirement; Discharge of Lien

Under the Act, a contractor does not have a right to a construction lien on the interest of an owner or lessee in a residential structure unless the contractor has provided an improvement to the residential structure pursuant to a written contract between the owner or lessee and the contractor. The contract must state that a residential builder or residential maintenance and alteration contractor, an electrician, and a plumbing contractor are required to be licensed under the applicable statutes. If the contractor is required to be licensed to provide the contracted improvement, the contract must state that the contractor

is licensed and state the license number. The bill also would require the contract to state that a mechanical contractor is required to be licensed under the Forbes Mechanical Contractors Act.

Under the bill, the owner of residential property on which a construction lien had been recorded by a person who was not licensed as required by the Act, or any person affected by the lien, could bring an action to discharge the lien. If the court determined that the person who recorded the lien was not licensed as required, that person would be liable to the person who brought the action for all damages that resulted from the recording and any attempts to enforce the lien, including actual costs and attorney fees.

A person who brought an action to recover for the performance of any act or contract for which a license was required would have to allege in the complaint and would have the burden of proving that he or she was properly licensed.

### Fees

Licensed Contractors. The Act imposes a \$50 fee on individuals applying for initial licensure as a residential builder or residential maintenance and alteration contractor, electrical contractor, plumbing contractor, or mechanical contractor. The fee must be paid in addition to the license fee and is deposited in the Homeowner Construction Lien Recovery Fund.

The bill would delete the \$50 fee. Instead, a person would have to pay a \$10 fee when applying for one of the licenses described above. When applying to renew the license, the person would have to pay a \$10 fee for each year that the renewed license would be valid.

Laborers & Other Lien Claimants. Currently, a laborer who seeks to recover from the Fund is not required to pay a fee until he or she obtains a recovery; at that time, a \$15 fee must be withheld from the Fund from the laborer's final recovery. Under the bill, this would apply the first time that a laborer sought to recover from the Fund. The bill also would delete a provision under which the total amount withheld from the Fund from a laborer in any one-year period may not exceed \$50.

Under the Act, except for licensed contractors and laborers, any other lien claimant may become a member of the Fund by paying a \$50 fee before the date of the claimant's contract for the improvement to a residential structure. The bill would delete a provision that limits a lien claimant's payment to \$50 in a year. Under the bill, if a lien claimant were a supplier that conducted business from more than one retail location, each retail location would have to be treated as a separate person for purposes of paying fees and renewal fees for Fund membership.

Under the bill, if a laborer or other lien claimant paid an initial fee (described above) on or before June 1, 2005, he or she would have to pay a \$50 renewal fee by June 1, 2008, and a \$50 renewal fee by June 1 of every third year after the first renewal payment. If the person paid the initial fee after June 1, 2005, he or she would have to pay a \$50 renewal fee by the first June 1 following the third anniversary date of the initial payment and a \$50 renewal fee by June 1 of every third year after the first renewal payment.

A person could pay a renewal fee after the date it was due, but would not be entitled to recover from the Fund for an improvement made after the due date and before the fee was paid.

Notice. A person who became a member of the Fund by paying a fee would have to give the DLEG division that administers the Fund written notice of a change in the person's name, address, or form of business organization within 30 days of the change. Proof that a notice or other document was mailed or, if another method of delivery were required by law or rule, delivered by that method to a member at the last address that the member gave the Fund administrator, would be conclusive proof that the member received the notice or document.

At least 30 days before a renewal payment was due, DLEG would have to send a notice of the amount that would be due and the payment due date to the laborer or other lien claimant who paid the fee. The notice would have to be sent by ordinary mail to the last address that the person gave the Fund Administrator.

Additional Assessments. Under the Act, if the Fund balance is under \$1.0 million on December 1 of any year, the DLEG Director may require an additional assessment or payment, not to exceed \$50, from licensed contractors and other lien claimants, unless the Legislature adopts a concurrent resolution to prohibit the additional assessment within 30 legislative days after the Director requires the assessment. The bill would delete this provision.

Assessment Cap. Currently, a person may not be assessed more than \$50 in an assessment period regardless of the number of licenses applied for or held. The bill would delete this provision.

### Fund Expenditures

Under the Act, wages, professional fees, and other administrative expenditures necessary for the operation of the Fund may not exceed 20% of funds collected by the Fund in the previous fiscal year. If, however, the \$50 fee is not assessed against license applications and renewals during a year, the limitation on Fund expenditures must be calculated on the basis of the closest previous year in which the \$50 fee was assessed and collected.

The bill provides, instead, that except for legal counsel fees, the amount paid in a fiscal year for wages, professional fees, and other administrative expenditures could not exceed 20% of the average of the ending balances in the Fund for the previous two fiscal years.

### Recovery from the Fund

The Act provides that a claim of construction lien does not attach to a residential structure, to the extent payments have been made, if the owner or lessee files an affidavit with the court indicating that he or she has paid the contractor for the improvement and the amount of the payment, has not colluded with any person to obtain a payment from the Fund, and has cooperated with DLEG in the defense of the Fund. The bill would require the owner or lessee also to attach to the affidavit a copy of any evidence of the payment that he or she had, including a canceled check or a credit card or other receipt.

A person who has recorded a claim of lien and who is precluded from having a construction lien under the previous provision, may recover from the Fund the amount for which the lien is established. Under the bill, the person could recover the amount he or she would have been entitled to recover but for the previous provision. The Act requires a person seeking recover to establish various facts, including that he or she would be entitled to a construction lien on a residential structure except for the defense described above. The bill also would require the person to establish that the contractor or subcontractor with whom the person claiming the construction lien contracted was the same individual or legal entity with whom the owner or lessee contracted.

In addition, if the person claiming the construction lien were a supplier, the person would have to establish that he or she had documentary proof that, before the person provided the material or equipment that was the subject of the lien without obtaining advance payment in full, he or she exercised due diligence to determine that the contractor or subcontractor to whom the person provided the material or equipment was creditworthy.

### Interest

After the bill's effective date, a construction lien of a subcontractor or supplier for an improvement to a residential structure could not include an amount charged or assessed

under the contract between the subcontractor or supplier and the general contractor for interest on the unpaid principal amount due, a time-price differential, a finance charge, or any other item of interest.

The bill also specifies that a payment from the Fund could not include an amount for interest on the unpaid principal amount due, a time-price differential, a finance charge, or any other form of interest.

### Maximum Fund Payment

Currently, DLEG may not pay out of the Fund to subcontractors, suppliers, and laborers more than \$75,000 per residential structure. When it appears that the amount claimed from the Fund with respect to a residential structure will exceed that amount, DLEG may delay payment until the total amount to be paid can be ascertained. If the total amount payable to subcontractors, suppliers, and laborers exceeds \$75,000, they must be paid their proportional shares of that amount. The bill would increase the \$75,000 cap to \$100,000.

MCL 570.1104 et al.

Legislative Analyst: Suzanne Lowe

### **FISCAL IMPACT**

The bill would change the revenue stream for the Homeowner Construction Lien Recovery Fund, a restricted revenue fund with the Department of Labor and Economic Growth. Currently, the revenue to the fund consists of fees and special assessments. Residential builders and contractors pay a \$50 fee to the Fund at the time of applying for their initial licenses. Special assessments may be levied at a rate of \$50 per licensed contractor. The special assessments are levied at the direction of the Director of the Department of Labor and Economic Growth when the balance in the Fund falls below \$1,000,000 as of December 1 of any year. The most recent special assessment was levied in FY 2004-05 and, if fully collected, will generate approximately \$4.7 million for the Fund.

Under the bill, the authority for special assessments and the initial license fees would be eliminated. Instead, a fee would be levied with the renewal of residential builder and contractor licenses. The fee would be \$10 for each year the license was in effect. Revenue from these fees is estimated at \$950,000 annually.

The bill also would prohibit the Fund from making any payments for finance charges on amounts recovered through the Fund. This is expected to reduce the expenditures from the Fund. The bill would increase the maximum payment from the Fund for any single residential unit from \$75,000 to \$100,000.

It is expected that administrative expenses would be reduced by the bill because collection of fees would be done in conjunction with regular license renewals, instead of requiring separate mailing and processing as with the special assessments.

The Fund has paid an average of approximately \$511,800 annually over the past five years for judgments and an average of \$408,710 annually for legal costs. The balance in the Fund as of March 2005 was \$3.54 million.

The bill would have no impact on the State's General Fund revenue or expenditures.

The bill would have no fiscal impact on local government.

Fiscal Analyst: Elizabeth Pratt

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.