Managing Construction Credit and the Importance of Obtaining Job Information

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Five Cs of Credit

**Character**  The creditability of your customer.
**Capacity**  Your customer's ability to manage their business.
**Conditions**  The internal and external forces that we need to know about that affect the customer's business.
**Capital**  The customer’s worth.
**Collateral**  Property pledged as a security to pay an obligation or loan.
Thomas Jefferson first introduced the Mechanic’s Lien Act in 1791 to encourage construction for what would be the nation’s capital in Washington, D.C.

If you reduce risk, you can sell more

$5,000 credit line
14% Interest rate

$500,000 credit line
4% Interest rate

Collateral
$15,000 write off on an order with 3% margin

Sales has to generate $500,000 in new business to offset that loss

Lien rights in all 50 States

Lien rights are unique to the construction industry.
Construction Credit has *unique* terminology:

- Retainage
- Back Charge
- Pay if Paid

Construction Credit has *unique* payment objections

I can't pay you ... I haven't been paid!
Construction Credit is Unique

Bank
Owner
GC
Material Supplier
Service Provider
Material Distributor
Sub
Sub
Sub
Property
Liens are a defined right

1. Be within 3 tiers of the owner.

2. Goods must be affixed, nailed, glued, bolted, painted on, etc.

3. No suppliers to suppliers.
2. Goods must be affixed, nailed, glued, bolted, painted on, etc.

3. No suppliers to suppliers
Your customer must complete the installation of your product and/or be directly using your service (i.e. trash removal).
State Requirements at-a-Glance

List of First Furnishing States
List of Direct to Lien States
List of Dollars Required on NTO's
List of List of Full Price and Unpaid Balance Lien States
List of Immediate Action States
List of Notice of Commencement States
List of Notice of Completion States
List of Remote Contractors States
List of Construction Trust Fund States
List of Pay if Paid Clause Enforceable
List of State-by-State Contractor's License Requirement

List of Rights for Suppliers to Suppliers

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Suppliers to Suppliers have limited lien rights based on type of project, state statute and case law.

<table>
<thead>
<tr>
<th>State</th>
<th>Private</th>
<th>Public</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>No rights</td>
<td>No rights unless considered subcontractor, materials are fabricated and large part of the main contract. See: Sparks Construction, Inc. v. Newman Brothers, Inc., 288 So. 2d 749.</td>
</tr>
<tr>
<td>Alaska</td>
<td>No rights</td>
<td>No rights</td>
</tr>
<tr>
<td>Arizona</td>
<td>No rights</td>
<td>No rights</td>
</tr>
<tr>
<td>Arkansas</td>
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| Oregon | Rights when material is part of the improvement. | May have rights, statute is not clear. |

Construction Credit is Unique

- Bank
- Owner
- Property
- IF
- GC
- Sub
- Sub
- Sub
- Material Supplier
- Service Provider
- Material Distributor
- IF
- IF
- Might
Securing Lien Rights typically requires 3 steps:

1. Preliminary Notice
2. Lien/Bond
3. Suit/Foreclosure

Construction Credit is Unique
The Preliminary Notice is the foundation on which Mechanic’s Lien rights are built.

What does a notice look like?
To whom should you send the notice?

STS Advice:

Regardless of the statute, send a copy to every party you can identify.

States Requiring Preliminary Lien Notices:

<table>
<thead>
<tr>
<th>Alabama</th>
<th>Massachusetts</th>
<th>Oklahoma</th>
</tr>
</thead>
<tbody>
<tr>
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<td>Michigan</td>
<td>Oregon</td>
</tr>
<tr>
<td>Arkansas</td>
<td>Minnesota</td>
<td>Pennsylvania</td>
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<tr>
<td>Arizona</td>
<td>Mississippi</td>
<td>South Carolina</td>
</tr>
<tr>
<td>California</td>
<td>Missouri</td>
<td>South Dakota</td>
</tr>
<tr>
<td>Florida</td>
<td>Montana (public)</td>
<td>Tennessee</td>
</tr>
<tr>
<td>Georgia</td>
<td>Nebraska</td>
<td>Texas</td>
</tr>
<tr>
<td>Indiana (Commercial)</td>
<td>Nevada</td>
<td>Utah</td>
</tr>
<tr>
<td>Iowa</td>
<td>New Hampshire</td>
<td>Virginia (residential)</td>
</tr>
<tr>
<td>Kansas</td>
<td>New Jersey (residential)</td>
<td>Washington</td>
</tr>
<tr>
<td>Kentucky</td>
<td>New Mexico</td>
<td>West Virginia</td>
</tr>
<tr>
<td>Louisiana</td>
<td>North Carolina</td>
<td>Wisconsin</td>
</tr>
<tr>
<td>Maryland</td>
<td>North Dakota</td>
<td>Wyoming</td>
</tr>
<tr>
<td></td>
<td>Ohio</td>
<td></td>
</tr>
</tbody>
</table>
Full Price vs. Unpaid Balance

Full Price Lien States

Lien rights are not limited to unpaid funds between the owner and prime contractor. By timely and accurately serving a notice to owner and timely and accurately filing a mechanic's lien the owner is subject to double jeopardy (paying twice).

Unpaid Balance Lien State

Lien rights are limited to unpaid funds between the owner and prime contractor. Once funds are paid to the prime contractor subsequent liens would be ineffective. The serving of a notice to owner or the filing of a lien (in a direct to lien state) generally traps unpaid funds between the owner and prime contractor.
Securing Lien/Bond Rights typically requires 3 steps

1. **Preliminary Notice**
2. **Lien/Bond Claim**
3. **Suit/Foreclosure**

What about the other States?

*Non-Statutory Notice!*

Looks like a notice

Gets you paid like a notice
Use notices to:

• Make yourself visible
• Explain what the notice is /why you’re sending it
• Invite corrections to inaccurate/missing information
• Solicit conversation to resolve disputes
• Improve cash flow

Private = Liens
Residential
Commercial

Public = Bonds
City
State
County
Municipality
Verifying all parties and addresses is critical

You’re justifying the $40,000 order against the property value

Property is worth $400,000,000

$40,000 job order
Customer is worthy of a $5,000 credit line

Property is worth
$400,000,000

You’re justifying the $40,000 order against the property value
Let’s break this job information sheet down.

Project Information: What Type of Project?

Project Type/Who’s the Owner?

Public
If the land being improved is "Public" the owner is state or county or a city (municipality). These projects are not subject to the mechanic’s lien laws, they’re subject to state bond claim laws.

Private Projects
If the land being improved is "Private" the owner is an individual, partnership or corporation. These projects are not subject to the state bond claim laws, they’re subject to mechanic’s lien laws.

Federal
If the land being improved is "Federal" the owner is the Federal Government. These projects are not subject to the state bond claim or mechanic’s lien laws, they’re subject to Federal Miller Act.

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When your customer is the owner:

It begins and ends with the owner.
Your rights against the owner are not limited to the property

Direct to Lien Rights
- Residential: you may have issues with homestead exemption
- Unsecured; sue for breach of contract using the Little Miller Act
- Unsecured; sue for breach of contract using the Federal Miller Act

When your customer is the General Contractor (GC):

Know who the property owner is ...
Because the property owners determines the type of project and what laws to follow

Private: verify the property address and verify who owns it

Public: verify the property owner and bonding information
When your customer is a subcontractor:

Obtain and verify the general contractor information (who hired your customer?)

Obtain and verify the owner information

If the property owner is public, think Miller Act or Little Miller Act and obtain and verify bonding information

If you have a contract with a subcontractor versus the general contractor, sometimes, that subcontract ties you into terms and conditions of the general contract.

When your customer is a Material Supplier:

Material Supplier means any entity that supplies materials, services, or equipment to be used in conjunction with the performance of work on a construction contract. [Law Insider definition]
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Leasehold interest is a legal right acquired by an individual or corporation to use certain property for a limited period of time. It is an official claim obtained through a lease arrangement to use an asset.

Either the property owner or the leaseholder can engage the work.

Did the tenant commission the work with the knowledge of the owner?

If the tenant commissioned work with the knowledge of the owner, you’ll be able to lien on the leasehold interest only.

If the owner forced the tenant, by contract, to do the work, and the contract can be verified, you’ve have a potential for lien rights.

You are only going against the leasehold interest of the party.

Lien on leasehold interest is not a security interest in the property. It puts pressure on the landlord and the tenant to uncloud the leasehold lien.

When your customer has a Leasehold Interest:

If your customer is a Public Private Partnership or a P3:

A project built on public land with private money and private control would only protect subcontractor payment if the P3 contract documents required it or, if the P3-enabling law mandated a payment bond be furnished on all P3 projects to ensure subcontractors and suppliers be paid for labor and materials furnished.

Though a mechanic’s lien is available against a private party’s leasehold interest in public property, such liens may have limited value and be difficult to enforce. A P3 project is potentially lienable if the property was transferred from the government to the private operator.
If your customer is a sub-subcontractor:

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Remote Contractors States

Remote contractors are defined as suppliers and labors 4 tiers (or lower) removed from the owner and does not include suppliers to suppliers.

States Providing Lien Rights To Remote Contractor:

Arizona – Private
Colorado
Connecticut
Hawaii
Idaho
Illinois
Iowa – Private
Kentucky
Louisiana
Maine
Maryland
Massachusetts
Michigan – Private

Missouri
Nevada
New Mexico – Private
New York – Private
North Carolina – Funds Only
North Dakota
Oregon – Public
South Carolina
Tennessee – Commercial
Utah
Vermont
Washington
Wisconsin
If your customer is a Commercial Useful Function Verified

The distinctive marks of a commercially useful function may include the DBE’s performance of tasks such as:

1. sourcing materials;
2. negotiating price;
3. verifying that the quality and quantity of materials meet contract requirements;
4. purchasing and making payment for materials from the DBE’s own funds;
5. warehousing materials;
6. scheduling the delivery of materials; and
7. invoicing for the materials. It is important to note that certification of the DBE is not determinative since certification focuses squarely on ownership status and control structure of the company.

Common indicators of sham DBEs include:

1. when the DBE firm works for only one contractor;
2. the work is outside of the DBE’s known experience or capability;
3. the volume of work is beyond the DBE firm’s capacity;
4. the DBE does not maintain a store or warehouse where products are bought, stored and sold to the public;
5. the DBE does not generally purchase and sell the materials being supplied; and
6. the DBE does not supply materials to a non-DBE goal project.

At a basic level, the distinctive marks of a commercially useful function may include the DBE’s performance of tasks such as:

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Knowing the location and type of project are two of the biggest factors when starting the lien or bond process.

The location of the project will generally tell creditors which statute to follow, while the type of project (residential or commercial and private or public) will typically let creditors know what type of security they need to file.

Among the items spelled out in statute are timeframes for filing certain documents, such as preliminary notices and the actual filing of the lien, as well as what information needs to be included—general contractor name, addresses, supplier name, etc.

Who Gathers job information?

- **Sales**: Bank, Owner, Sub, Material Supplier, Service Provider
- **Credit**: GC, Sub, Material Distributor
Recent Poll:

71% said Sales gathers information

18% said Credit gathers information

11% said combined effort of Sales and Credit

Miller Act - Federal Projects

Establishes a threshold of $100,000 - $150,000.
DOD sets time frames for filing

Little Miller Acts - State Projects

Moves thresholds and time frames
1. **Ask for and get a copy of the bond up front**
   
   Timetables are short and it’s a friendlier time. Be sure to read the bond.

2. **Bonding companies make money by collecting premiums**
   
   Claims come in two buckets.

3. **Suits are prevalent**
   
   DSOs are extended.

4. **Bond Assessment**
   
   A.M. Best, Federal Treasury List
   
   [https://www.fiscal.treasury.gov/surety-bonds/list-certified-companies.html](https://www.fiscal.treasury.gov/surety-bonds/list-certified-companies.html)

5. **Who can you trust?**

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**Examples**

A supplier to supplier has no rights to pursue the Miller Act payment bond.

Another important reason to know where you are in the tier on the job is that the rights against the Miller Act payment bond cut off at the second tier.

You count the tiers starting below the general contractor, so the subcontractor(s) contracting with the general contractor are tier 1 and any sub-subcontractor or material supplier contracting with the subcontractor is tier 2.

The danger usually comes into play when a supplier is contracting with a sub-subcontractor as that makes the material supplier tier 3 and below the cutoff line.

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“Knowing the right detail gets you a great return. Ignore them and you just crash and burn.”

Robert Rolih
It may appear that some companies offer you a low rate for Notice-to-Owner services. But is the advertised cost the true invoice cost? Let's see...

Some companies charge you a priority fee. **WE DON’T.**

Some companies charge you more for larger projects. **WE DON’T.**

Some companies charge you for incomplete information. **WE DON’T.**

- We post our prices online.
- You get the support of prior experienced construction professionals.
- We have live people researching every job.
- We’ll verify your project’s address to confirm ownership making sure your notice gets to where it needs to go so you’re secured.
- We are there to help and answer your questions through the entire complicated process.

Never be caught unsecured on construction projects. Let NACM Secured Transaction Services do the work and know that your project is being handled with care.

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**WE GOT PAID ON TIME!**
Access to Everything, Anytime!

Whether sitting in a plane, stuck waiting in a reception room or relaxing at home, the new FREE Business Credit App makes keeping up-to-date with the latest news about commercial credit a breeze.

Stay informed with all of NACM's and FCIB's editorial content in one place. That's Business Credit magazine, FCIB's Web in Review, NACM’s blog and the daily Strategic Global Intelligence brief by NACM Economist Chris Nash, Ph.D. all right there at your fingertips!

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