Construction Law Newsletter

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MESSAGE FROM THE CHAIR

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The Construction Law section continues its focus on member outreach and education in 2013.

First, the Section website, *www.osbarconstruction.com*, posts quite a bit of information, including the Section newsletter, upcoming events, useful links, a member directory and meeting minutes. It can be a valuable resource. The member directory is linked to the Oregon State Bar's directory, so if you update your information there, we should have the update as well.

Second, the section newsletter, published three times a year, includes discussion of current legal issues affecting members practicing construction law. Past newsletters are archived on the website and are searchable. Board members contribute to the newsletter as part of their service to the section and the results are always informative and useful. Thanks to all our board members for their hard work and to Alan Mitchell, our long-time editor.

Third, the Section continues its "brown bag" series of free CLEs. They are usually hosted in the Portland metropolitan area, but we are exploring to see if they can be recorded and placed on our website.

Fourth, for the past couple of years the Section has put on CLEs in both Bend (twice) and Eugene (once). This was an effort on our part to reach out to our membership, as well as other attorneys interested in the area, beyond the Portland metropolitan region. In general, the CLEs were well attended and the Board received positive feedback from those attending.

For this year, we are not putting on any regional CLEs in Eugene and Bend because other CLEs sometimes cover the same material and because we believe we may have saturated our market for the time being. We are open to considering CLEs in southern and eastern Oregon as well as on the coast, if enough interest from our members is expressed. We are also interested in receiving feedback from our membership in that area as to how we might serve you better.

This past year saw increased activity from section members in regard to construction legislation, as members of the Board were asked to comment or assist on the legislation. Any activity that involves the Section's imprimatur is coordinated and blessed by the Bar as a whole. In addition, the Section rarely takes substantive positions on bills because the section's membership represents such a diversity of different clients and views. Often our input is simply for clarification purposes only. Board members, of course, are permitted to offer their own personal opinions on such bills.

[1] The comments in this article reflect my personal opinions and do not represent official policy of the City of Portland.

Finally, every other year the Section holds a half-day CLE focused on practice before the Construction Contractors Board. Following that tradition, we will hold a half-day CLE on the CCB on December 7, 2012 at the Oregon State Bar Center. Our annual meeting will be held at noon following the CLE. More information about this CLE will be forthcoming.

I welcome your participation in the section. Please feel free to send any thoughts or suggestions to me or any of our other board members (whose names are listed below and are also posted on our website).

UPDATE ON OREGON'S PRIVATE PROMPT PAYMENT ACT

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Oregon Revised Statutes 701.620 through 701.645 are known as the Private Prompt Pay Act (the "Act"), and became effective in Oregon on January 1, 2004. As the name suggests, the statute mandates a schedule for payments on construction contracts. The Act's primary purpose is to ensure that the contractors, subcontractors, and material suppliers are paid on a regular and predictable basis throughout the life of a construction project.

The Oregon legislature amended the Act in 2011 in several respects. The revisions apply to private construction contracts entered after January 1, 2012. This article briefly reviews the Act and discusses the recent revisions.

The Act

The Act mandates a payment schedule for private constructions contracts that are expected to take more than 60 days to complete. The owner of the project must make a progress payment within 14 days of receiving a monthly invoice from its original contractor. The original contractor must pay the invoices of its subcontractors and material suppliers within 7 days of receiving payment from the owner. The owner must pay the final invoice no later than 7 days after approving the work.

The Act provides nine bases for an owner to decline all or part of an invoice. The reasons must be stated in writing within 10 days of receiving the invoice. An owner may also withhold amounts required to pay for curing the problems identified in the written response to the invoice, and a contractor may do the same when responding to an invoice of its subcontractors and material suppliers. If the owner does not provide a written response within 10 days, then the invoice is considered certified, and the owner must pay the full invoice price within 14 days of receipt.

The Act further provides remedies when owners and contractors fail to make timely payments. A contractor is entitled to interest at 1.5% per month on invoice amounts that are not paid within 14 days of submission.

If an owner fails to pay, a contractor may suspend work after providing notice and allowing 7 days for the owner to make the payment. If work is suspended for more than one month, the contractor may terminate the construction contract.

Similarly, a subcontractor may suspend work if the owner pays the contractor, but the contractor does not timely pay the subcontractor, or if the owner refuses to pay the contractor based on problems that do not involve the subcontractor's work. Subcontractors must also give 7 days' notice of suspension of the work, and may terminate the contract if work is suspended for a month.

2011 Amendments to the Act

Any alternate billing cycle must be identified in the contract and noted on each page of the drawings and specifications. Any such disclosure on the drawings and specifications may be made "on either side of the page." ORS 701.625(7).

Another change appears to prohibit a party from forcing a lower tier contractor to contract away its right to prompt payments. A new sentence in ORS 701.625(8) states that "A construction contract may not be changed in a manner that alters the right of any subcontractor or material supplier to receive prompt and timely progress payments pursuant to [the Act]."

The legislature has also narrowed the scope of instances in which a party may collect attorney fees. Former ORS 701.625 and 701.630 stated that the prevailing party was entitled to its attorney fees on actions "to collect payments or interest," but both were revised to now only allow for attorney fees on actions "to collect interest." The statute no longer entitles a prevailing party to its attorney fees for actions to collect outstanding payments.

Finally, the revised Act also corrects a former omission whereby parties were free to contract for an alternative payment arrangement, but were not free to change the schedule for the final payment. The revised Act now allows parties to alter the schedule for final payment as well as the progress payments.

WORKERS' COMPENSATION: EMPLOYER-PROVIDED VEHICLES, AND TRAVEL TO WORK

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In a recent workers' compensation ruling (Kimberly K. Mitchell WCB No. 11-02713), a worker who was injured in a multiple vehicle accident on her way to work before her shift began was nonetheless found entitled to have a legitimate workers' compensation claim. Typically, injuries that occur while commuting to work are not covered by workers' compensation benefits (this is the "going and coming rule") because there is no active employment relation and the employee is not yet providing a service for the employer. There are exceptions to this rule, notably the "employer conveyance" rule, which can bring employees back into the employment relationship for purposes of workers' compensation coverage.

While this worker did not fit the usual parameters for the employer conveyance rule (typically the employer has direct control such as providing interim transportation out to a work site), the administrative law judge worked through a detailed analysis of the facts in the case to determine whether the worker met the two-pronged work connectedness test, such that the circumstances of the injury arose in the course of employment and arose out of employment.

The salient facts are that the worker was driving a company truck, issued to her as a perk after her first year of employment. The truck had the employer's logo on it and was loaded with the type of equipment the employee would use throughout the day as a utility locator. The worker was allowed to drive the truck to work and home, and of course use the truck during the work day, but was not allowed any other personal use of the truck. The company maintained the truck, provided auto insurance, and provided a company gas card for the truck.

The morning of the accident, the worker's route to work was a direct one from her home to the employer. She deliberately overshot her normal freeway entrance in order to first fill the truck with gas. On her way to the gas station, a Tri-Met bus hit her truck. The timing of this accident was well before her work shift started and, had there been no accident, the employee would have been at work, as usual, about 15 minutes before her shift.

These facts led the administrative law judge to conclude the injury occurred "in the course" of employment. The employer would have expected the worker to fill the truck with gas throughout the week, and the employer exerted some control by providing a gas card that directed the worker to specific gas stations. The fact that the worker was not yet on the clock was not dispositive, partly because the worker's choice to fill the truck on the way to work benefitted the employer (the worker would arrive ready to go and did not have to take time out of the work day to fuel the truck). The employer would have a reasonable expectation that the worker would be in the location where she was hurt, as again the employer provided company gas cards and the gas station was extremely close to the worker's normal route to get to the job.

Another factor that supports whether or not an injury is in the course of employment is whether or not the employer had some control of the situation. In this instance, the worker called the employer immediately, as per protocol for work injuries. Her employer advised her that they would handle any interactions with Tri-Met, and her manager came out to the accident site. The manager drove the worker to the emergency room and then on to work, and made arrangements for the damaged vehicle.

All of the above considerations led the administrative law judge to conclude that the "course of employment" prong of the work connectedness test had been satisfied.

Next, it was necessary to evaluate whether or not the injury "arose out of" employment, such that the risk of injury resulted from the nature of work or from some risk that would be found in the work environment. Put another way, the question is whether the employee's work exposed her to the type of conditions that put her in a position to be injured.

In this case, the administrative law judge felt the worker's employment exposed her to conditions that put her in the position to be injured in the manner in which she was injured. The worker's use of the company vehicle for commuting to work, and her practice of filling the truck with gas prior to clocking in to be ready for work when her shift began, was acquiesced in, beneficial to, and financially supported by the employer. The employer expected its workers to be at certain gas stations to fill the company truck (by providing the gas cards instead of allowing the employees pick the gas providers and seek reimbursement). The employer would have no reason to protest the location of the worker at the time of the accident.

Thus, the circumstances of the injury led the administrative law judge to find that the injury was sufficiently connected to work, satisfying the "in the course" prong of the test, as well as "arising out of employment" portion of the test, thus making the injury work connected.

Important Note: This is an Opinion and Order, and is unpublished. This case is currently under appeal.

CONSTRUCTION LIEN NOTICES TO MORTGAGEES JUST GOT A LITTLE SIMPLER

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Oregon's construction lien statutes, ORS 87.001, *et seq.*, require a lien claimant to send certain notices to any "mortgagee" that holds an interest in a mortgage or trust deed on the real property that is subject to the claimant's construction lien. In some instances a material supplier must serve the "mortgagee" with a prelien notice under ORS 87.025, in order for the material supplier to maintain priority of its construction lien over the mortgagee's interest in the improvement. Further, under ORS 87.039 and 87.057, lien claimants must send the mortgagee (and owner) notice of filing and intent to foreclose the claim of lien in order to preserve the right to an award of attorney fees, costs, and disbursements.

Prior to January 1, 2012, the term "mortgagee" simply meant the person or entity who held a valid mortgage or trust deed of record securing a loan upon the subject land or improvement. The statutory mortgagee was often the lender identified as the holder of the mortgage or the beneficial interest under a trust deed recorded against the property.

For some time, there has been a rise in lenders selling their interests in the loans. Thus, a loan may be sold, and its related mortgage or trust deed may be assigned, a number of times. To avoid the administrative burdens of recording multiple assignments of trust deeds, lenders often designate Mortgage Electronic Registration Systems, Inc. ("MERS") to act as the beneficiary under the trust deed solely as the nominee for the lenders and the lender's successors and assigns.

When MERS is identified in the public records as the trust deed beneficiary, the owner of the promissory note for the underlying loan may not be identified in the public records. Lien claimants did not always know whether providing notice to MERS as the "mortgagee" satisfied the statutory requirements of ORS 87.001, *et seq*. Under those circumstances, and without knowing the identity of the promissory note holder, lien claimants were faced with a challenge to comply with the construction lien statutory notice requirements.

In 2011, the Oregon Legislature clarified the "mortgagee" notice requirements to meet the reality of MERS, thus alleviating these concerns. Oregon Laws 2011 Chapter 505 made changes to several statutes (including ORS 87.005 and ORS 87.018) to require that notices to the "mortgagee" under ORS 87.001 to 87.060 or 87.075 to 87.093 need only go to the person (or entity) whose name and address appear in the public records as the mortgagee, trust deed beneficiary, or the assignee. Thus, if MERS is the only trust deed beneficiary identified in the public records, the required statutory notices need only go to MERS.

Notwithstanding, if the lien claimant knows the identity of the current holder of the loan secured by the MERS mortgage or trust deed, it is good practice to send courtesy copies of the lien notices to such lender, as it may increase the chances of getting paid prior to foreclosing the lien claim.

STONEWOOD DESIGN V INFINITY HOMES: COURT PLACES SUBSTANCE OVER FORM RE: LIEN RELEASE BONDS

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The Washington Court of Appeals recently decided the case of *Stonewood Design, Inc. v. Heritage Homes of Wa dba Infinity Homes, et al*, 164 Wn. App. 1034 (2011) (published on January 17, 2012). The court's decision (referenced herein as *Stonewood v. Infinity*) provides clarity to Washington's statute governing release of lien bonds, and clarifies the Court of Appeal's holding in an earlier case. This article discusses *Stonewood v. Infinity*, and discusses the language of Oregon's release of lien bond statute in comparison to Washington's release of lien bond statute.

In *Stonewood v. Infinity*, the general contractor Infinity contracted with Stonewood for Stonewood to install tile in a home. Stonewood performed the work and billed Infinity in an amount slightly over $30,000. Infinity withheld approximately $9,000 from Stonewood, claiming that some of the tiles were chipped and needed to be replaced.

The parties' attempts to resolve the dispute were unsuccessful. Stonewood filed a construction lien for the contract balance and then sued to foreclose the lien. Stonewood's lawsuit included a claim against Infinity for breach of contract and a claim against Stonewood's contractor's registration bond.

The defendant homeowners posted a release of lien bond under RCW 60.04.161 and obtained release of the Stonewood lien.

In the lawsuit, Infinity contested Stonewood's claim for foreclosure on the release of lien bond, and asserted a counterclaim against Stonewood for Infinity's alleged costs to repair the tile work.

At trial, the jury awarded damages to Stonewood for the approximate $9,000 sum withheld by Infinity, and rejected Infinity's claim for offset.

In post-trial proceedings, Infinity argued that Stonewood's lien was invalid. The court rejected that argument and held that Stonewood had "proved the facts necessary to execute upon the release of lien bond." The court entered judgment in favor of Stonewood for the amount of the jury verdict.

The court's judgment provided in part that Stonewood was "entitled to execute" on the release of lien bond, as well as on Infinity's contractor's registration bond because Stonewood "prevailed in its breach of contract action against Infinity."

Infinity's primary argument on appeal was that Stonewood had not obtained a "judgment upon the lien" under the language of RCW 60.04.161 and therefore the trial court had erred in allowing Stonewood to execute on the release of lien bond.

The relevant language of RCW 60.04.161 provides that "[T]he condition of the bond shall be to guarantee payment of any *judgment upon the lien* in favor of the lien claimant entered in any action to recover the amount claimed in a claim of lien, or on the claim asserted in the claim of lien." (*Emphasis added*).

On appeal, Infinity placed much reliance on the Court of Appeals' decision in *DBM Consulting Engineers, Inc. v. United States Fidelity & Guaranty Co.*, 142 Wn. App. 35 (2007), in which the court held that a release of lien bond guaranteed payment only where there is a "judgment upon the lien" not merely a judgment on the underlying claim.

The court found that the *DBM* case was distinguishable. In *DBM*, the lien claimant had obtained a judgment against the owner for breach of contract, but had not pursued its claim for foreclosure of the construction lien that it had asserted. Instead, the lien claimant filed a second lawsuit naming the bonding company and seeking payment from the release of lien bond that had been posted. The parties had not litigated the validity of the construction lien.

Infinity argued on appeal that since the trial court's order did not specifically state that Stonewood's construction lien was foreclosed, the order did not obligate the surety to pay the lien under the release of lien bond. The court held that Infinity's argument "elevates form over substance", and stated further that "*DBM* does not impose vocabulary requirements for judgments." The court noted that what is required under the *DBM* case is that the construction lien must be litigated before execution on a release of lien bond is appropriate. The court reasoned that litigating the validity of the underlying lien preserves the link between the lien and the release of lien bond.

In affirming the trial court, the Court of Appeals held that because Stonewood had established the validity and enforceability of its lien, the trial court was correct in authorizing execution on the release of lien bond.

Oregon's statute regarding release of lien bonds, ORS 87.076 (1), requires that a release of bond shall provide for payment of the claim and all costs and attorney fees that are awarded against the land and improvement "on account of the lien." Although there are no reported appellate cases in Oregon construing this language, it is reasonable to conclude that such language requires, as does Washington's statute, that the validity and enforceability of the construction lien be established in order for there to be execution on the release of lien bond.

It is also reasonable to conclude that an Oregon appellate court would look to the substance of the trial court's decision in a construction lien case where other claims have been adjudicated, and as with the *Stonewood v. Infinity* court, not "impose vocabulary requirements for judgments." However, in light of the lack of appellate court precedent in Oregon on this issue, an Oregon lien claimant should include language in the judgment and decree of foreclosure that specifies in substance that the lien was found to be valid and enforceable, and that the judgment and decree is on account of the lien.

MERS UNCERTAINTY CONTINUES

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In the June 2011 Issue of the Construction Law Newsletter, Katie Jo Johnson of McEwen Gisvold LLP provided the section with an update on the most recent cases and legislation related to Mortgage Electronic Registration Systems, Inc., ("MERS"). Since the June Issue, there have been a slew of new cases related to MERS that have added to the uncertainty about how the Courts will treat MERS issues going forward.

Recent MERS Cases: Since the *Hooker* opinion described in the June 2011 issue, the MERS decisions coming out of the Oregon District Court have taken a turn and have been much more favorable to MERS. *Hooker* stood for the propositions that 1) a MERS loan is inappropriate for the non-judicial foreclosure process because MERS is not the actual beneficiary and 2) there needs to be recorded assignments reflecting every change in lender/beneficiary. However, the more recent decisions coming out of the District Court are finding that, contrary to Judge Panner's reading of the statues in *Hooker*, MERS can rightfully be named as a beneficiary under the Oregon Trust Deed Act and that not all assignments need to be recorded in order to foreclose a deed of trust. These contrary findings can be found in the following decisions:

In *Beyer v. Bank of Am.,* 800 F. Supp. 2d 1157 (D. Or. Aug. 2, 2011), Judge Mosman was asked to determine whether MERS was a proper beneficiary under the Oregon Trust Deed Act. The Court noted that "because MERS is named in the trust deed as the beneficiary, which is to say the person for whose benefit the trust deed is given, state and federal courts have found that MERS is the beneficiary under Oregon law." *Id.* at 1160. It was also noted that other courts, including the court in *Hooker,* have found that "despite clear language declaring MERS the beneficiary," the lender was the actual beneficiary under the Oregon Trust Deed Act. The *Beyer* court determined that it did not need to resolve this dispute and found that MERS was both named and "designated" as the person receiving the benefit. *Id.* at 1160-1161.

Construing ORS 86.705(5), the Court found that the purpose of a trust deed is to secure the performance of an obligation owed to the beneficiary, and therefore, the "benefit" of a trust deed is that the obligation is fulfilled. *Id.* at 1161. Because the trust deed granted MERS the right to exercise all rights and interests of the lender if necessary to comply with law or custom, and the trust deed repeatedly calls MERS the beneficiary, calling MERS a beneficiary would not comply with law or custom unless MERS's powers were expanded to include the right to receive payment of the obligation. Therefore, MERS has the right to receive payment and is both named and designated beneficiary.

In the same month as *Beyer* was decided, Magistrate Judge Janice M. Stewart, relying heavily on Judge Mosman's opinion in *Beyer*, handed down her decision in *James v. Recontrust Company*, 2011 U.S. Dist. LEXIS 101139 (D. Or., August 26, 2011) and also found that MERS was a proper beneficiary under Oregon law. *Id.* at 18-26. The deed of trust in *James* contained the same language as in *Beyer,* naming MERS as the beneficiary and giving it a broad scope of authority to act as an agent on the Lender's behalf. According to the Court, that was enough to satisfy the Oregon Trust Deed Act.

Additionally, the *James* court was asked to determine whether all assignments of the deed of trust were properly recorded under Oregon law. Here, what seemed to be a trend of requiring all assignments to be recorded under the Trust Deed Act was reversed and the Court held that "nothing in Oregon law requires recording of each assignment of the trust deed when the underlying note is transferred." The Court noted that the only recording requirement is found in ORS 86.735(1) and requires recording of all "'assignments of the trust deed by the trustee or the beneficiary' before a non-judicial foreclosure by advertisement and sale." *Id.* at 29. The Court drew a distinction between recording assignments of the actual trust deed itself, and assignments of the promissory note that the trust deed secures even though, as the Court admits, "a transfer or assignment of the note transfers the security interest for the protection of the beneficiary." *Id.* at 30. The Court's holding on the assignment issue was directly contrary to the Court's holding in *Hooker.*

Finally, in the recent decision of *Stolz v. OneWest Bank*, 2012 U.S. Dist LEXIS 8141 (D. Or., January 13, 2012), Magistrate Judge Dennis J. Hubel continued the recent trend and found that, because the trust deed named MERS as the beneficiary and MERS had the right to receive the benefit of the trust deed, MERS was a proper beneficiary under the trust deed. *Id.* at 36. Judge Hubel also agreed with Judge Stewart's findings that ORS 86.735 only requires the recording of assignments by the parties who have a recorded interest in the real property providing security, that is, the trustee or the beneficiary. *Id.* at 36-38. A recording of transfers of the note is not required. *Id.* If MERS remains the beneficiary to act for the lender and its successors and assigns, even if the note was sold, MERS does not need to record. *Id.*

While these most recent cases have sided with MERS, the Oregon District Court and the Oregon Bankruptcy Courts are still divided as it relates to what the Oregon Trust Deed Act requires. As Judge Stewart noted in *James*, "this court longs for the guidance of the Oregon appellate court as to the proper interpretation of the [Oregon Trust Deed Act]." The federal courts may receive this guidance soon because a state court case requesting clarification of these MERS issues is currently on appeal to the Oregon Court of Appeals, *Niday v. GMAC Mortg., LLC,* Clackamas County Circuit Court Case No. CV-10-02-0001. The Oregon Court of Appeals decision will hopefully provide some clarity as to the proper interpretation of the Oregon Trust Deed Act.

Why Construction Lawyers Should Care: MERS is involved in approximately 40% of all residential foreclosures and is the mortgagee of record on nearly two-thirds of all newly originated residential loans. *See Jackson v. MERS,* 770 NW 2d 487, 491-492 (Minn. 2009). Therefore, in approximately 40% of the cases in which a construction lien claimant is noticing its construction lien claim, foreclosing a construction lien or is being foreclosed due to a lender's foreclosure of its note, MERS issues exist. How the courts decide these MERS issues will affect both notice and pleading issues.

Some Good News. The good news for construction lien claimants as it relates to MERS is that, on June 23, 2011, the Governor signed Senate Bill 382 relating to the notices required from construction lien claimants to "mortgagees." The Bill amends ORS 87.005, 87.018 and 205.234 and went into effect on January 1, 2012. It applies to all trust deeds and mortgages filed on or after the effective date, and all assignments of mortgages and trust deeds that are recorded on or after January 1, 2008. Essentially the amended statutes ease the burden on construction lien claimants by requiring them to notify mortgagees of the construction lien only "if the name and address of the mortgagee appear in a mortgage of record or a trust deed of record as required under ORS 205.234(1)(b) or in the instrument that assigns a mortgage or trust deed as required under ORS 205.234." ORS 87.018(2) (2011). This amendment goes a long way to ease the notice burden that was created, in large part, by MERS on construction lien claimants.

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NOTE: Prior newsletters are available (in a searchable format) at the Section's website: *www.osbarconstruction.com*.