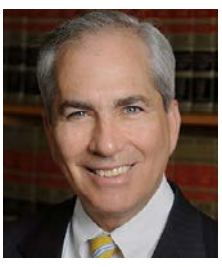
PRIVATE DEVELOPMENT ON PUBLIC LAND – STA LEGISLATIVE VICTORY UNDERMINED BY APPELLATE COURT



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Over recent decades, the STA has developed an exemplary track record of legislative victories on behalf of the industry. In 2004, we at the STA sought to address one of the many serious problems then confronting the industry, namely, the legal loophole that had existed with regards to assuring payment on projects that were developed by private parties on public land. Since there can be no mechanic's lien filed on public land, no private improvement lien could be filed against such public property. And since no public funds were being used, no public improvement lien could attach against such private funds.

In short, a legal Catch-22 existed on these types of projects, depriving those who worked on them, or provided materials, equipment or supplies to them, of any protection under the mechanic's lien provisions of New York's Lien Law.

An appellate court decision has just come down adversely impacting the issue. The project involved in the case was "Atlantic Yards", the 22 acre mixed-use development in Brooklyn, anchored by the Barclay's Center sports arena. Skanska U. S.A. Building, Inc. ("Skanska") and Forest City Ratner Companies, LLC ("FCR") entered into an agreement in 2012, which would provide for the "modular" construction of Building "B2", a proposed 34 story residential building with 350 units.

There were many legal issues embroiled in the failed relationship between Skanska and FCR addressed in the court's decision. Among them were issues related to STA's legislative efforts in 2004. At that time, the STA had successfully sought reform legislation with the following language amending Lien Law §5:

> *"[w]here no public fund has been established for the financing of a public improvement… The chief financial officer of the public owner shall require the private entity for whom the public improvement is being made to post… a bond or other form of undertaking guaranteeing prompt payment of monies due."*

As can be seen, this required the public owner, in the case of large private improvement projects on public land such as Atlantic Yards, to address the problem with a specific, effective remedy, namely, the providing of a surety bond. However, the crux of the aforementioned appellate court decision just decided, as it relates to the Lien Law, was whether a mere corporate guarantee does, or does not, comply with the Lien Law's amended Section 5. In other words, does a corporate guarantee qualify as "a bond or other form of undertaking" under the statute? Incredibly, the appellate court decided that it was.

We believe the appellate court was simply wrong and that a surety bond from a third party entity (i. e., from a New York licensed surety), and not simply a corporate guarantee from FCR's corporate "affiliate, " was required by the clear language and intent of the STA's 2004 Lien Law amendments.

Twelve years after its passage, the appellate court did not find the revised language of Section 5 of the Lien Law to be quite so clear. As we have seen countless times in New York State, a court egregiously failed to appreciate the construction-industry-based context of the matter that came before it.

The STA amendments to Lien Law §5 were designed to require a surety bond, the promise to pay of an independent, third party guarantor. Sureties underwriting bonds of the magnitude of the Atlantic Yards project are invariably major insurance companies, having extraordinary balance sheets and billions of dollars of capacity across their business lines (of which suretyship is typically only a small part).

The appellate court, however, disemboweled the Section 5 protection, finding that a corporate guarantee of FCR's "affiliate" would suffice. This makes a mockery of the entire 2004 reform effort.

An undertaking, as the appellate court itself acknowledged, is defined as:

> *"[a]ny obligation whether or not the principal is a party thereto, which contains a covenant by a surety to pay the required amount, as specified therein, if any required condition… is not fulfilled."*

However, the appellate court did still further damage. Although, the amendment to Lien Law §5 still exists and was not technically overturned, it was significantly undermined. As contrasted to a surety bond from a licensed surety in NYS, what guarantee would suffice? Whose guarantee would suffice? As indicated, here the appellate court found (ignoring, as well, the obvious conflict of interest) that a corporate guarantee of an FCR "affiliate" would suffice. As the court stated:

> *"ESDC, as the public owner, was satisfied with the guarantee issued by Forest City Enterprises, Inc. Certainly if the legislature had wanted the guarantee to be on par with a letter of credit, it could have said that or identified the various types of guarantees that would satisfy the statute."*

Finally, not being finished, the appellate court even went so far as to challenge the efficacy of the corporate guarantee itself, when it put the "last nail in the coffin" as follows:

> *"Since plaintiff (Skanska) is seeking only to force defendants to post a bond under Lien Law §5, we need not decide whether it would [even] have standing to enforce the guaranty as against Forest City Enterprises, [the FCR affiliate- guarantor], as a third-party beneficiary."*

Thus, the court raises this possible defense for any non-paying entity to raise as an unresolved question in any future Lien Law §5 litigation.

The impact of this untimely evisceration of the Lien Law §5 reform, cannot be overstated, as private funds are increasingly being called upon to fill public funding deficiencies (e. g., "P-3s"). Many more of these "loophole" projects will be undertaken.

It's clear, as is so often the case, that only further corrective legislation can resolve the damage this appellate court decision has done to an important STA-initiated legislative reform. Given the importance and currency of this issue (private projects on public land) there will no doubt be further developments. As we have seen recently with the almost unanimous passage of the STA's COFED Reform Bill in Albany, New York legislators are interested in parties being treated fairly and fully paid on all public sector-related projects.