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Commonwealth of Kentucky

Court of Appeals

NO. 2008-CA-000263-MR
and
NO. 2008-CA-000328-MR

LOUISVILLE GALLERIA, LLC
AND MANUFACTURERS AND TRADERS
TRUST CO. APPELLANT/CROSS-APPELLEE

APPEAL AND CROSS-APPEAL
FROM JEFFERSON CIRCUIT COURT
v. HONORABLE KATHLEEN VOOR MONTANO, JUDGE
ACTION NO. 04-CI-010178

SCARBOROUGH MECHANICAL
SERVICES, INC. APPELLEE/CROSS-APPELLANT

OPINION
VACATING AND REMANDING AS TO APPEAL AND
DISMISSING AS TO CROSS-APPEAL

** ** ** ** **

BEFORE: COMBS, CHIEF JUDGE; NICKELL AND TAYLOR, JUDGES.

COMBS, CHIEF JUDGE: Louisville Galleria, LLC and Manufacturers and Traders Trust Co., appeal from the partial summary judgment of the Jefferson

Circuit Court entered on September 25, 2006, and from the final judgment of the trial court entered January 18, 2008; Scarborough Mechanical Services, Inc., cross-appeals from the final judgment. In its partial summary judgment, the trial court concluded that Galleria's property was subject to Scarborough's lien and that Scarborough had perfected its lien against the property by providing proper pre-filing notice to Galleria's "representative." In its final judgment, the court awarded Scarborough a mechanic's lien to secure its claim of $266,867.50; however, the court denied Scarborough's claims for prejudgment interest and attorneys' fees. Because we conclude that a question of fact precluded the entry of summary judgment with respect to the viability of Scarborough's lien, we vacate the trial court's partial summary judgment and remand for further proceedings. We dismiss Scarborough's cross-appeal as moot.

The litigation between the parties to this appeal is intertwined with a number of claims asserted by a variety of other lien-holders. Over time, a voluminous record was amassed. We have attempted to simplify our discussion by referring only to those facts and to those parts of the record that are directly relevant to a resolution of these proceedings. A short summary of the parties' relationship follows.

In November 2003, Galleria leased a portion of its property known as "Fourth Street Live" to Premier Health & Fitness, LLC. Premier Health & Fitness planned to convert the leased space into an upscale fitness facility, and it hired Evolution Construction & Development as its general contractor for the project.

Evolution subcontracted with the appellee, Scarborough, to do plumbing and HVAC work at the site. Scarborough worked on the project for more than three months. During this period, Scarborough's requests for payment were wholly ignored. To protect its interests, Scarborough attempted to lodge a lien against Galleria's real property.

On September 27, 2004, Scarborough corresponded with Gary Darnell, a "tenant coordinator," who had helped Premier Health & Fitness with the renovation. The correspondence indicated that Scarborough intended to claim a lien in the amount of $298,355.00 against Galleria's real property.

Scarborough continued to perform work on the project until October 9, 2004. As of this date, more than 90% of Scarborough's contract work had been completed. Within two days, Scarborough filed a lien statement in the amount of $325,327.00. Three weeks later, Scarborough sent a notice to Galleria and to Gary Darnell advising that the lien statement had been filed. Ultimately, Premier Health & Fitness filed for bankruptcy protection and defaulted on its lease agreement with Galleria.

On December 2, 2004, two subcontractors who had worked on other parts of the Premier Health & Fitness construction project filed a complaint against Galleria. Scarborough was made a party-defendant in the action since the county clerk's records revealed that it, too, was claiming an interest in the property. Scarborough filed a cross-claim demanding that its lien also be enforced against

Galleria.[1] By agreement of the parties, the action was referred to a master commissioner.

After several months, Scarborough filed a motion for summary judgment. In its memorandum in support of the motion, Scarborough requested the court to recognize its perfected security interest in Galleria's real property since it had substantially complied with the statutory provisions governing the creation of mechanics' and materialman's liens.

In response, Galleria filed a motion to dissolve Scarborough's lien, arguing that Scarborough could not enforce its lien because its attempts to perfect the lien were technically defective. Galleria contended that Scarborough's only recourse was through an action for unjust enrichment and recovery in *quantum meruit*.

After considering the parties' motions, the court's master commissioner recommended that neither of the motions be granted. Galleria immediately objected to the recommendation, arguing emphatically that Scarborough's lien was fatally defective and invalid as a matter of law.

In an order entered September 25, 2006, the circuit court rejected Galleria's contention that Scarborough's attempts to perfect its lien were deficient and concluded that Scarborough was entitled to partial summary judgment with respect to the viability of its lien. The court concluded that the only issue to be resolved at trial was the specific value of Scarborough's security interest in

[1] Scarborough filed a third-party complaint against Manufacturers and Traders Trust Company in March 2005. That institution had filed a bond to release Scarborough's lien.

Galleria's property. After entry of the final judgment, Galleria filed this appeal; Scarborough filed a cross-appeal.

Galleria presents several arguments on appeal. While we have considered each of them, we shall discuss only two since the second argument is dispositive of Galleria's challenge to the trial court's interlocutory order of partial summary judgment. Since our resolution of these issues renders moot Scarborough's cross-appeal, we shall not address it on the merits.

We limit our discussion to a sequential analysis of two issues. First, we must determine whether Galleria's property was subject to Scarborough's claim of lien. If the property was properly subject to a claim of lien under the circumstances presented, we must then determine whether Scarborough strictly complied with the requirements of the Commonwealth's mechanics' and materialman's lien statutes to perfect its lien.

Whether Galleria's property was subject to Scarborough's claim of lien involves an analysis of the provisions of Kentucky Revised Statute(s) KRS 376.010 governing mechanics' and materialman's liens. The statute sets forth conditions of eligibility for a lien, providing that any person who performs labor or furnishes materials for the improvement of real property:

> by contract with, or by the written consent of, the owner, contractor, subcontractor, architect, or authorized agent, shall have a lien thereon, and upon the land upon which the improvements were made or on any interest the owner has therein, to secure the amount thereof with interest and costs.

Scarborough did not contract with Galleria, the owner, for the improvements made to the real property. Scarborough contracted with Premier Health & Fitness, Galleria's *tenant*, for the improvements. Thus, the question is whether under these circumstances Scarborough can assert a lien against the *landlord's* fee simple interest in the property as distinguished from the *tenant's* more limited interest in the real property.

Scarborough relies on the provisions of the statute to assert its entitlement to claim a lien against the landlord's fee simple interest in the real property. Galleria, on the contrary, contends that it took every precaution possible to prevent its tenant's subcontractor from asserting a claim of lien against the real property. Its arguments are grounded in the reasoning of a series of cases decided in our courts that indicate generally that laborers may have a lien upon the property which they have improved *only* if the improvement was made "by contract with or by the written consent of the owner" or his "authorized agent."

In *Luigart v. Lexington Turf Club*, 130 Ky. 473, 113 S.W. 814 (Ky. 1908), the court considered whether Montague's real property was subject to the lien claimed by Luigart, a contractor, who had furnished materials and built a structure and other improvements for Montague's lessee, Lexington Turf Club. The court concluded that the terms of the lease agreement between Montague and Lexington Turf Club did not amount to "the written consent of the owner" and that any knowledge or verbal consent of the owner to any improvement was insufficient to create a remedy against the real property.

However, the facts were slightly different in *Penny v. Kentucky Utilities Co.*, 238 Ky. 167, 37 S.W.2d (Ky. 1931). In *Penny,* J.F. Smith intended to purchase the property at issue. Under the terms of a written contract, Smith was required to repair and remodel a hotel owned by J.E. Penny (the seller). In order to secure the necessary repairs, Penny was bound to lend Smith $15,000.00. Since the contract plainly required that the work be performed, the court concluded that Penny's fee simple interest in the real property was subject to a materialman's lien.

In *Campbell v. Summerhays, Inc. v. Greene,* 381 S.W.2d 531 (Ky. 1964), the court considered whether mechanics' liens for the materials and labor supplied under a contract with the lessee could be enforced against the landowner's interest in the property. Under the terms of the lease agreement, the lessee was required to construct a building to be used as a funeral home. After the lessee defaulted, the laborers sought to enforce mechanics' liens against the real property. The court concluded that the liens could be enforced since the terms of the lease agreement satisfied either the "agency" clause or the "consent of the owner" clause of the statute.

After reviewing the case law, we are persuaded that Scarborough performed labor and furnished materials for the construction project with what amounts to the written consent of the owner. The terms of the lease agreement between Galleria and Premier Health & Fitness provided that the tenant would transform the leased property and use the premises "only for the operation of a first class health club and fitness facility." Premier Health & Fitness was to provide

Galleria with plans and specifications showing all the interior and exterior alterations or improvements that it proposed to make to the premises, and Premier Health & Fitness was not to begin work on the premises before obtaining Galleria's written approval. While Premier Health & Fitness was to bear the entire upfront cost of the alterations, Galleria was to provide a Tenant Construction Allowance of $400,000.00 to be paid to premier Health & Fitness upon completion of the project. These provisions are plainly sufficient as a matter of law to cause Galleria's property to be subject to Scarborough's lien.

Two other contract provisions are also raised as peripheral issues. One required Premier Health & Fitness to remove the improvements and fixtures upon Galleria's request; the other prohibited Premier Health & Fitness from permitting any mechanic's lien or notice of lien to be filed against the property. We are not persuaded that either of these provisions is relevant to our analysis. Neither of these provisions changes the parties' agreement that Premier Health & Fitness would make <u>all the improvements</u> to the premises that the Galleria required. Thus, the trial court did not err by concluding that Galleria's property was subject to Scarborough's claim of lien.

Having determined that the property was subject to Scarborough's claim of lien, we must next consider whether Scarborough properly perfected its lien against the property. Kentucky adheres to the rule that the statutory provisions for perfecting a lien must be strictly followed. *Hub City Wholsale Electric, Inc. v. Mik-Beth Electrical Co., Ltd.,* 621 S.W.2d 242 (Ky.App.1981). The statutory

scheme provides a good faith creditor with a means of converting an unsecured debt into a secured debt by complying with certain prescribed steps. *Laferty v. Wicks Lumber Co.*, 708 S.W.2d 107 (Ky.App.1986). If the subcontractor has not contracted directly with "the owner or his agent," the owner or his "authorized agent" must be notified in writing (within 120 days after furnishing the last labor or material) of the claimant's intention to claim a lien if he is not paid. KRS 376.010(3). Within six months after furnishing the material, a lien statement must be filed with the county court clerk. KRS 376.080. Finally, an action to enforce the perfected lien must be commenced within one year after the filing of the statement with the clerk. KRS 376.090. Failure to take any of these steps dissolves the lien. *Lafferty, supra.*

Galleria argues that Scarborough did not comply with the first of these requirements – the requirement that the mechanic or materialman notify the owner of the property or his "authorized agent" in writing that he intends to claim a lien -- and that the trial court erred by concluding otherwise. Scarborough responds that that it was not required to provide any notice whatsoever that it intended to claim a lien since it dealt directly with Galleria's agent, Premier Health & Fitness. In the alternative, Scarborough contends that it complied with the requirements of the statute by corresponding with Gary Darnell, Galleria's "authorized agent," on September 27, 2004, and advising him that it intended to claim a lien in the amount of $298,355.00 against Galleria's property.

Both parties rely on the specific provisions of KRS 376.010(3) as follows:

> No person who has not contracted directly with the *owner or his agent* shall acquire a lien under this section unless he notifies in writing the owner of the property to be held liable *or his authorized agent*, within . . . one hundred twenty (120) days on claims in excess of $1,000 after the last item of material or labor is furnished, of his intention to hold the property liable and the amount for which he will claim a lien. It shall be sufficient to prove that the notice was mailed to the last known address of the owner of the property upon which the lien is claimed, or to his duly authorized agent within the county in which the property to be held liable is located.

(Emphasis added).

The trial court specifically rejected any notion that Premier Health & Fitness was an agent of Galleria, a status that -- if valid -- would have relieved Scarborough of the obligation to provide written pre-lien notice to the property owner altogether; Scarborough did not appeal the issue. Thus, a notice requirement remained. The purpose of the required notice to the property owner is to so inform the owner of both the nature and the amount of the claim in order that he may protect himself in his future dealings with the person with whom the subcontractor claimant has contracted -- and particularly to enable him, in the majority of cases, to retain whatever money may be due the contractor and to apply it to the payment of the lien claimed. *Middletown Engineering Co. v. Main street Realty, Inc.*, 839 S.W.2d 274 (Ky.1992). Actual notice does not serve as a substitute for the required statutory notice. *Id.* The knowledge or the lack of

knowledge by the owner is immaterial. *Powers v. Brewer,* 238 Ky. 579, 38 S.W.2d 466 (Ky. 1931).

Therefore, we next consider the second of Galleria's contentions – whether the trial court erred by concluding that Scarborough had complied with the notice requirement by mailing a pre-lien notice to Gary Darnell. We are not convinced by the limited record on this issue that Gary Darnell qualified as Galleria's "authorized agent" pursuant to the provisions of KRS 376.010(3). Consequently, we cannot conclude that Scarborough's correspondence to Darnell satisfied its obligation to notify the property owner in writing of its intention to claim a lien under the provisions of KRS 376.010(3) as a matter of law.

It is clear from the record that Darnell was not and is not a Galleria employee. Whether he qualified as an "authorized agent" of Galleria otherwise is a question of fact to be determined from the entirety of the circumstances and the conduct of the parties. *Middletown Engineering Co. v. Main Street Realty, Inc.*, 839 S.W.2d 274 (Ky. 1992). The existence of this material question of fact precluded the entry of summary judgment with respect to the viability of Scarborough's lien, and we must remand the matter to the trial court for further proceedings to determine the nature of the relationship between Galleria and Darnell and to ascertain whether their relationship was indeed that of principal and agent.

The partial summary judgment of the Jefferson Circuit Court is vacated. This matter is remanded for further proceedings.

ALL CONCUR.

BRIEF FOR APPELLANTS/CROSS-APPELLEES:

Robert W. Griffith
Chadwick A. McTighe
Louisville, Kentucky

ORAL ARGUMENT FOR APPELLANTS/CROSS-APPELLEES:

Robert W. Griffith

BRIEF AND ORAL FOR APPELLEE/CROSS-APPELLANT:

Ronald L. Coombs
Louisville, Kentucky