

# Construction Conversations around the Licensing Board, Liens, and the Supply Chain

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My colleagues and I recently provided key updates on supply chain disruption, liens, and licensing boards during the firm's 2021 Construction Conversations Webinar.

In the Rapid-Fire Legal Update session, we covered a variety of topics relevant to the construction industry, including:

- Dealing with the North Carolina Licensing Board for General Contractors
- Ongoing supply chain issues
- Lien law best practices
- Economic loss rule

This article summarizes the main takeaways.

## Licensing Boards

My law partner, Evan Musselwhite, started the session with important considerations for general contractors dealing with a licensing board complaint. Before delving into these issues, Musselwhite provided an overview of the intricacies of when a general contractor's license is required and the importance of strictly following licensing regulations.

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Aside from the Board having the ability to restrict, suspend or revoke a license, Musselwhite said another negative outcome could result from failing to pay careful attention to licensing rules and regulations.

A contract is generally unenforceable by the general contractor if it does not have the required license. Strict compliance with the licensing rules and regulations, not substantial compliance, is the rule.

“The courts here consider that an illegal contract,” said Musselwhite. “That means if you complete the entire project and do all the work perfectly, that owner doesn’t have to pay you, and you can’t go to the courts to enforce that contract to try to get paid.”

Some view this as a very harsh result, especially from a collectability standpoint. “A lot of times, this is a big windfall for owners, but that is just the way the courts have interpreted these regulations because they feel they deal with the health and safety of the public,” Musselwhite explained.

The question of who actually needs a license is more complex than it seems. “Every corporation, partnership, and LLC has to have its own license in its own name if it’s practicing general contracting within the state,” noted Musselwhite.

He added that, in general, each member of a joint venture has to have a license. “Sometimes there can be confusion over an unlicensed entity wanting to team up with a licensed contractor to do a project under a joint venture and thinking if we team up with them and they are licensed, then we are OK, but that is **not** how it works,” said Musselwhite. To avoid disciplinary action, each joint venture member would require a license, or the joint venture itself could obtain its own license.

As far as what the Board is looking for when it gets a complaint, the bases for disciplinary action include:

- Unauthorized practice of general contracting
- Fraud or deceit in obtaining a license
- Gross negligence, incompetency, or misconduct in the practice of the profession
- Willful violation of licensing statutes

Musselwhite explained that it is important to cooperate with the Board when faced with a complaint. “It’s important to be proactive about a complaint; keep and maintain all records, and don’t try to defend an indefensible position,” advises Musselwhite. “One of the worst things to do is to try to cover something up or make a misrepresentation to the Board, as it’s much more likely to have a harsh consequence.”

Honesty is the best policy when dealing with the North Carolina Licensing Board for General Contractors. Some issues may have originated from a simple mistake or oversight that can be explained to the Board. Musselwhite explains: “The Board wants acknowledgment of a mistake, if there was one, someone to take responsibility for it, and what steps you will take to ensure that the issue doesn’t happen again.”

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## Supply Chain Issues

As a business attorney with decades of experience representing contractors, design professionals, and project owners, I have increasingly fielded a multitude of questions about dealing with supply chain disruption in recent months. As noted, “[t]he global pandemic has caused shortages of materials, components, and equipment at a level most of us have never seen, and this has caused rapidly escalating prices, unpredictable delivery times and ultimately, more risk for contractors and subcontractors.”

The mindset of doing business as usual is simply not going to work anymore. To help contractors and subcontractors adapt to the modern business environment, I provided a number of steps for minimizing risk, including:

- Communicate early and often about supply chain issues, set clear expectations
- Provide for price increases in the contract based on market changes
- Use allowances for volatile materials that could fluctuate in price
- Work with the owner(s) to buy materials in advance
- Include material shortage as a reason for additional time or delays

“If you can educate all the parties, they may be convinced to do things differently. We need to recognize the market we’re in and create specific carve-outs in contracts for problems related to epidemics, pandemics, and material shortages.”

## Lien Law Update

Luke Tompkins provided guidance and best practices for navigating lien laws.

Tompkins noted that there have been no significant changes to North Carolina lien laws since 2013 when lien agent requirements were added. He advised contractors to post building permits and lien agent information conspicuously on the job site.

Also, contractors and subcontractors should serve a notice to the lien agent no later than 15 days after furnishing labor or material at the job site. Failing to do so shifts the priority of any lien claims from the date of first furnishing to the date where the lien is actually filed and perfected.

“This can have vast consequences because if other subcontractors do this process correctly and get everything in place before you file your lien, and you didn’t serve the notice to the lien agent, you could lose your ability to recover,” Tompkins explained.

To be safe, Tompkins recommended that, “Every time you begin work on a project, get the lien agent information, serve that notice to the lien agent and maintain proof that you served the lien agent by using certified mail or another method of service by which you can show receipt of service.”

Tompkins also strongly suggests that contractors post and file a notice of contract to guard against the threat of double payment. On the other hand, subcontractors should check to see if a notice of

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contract has been posted on the job site and, if so, should serve the contractor with a notice of subcontract to preserve their right to file a lien on real property.

Lastly, Tompkins emphasized the importance of asserting lien claims in a timely fashion. A lien on real property must be filed within 120 days of the last furnishing of work or materials and enforced by legal action within 180 days of the last furnishing. Waiting until the last minute to file and enforce your lien on real property can result in a loss of your claim. Likewise, it is paramount to give notice of a claim of lien on funds as soon as it becomes clear that a payment is late and not forthcoming.

## **Economic Loss Rule**

Bill Durr weighed in on a recent North Carolina Supreme Court decision addressing the application of the economic loss rule.

In the case, *Crescent University City Venture, LLC v. Trussway Manufacturing, Inc.*, a commercial property owner brought a lawsuit against a general contractor and the manufacturer of the trusses used in the project.

“As is often the case, this dispute involved a property owner looking for as many deep pockets as they can possibly find,” said Durr.

The owner sought to make a direct claim against the truss manufacturer, alleging the trusses were negligently manufactured. The North Carolina Supreme Court affirmed the ruling from the Business Court, holding that the only means of recovery would be against the general contractor since there was no contract between the owner and manufacturer.

“This decision clarifies the applicability of the economic loss rule in the context of commercial construction projects, especially where the property owner is an experienced real estate developer,” added Durr.

## **Questions and Answers**

At the close of the webinar, the moderator opened the floor for questions. One attendee wanted to know: “Can I fire an employee for refusing to wear a mask while working?”

“Yes, if you go through the right process,” said Emily Massey. “The first question to ask is, ‘Is this for a medical or religious accommodation?’ We have seen terminations happen: the key is to engage legal counsel, have multiple conversations, and document the process.”

Another attendee asked, “Does the economic loss rule apply to single-family homes?”

“I think you can argue it does apply,” said Durr. “I think the courts would look at whether there is a right of recovery in the contract. Courts will take a firmer view in regards to a commercial contract, but they may give the benefit of the doubt to a homeowner with less experience negotiating contract terms.”

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