

Second Supplement to Memorandum 2000-37

Mechanic's Liens (Materials Submitted at June 2000 Meeting)

The attached letters were submitted to the Commission and discussed at the June 22, 2000, meeting:

	<i>Exhibit p.</i>
1. Letter from Ellen Gallagher, Staff Counsel, Contractors State License Board (June 20, 2000)	1
2. Lumber Association of California and Nevada (June 22, 2000)	3

Respectfully submitted,

Stan Ulrich
Assistant Executive Secretary

CONTRACTORS STATE LICENSE BOARD
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June 20, 2000

Mr. Stan Ulrich
Assistant Executive Secretary
California Law Revision Commission
4000 Middlefield Road
Room D-1
Palo Alto, California 94303

Dear Mr. Ulrich:

Re: **Mechanics' Liens**

Thank you for including my proposal in your June 13, 2000 mailing. I agree with your analysis of Direct Pay with three exceptions.

You ask whether there should be preconditions to service of the Direct Pay Notice (DPN). Without preconditions, how will the homeowner know whether the claim is valid, the services performed, and/or the job is finished?

The homeowner would know that the claim is valid, the services have been performed, and/or the job is finished because the prime contractor says so. As I see it, the DPN would, in effect, tell the homeowner "When the contractor tells you it is time to pay for *the framing material or the tile work*, do not pay the contractor, send a check for the amount authorized by the contractor directly to me." This simple approach covers all the issues and is consistent with current home improvement law. Right now, it is against the law for a contractor to request payment for work not completed or material not yet provided. In addition, as you note, if only part of the work is covered by the payment, the DPN could show a schedule for payments based on progress. Under this plan, as now, the contractor would be charged with following the law by authorizing payment only as progress is made.

You also ask, "What happens if there is a dispute between the contractor and the subcontractor?" Answer: The same as now. If the subcontractor has not satisfactorily completed the work, the contractor should not ask for the homeowner for payment. If the contractor replaces the subcontractor or needs to hire someone else to fix the subcontractor's work, the contractor should only ask the homeowner for money to pay the subcontractor who did the work. The dispute remains between the prime and the subcontractor or material supplier. The homeowner is not in it.

On the same issue of a dispute between the contractor and the subcontractor you appear to be saying that, under Direct Pay, there would be no profit. I don't see this. Most homeowners contracting for remodeling and repair services expect the contractor to have some mark up on the work of subcontractors or material suppliers. At the time the contractor authorizes payment for the subcontractor, he or she could request two payments. For example, "Mail a check to Joe for \$3,000 and give me \$300, according to the \$3,300 payment scheduled in the contract upon completion of the bathroom tile."

Of course, contractors who develop a clean credit profile will avoid the need to disclose the mark up. Subcontractors and material suppliers providing goods and services to these primes will forgo asserting lien rights.

Finally, your analysis connects Direct Pay to Mr. Acret's contention that full payment can be a complete and constitutional defense to the mechanics' lien right (pages 17-18). I can't tell you what a thrill it is to be mentioned in the same sentence as Mr. Acret but I don't believe we need this connection. Direct Pay was developed to sidestep the constitutional issues.

Direct Pay does not extinguish a lien. Direct Pay merely rewrites the 20-day Preliminary Notice. Instead of offering joint control, joint checks or conditional and unconditional releases, the legislature would offer Direct Pay as a way to make sure the subcontractor or material supplier is paid. If the homeowner chooses not to follow the DPN (the way the homeowner presently fails to get a release or use a joint check or find some other means of making sure the subcontractor or material supplier is paid), a lien may be placed on the home. Just as the legislature might mandate payment bonds or joint control accounts as the preferred solution to mechanics' liens, Direct Pay can be chosen without raising the specter of abridged constitutional rights.

Thank you for the opportunity to participate in this process. If you have any questions, please call me at 916-255-4116 or e-mail me at EGallagher@dca.cslb.ca.gov.

Sincerely yours,

Ellen Gallagher, Staff Counsel
Contractors State License Board



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June 22, 2000

Mr. Stan Ulrich
Assistant Executive Secretary
CALIFORNIA LAW REVIEW COMMISSION
4000 Middlefield Road Room D-1
Palo Alto, CA 94303-4739

Re: Mechanic's Lien Study

Dear Mr. Ulrich:

The Lumber Association of California & Nevada (LACN) provides the following response to proposals previously submitted to the Commission, including those of Sam Abdulaziz of Abdulaziz & Grossbart, Ellen Gallagher of the Contractors State License Board, and James Acret with respect to the Mechanic's Lien Study.

The LACN concurs that further protection of California homeowners is appropriate for consideration. However, LACN believes that most contractors pay their obligations, and that in only a very few circumstances is a homeowner required to pay a labor or material bill twice. In those circumstances, it is likely that the homeowner did not understand the consequences of their action or inaction, or the application of the existing lien laws. Moreover, in many of the cases in which a homeowner has been required to pay twice, the low value of the Contractor's License Bond has precluded the homeowner's recovery from the party responsible for (and likely improperly benefiting from) such double payment.

Accordingly, the LACN believes that homeowners may be afforded greater protection and many such problems may be addressed by the implementation of the following suggestions. These suggestions will not dramatically complicate procedures under the existing mechanic's lien laws and recognize that in the vast majority of situations, the present lien laws are sufficient to protect the rights of all parties and do not promote injustice to the homeowner.

1. Educate the Homeowner. Existing laws afford reasonable protections for the homeowner and the means to avoid problems, including double payment. However, regardless of changes to the law, if the homeowner does not understand the provisions of the laws, problems can arise. LACN supports Mr. Abdulaziz's suggestions for:

a) simplification of the existing notices to language which the homeowner will understand, while still providing an appreciable warning of consequences; and

b) for a simple checklist to be used by a homeowner when starting a project.


2. Increase the License Bond Requirements. The current license bond requirement of \$7,500 does not afford reasonable protection for those that may be harmed by a contractor's actions. LACN believes the bond must be in a minimum amount of \$20,000 in order to afford any meaningful possibility of relief to an aggrieved homeowner, and that the cost of such a bond will not be too expensive for the competent contractor.

3. Change the Preliminary Notice Requirements. The LACN believes a homeowner should be required to sign a preliminary notice acknowledging his receipt. While this requirement will impose an additional burden on subcontractors and material suppliers who are presently required to provide such notice in order to assert lien rights, it may afford worthwhile protection for the homeowner. The language of the Preliminary Notice may also be revised to plain English, to better advise the homeowner of the risks and issues present.

Other proposals, including direct pay, joint check control and increased liability insurance requirements do not afford the homeowner significant additional protection, and will require wholesale changes in the existing laws, impacting all participants in the trades. Moreover, the direct pay proposal advanced by the CSLB is premised upon assumptions that material suppliers are in the best position to assess the risk of extending credit, when such material suppliers have less contact with the prime contractor than the homeowner, who has chosen such prime contractor as his representative for the construction of the work. Material suppliers largely do not provide their materials to the prime contractor, whose defalcations are most often the reason for the double payment problem which has fomented this study.

LACN and our members believe that the existing mechanic's lien laws, when complemented by the foregoing suggestions, will achieve the desired result of affording greater protection to a homeowner, without significant and drastic revisions to the existing law and procedures. The other proposals require dramatic revamping of the law and procedures, and may require constitutional amendment to broach the constitutional stature of the mechanic's lien.

Sincerely,



Jan Hansen

Jan Hansen
Executive Director

Prepared by Frank Solinsky, Kevin Destruel, & Peter Freeman.