Study H-820 July 18, 2000

First Supplement to Memorandum 2000-47

Mechanic's Liens (Additional Comments)

Attached to this supplement are some additional mechanic's lien reform commentary. The following items are attached:

We will discuss these materials in more detail at the meeting. The major points are as follows:

Homeowner's Relief Recovery Fund Proposal

Professor Clark Kelso, writing from the Institute for Legislative Practice, proposes an insurance scheme, inspired in part by Assemblyman Honda's AB 2113. (Exhibit pp. 1-10.) The key to the proposed "Homeowner's Relief Recovery Fund" is a fee added to the building permit based on the value of the project. Professor Kelso believes that the fee could be in a modest amount and by being based on the value of the project, would avoid the regressive aspects of flat-fee proposals. The report recognizes that the appropriate amount of the fee would need to be studied, and cites the Strong Motion Instrumentation Program as an existing statewide program funded by value-based fees collected through building permits.

This looks like an interesting approach that may solve some of the problems with recovery fund proposals. We will study the proposal in more detail and discuss it at the meeting. Prof. Kelso also expresses his regrets at not being able to attend the upcoming meeting.

Gallagher Letter

Ellen Gallagher provides some additional information and insight into the issue of the extent of the double payment problem. (Exhibit p. 11.) Specifically, she disagrees with the staff's comment that the double payment problem is a

"rare occurrence." She also provides some examples of recent cases where double payment apparently occurred.

The staff looks forward to receiving more information on these cases. The CSLB is probably in the best position to help the Commission with this data. This is an interesting issue because if double payment situations are rare, in relation to the number of contracts, then a simple solution such as the Acret full-payment defense should be unobjectionable. If we begin to find that there are relatively more double payment occurrences, then more pervasive reforms may be called for. Either way, since we know there are at least some problems, and that they can be very serious for the persons involved, it looks like some remedy is needed. Of course, law reform in the home improvement contract area may be needed for other reasons, so the degree of double payment is not conclusive either way.

Abdulaziz Comments

Sam Abdulaziz has provided some preliminary comments concerning Memorandum 2000-47. (Exhibit pp. 12-13.) He reserves his objection to the payment defense on the grounds of unconstitutionality.

As to forms, Mr. Abdulaziz thinks that the form language should be provided in the statute, in that the future of the CSLB is in question. The staff believes that even if the CSLB ceases, the Department of Consumer Affairs would take over its functions, and the duty to issue and maintain forms would presumably follow.

As to the scope issue, Mr. Abdulaziz argues against adopting the scope of home improvement contracts since it would cover apartment buildings, which he considers to be commercial work.

As to the direct pay proposal, Mr. Abdulaziz suggests, if we understand the comment, that the notice should also go to the "customer" (subcontractor) of a supplier. The draft provides for notice to go to the prime contractor because of the role the contractor plays — telling the owner when payment is due to a subcontractor or supplier. He also asks how the direct pay proposal would affect lenders. The staff has not yet considered this issue.

Mr. Abdulaziz argues that the direct pay proposal, as set out, would be unconstitutional because draft Section 3107.3 would cause the lien to be lost if the homeowner pays before the notice is received. The staff disagrees with this conclusion. It may be that some additional time limits would need to be implemented, but if the subcontractor or supplier doesn't get notice to the owner, the cost of that failure shouldn't fall on the homeowner. The simplicity and

utility of the direct pay concept, as we understand it, would be lost if it included the retroactive feature of the so-called "preliminary" 20-day notice of existing law. But we will give further consideration to the problem Mr. Abdulaziz identifies. Ultimately, there may need to be enforceable payment schedules so that there is always time to get notices delivered, if desired.

The correction of the description of the lien recording and suit filing limits on Exhibit page 13 is well-taken. The other points concerning the full payment defense will be considered in due course at the meeting.

Respectfully submitted,

Stan Ulrich
Assistant Executive Secretary

UNIVERSITY OF THE PACIFIC
McGEORGE SCHOOL OF LAW
INSTITUTE FOR LEGISLATIVE PRACTICE

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July 18, 2000

Mr. Stan Ulrich
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Dear Stan:

One of my students and I have been following with some interest the discussions regarding mechanics liens and would like to make a suggestion for a solution to the problem that I believe has not yet been raised with the Commission. I apologize for the delay in getting you this letter, but I have been unexpectedly busy the last few weeks.

As you know, Section 3 of Article XIV of the California Constitution provides for mechanics liens as follows:

> Mechanics, persons furnishing materials, artisans, and laborers of every class, shall have a lien upon the property upon which they have bestowed labor or furnished material for the value of such labor done and material furnished; and the Legislature shall provide, by law, for the speedy and efficient enforcement of such liens.

Various provisions of the Civil Code provide for creation and enforcement of mechanic's liens and govern payment provisions contained in contracts for works of improvement to real property. Civ. Code §§ 3109-3154.

As we understand it, the mechanic's lien law may operate to the detriment of an innocent homeowner. For example, the situation may arise where a homeowner or residential land improver executes a contract with a general contractor to make an addition to a home or improve a vacant lot. Often, the homeowner will agree to pay the general contractor in full for all services to be performed upon his or her land. The general contractor then hires subcontractors, laborers and materialmen to make the required improvements. In some instances, the general contractor may fail to pay these persons for the value of their work. These persons, under California law, have the right to place a lien upon the improved property which forces the homeowner, whose property is encumbered, to pay twice or forfeit his or her land to satisfy the lien. Under current law, the homeowner may not interpose as a defense the fact that the homeowner already has paid the full contract price to the general contractor.

Existing law provides that the amount of a mechanic's lien shall be for the reasonable value of the labor, services, equipment, or materials furnished or for the price agreed upon, whichever is less, but that any original contractor or subcontractor may recover only such amount as may be due under the terms of a contract, after deducting all claims of other claimants for labor, services, equipment, or materials furnished and embraced within the contract. Existing law authorizes the owner of property to petition the proper court for an order to release the property from the lien if specified conditions are met.

Several proposals to protect the homeowner from the burden of paying twice for the same work have been circulated for consideration. There are difficulties with each of these proposals, both political and practical, which have been noted at the Commission's recent meetings on this topic.

In an effort to assist the Law Revision Commission and the Legislature in their consideration of this issue, we propose an alternative solution to the problem of double-payment by homeowners. As we see it, the double-payment problem is best approached through an insurance-type program. Under current law, most homeowners are at risk of a double-payment situation, although most homeowners are either unaware of the risk or willing to take that risk in order to avoid the costs of protecting themselves against it. In an idealized world, an enlightened homeowner who wished to avoid the risk of a mechanics' lien would purchase insurance against such a risk (or would self-insure). Then, if a mechanic's lien is placed upon the property because of non-payment by the general contractor, and the owner has already paid the general contractor, the lien holder could be paid from the insurance funds, resulting in the lien being discharged.

Assemblyman Honda's proposal seems to recognize the insurance-like nature of the problem. AB 2113 proposes creating a Contractor Default Recovery Fund ("CDRF") which would be used to satisfy claims of non-payment by sub-contractors who provide labor, service, equipment, or material to an improvement on residential property. This would protect homeowners who have already paid a general contractor from having to pay a sub-contractor to satisfy the lien obligation.

Although AB 2113 is intended to protect homeowners, it proposes to finance the CDRF by initially imposing a $200 annual fee upon licensed home improvement contractors and giving the Contractors' State License Board the responsibility for recommending adjustments to the fee to meet the projected claims over the next year.

On first glance, it is arguably appropriate to finance the CDRF from fees paid by home improvement contractors since those contractors, as well as home owners, stand to benefit from creation of the CDRF. However, under current law, home improvement contractors already have a potent weapon to collect payments through the lien law, a weapon that has constitutional support. Thus, from the perspective of home improvement contractors who are comparing AB 2113 with existing law, AB 2113 increases the cost of

doing business without creating significantly greater security for payment than currently exists. Moreover, it is not at all clear that the burden of additional fees would actually weigh equally upon all contractors. For example, sub-contractors who have established long-standing, stable relationships with general contractors and who may never face the problem of non-payment will be required to pay the same fee as sub-contractors who are at a much greater risk of non-payment.

Arguably, since AB 2113 would impose the identical fee upon all home improvement contractors, the increased costs would ultimately be borne, at least in some measure, by homeowners (since subcontractors would attempt to pass the increased cost to general contractors who, in turn, would attempt to pass the increased cost to homeowners). Since the primary benefit of AB 2113 is to homeowners (compared to existing law), it is appropriate that homeowners be responsible for paying for any statewide insurance program.

Our proposal builds upon Assemblyman Honda's AB 2113. As with AB 2113, we propose creation of a fund, called the Homeowner's Relief Recovery Fund ("HRRF"), to be administered by the Contractors' State License Board, which would be used to make payments to sub-contractors or homeowners in situations where the homeowner has already paid the general contractor for work performed by the sub-contractor (we are uncertain whether the program is best administered by having a sub-contractor make a claim against the fund or having a homeowner make a claim against the fund). Since the primary benefit of the fund is to homeowners, we propose that a modest Homeowner's Lien Protection Fee be added to residential building permit fees. The Homeowner's Lien Protection Fee would be collected by the local jurisdiction at the time a residential building permit is issued and, after a deduction for local expenses associated with collection of the fee, would be forwarded to the State Treasury for deposit in the HRRF.

We are not breaking any new ground in proposing that a state fund be financed by fees on building permits. The Strong Motion Instrumentation Program (Pub. Res. Code §§ 2700-2709.1) requires that all persons receiving building permits pay an additional fee, the amount of which is in relation to the total value of all labor and material to be used within a building project. Pub. Res. Code § 2705. Thus, there is already a mechanism for using county and city building permit fees to support a statewide program.

As with the Strong Motion Instrumentation Program, we propose funding the Homeowner's Relief Recovery Fund through a small fee added to the fees already charged for the issuance of residential building permits which are issued to the homeowner or land improver. This fee would be a small fraction of the value of the proposed improvement, including the value of all labor and materials used. Under this approach, the cost of protecting homeowners against the risk of double-payment will be borne by homeowners themselves, which is appropriate since they are the ones who most directly benefit from the change in law proposed by this legislation.

Because of the uncertainty regarding the exact scope of the double-payment problem, we have not attempted to suggest how large the fee should be to provide sufficient funds for the Homeowner's Relief Recovery Fund to operate properly. However, if a reliable estimate of the yearly costs can be developed, it will be a straightforward process to determine the rate for the fee based upon the funds raised by the Strong Motion Instrumentation Program.

I am sorry that I will not be able to attend the meeting in San Diego this week, but my duties as Acting Insurance Commissioner require my attendance elsewhere. If there are any questions I can answer before the meeting, please do not hesitate to call me at the Department of Insurance (916-492-3500).

Sincerely,

J. Clark Kelso
Director

cc: Mike Honda

PROPOSED LEGISLATION

SECTION 1. Article 8 (commencing with Section 3155) is added to Chapter 2 of Title 15 of Part 4 of Division 3 of the Civil Code, to read:

Article 8. Homeowner's Relief Protection Fund

3155. This article shall be known and may be cited as the Homeowners Relief Recovery Act of 2000. 3155.1. For purposes of this article, the following definitions shall apply: (a) "Board" means the Contractors' State License Board. (b) "Claimant" means a homeowner or residential land improver who has a lien placed upon his residence by a person, other than an original contractor, who provides labor, service, equipment, or material to a work of improvement on property with an existing single-family owner-occupied dwelling pursuant to a contract entered into on or after January 1, 2001, with an original contractor, or any of the original contractor's subcontractors or subcontractors, and who records a lien upon that real property for the reasonable value of labor, services, equipment, or material provided or supplied to the property. (c) "Full payment" and "paid-in-full" means that the person who provided his or her labor, services, equipment, or material has received compensation for that labor, service, equipment, or material in an amount equal to the reasonable value of that labor, service, equipment, or material. A person shall not be considered to have been paid in full if 10 percent or more of any retention proceeds have been withheld. (d) "Fund" means the Homeowner's Relief Recovery Fund. (e) "Original contractor" is a person who has a direct contractual relationship with the owner of an existing single-family, owner-occupied dwelling to provide labor, services, equipment, or material toward a work of improvement on that property. (f) "Owner" is a person who is the record owner of a single-family dwelling that is his or her primary residence. (g) "Lienholder" is any contractor, subcontractor, materialman, laborer or artisan, not in direct contractual privity with the claimant, who has not received the reasonable value of their services due to the unscrupulous nature of a general contractor in contractual privity with the claimant, where the general contractor was paid in full for the reasonable value of such lienholder's

labor or materials. 3155.2. (a) A lienholder shall not be entitled to maintain an action to foreclose a recorded lien against the property pursuant to any other provision of law unless a hearing officer determines that the owner has not paid the original contractor in full in a hearing held pursuant to this article or the owner has not complied with subdivision (b). (b) In order for an owner to receive the protection of this article against foreclosure on a lien, the owner shall do all of the following: (1) Hire only licensed original contractors pursuant to a written contract. (2) Prepare an affidavit, under penalty of perjury, that the owner has paid the original contractor in full. (3) Record the affidavit within 30 days of receiving a notice of lien from the claimant pursuant to Section 3097. (4) Serve the affidavit upon the lienholder. 3155.3. (a) There is hereby established within the State Treasury the Homeowner's Relief Recovery Fund, which is hereby continuously appropriated for the purpose of administering this article, including paying the compensation of hearing officers appointed pursuant to Section 3155.13, and providing monetary relief to any claimant who is not paid in full for labor, services, equipment, or material. (b) Notwithstanding any other provision, payments from the fund to satisfy claims against it shall not exceed: (1) Seventy-five thousand dollars ($75,000) per single-family, owner-occupied residence for all claims brought against that property. (2) Five hundred thousand dollars ($250,000) per claimant over the claimant's lifetime. (c) If claims against the fund exceed the limit in paragraph (1) of subdivision (b), the seventy-five thousand dollars ($75,000) shall be awarded proportionately so that each claimant who is awarded compensation from the fund shall receive an identical percentage. (d) The state shall not be liable for any claims against the fund except as provided in this article. 3155.4. In order to establish a claim from the Homeowner's Relief Recovery Fund, a claimant shall provide evidence that he or she has a recorded against his or her property pursuant to this chapter. 3155.5. (a) The Contractors' State License Board shall administer the Home Owner's Relief Recovery Fund and shall develop rules and regulations to administer the fund pursuant to this article. (b) The board may file a civil action against any licensed original contractor in order to obtain reimbursement to the fund for any payments made to a claimant upon a finding by a hearing officer that the original contractor failed to pay the claimant in full.

3155.6. (a) All counties and cities shall collect a fee from each applicant for a building permit. Each such fee shall be equal to a specific amount of the proposed building construction for which the building permit is issued as determined by the local building officials. The fee amount shall be assessed in the following way: (1) All homes qualifying as a single family residence shall be assessed at the rate of fifty dollars ($50) per one hundred thousand dollars ($100,000), with appropriate fractions thereof. Off the amount assessed forty-five dollars ($45) shall go to the Homeowner's Relief Recovery Fund. Of the amount assessed five dollars ($5) shall go to the local city or county collecting the fee. (2) The fee will be assessed upon all construction performed upon existing single-family residences and single-family residences where construction is yet to commence. (3) The fee will only be assessed to building permits for single family residences, no other building permit applicants will be assessed the fee. (b) The board shall annually determine whether the fees collected are sufficient to meet the projected claims over the next year and annually report to the Legislature on the need to increase or decrease fees accordingly. In making this determination, the board shall not include in any fund balance moneys in the fund that are encumbered by claims approved pursuant to this article. (c) The board shall be responsible for an annual review or audit of the fund. 3155.7 All fees collected pursuant to 3155.6, except those retained by the local city or count collecting the fee, shall be deposited in the State Treasury in the Homeowner's Relief Recovery Fund, which is hereby created, to be used exclusively for the purposes of this chapter. 3155.8. Notwithstanding any other provision of law, the time for a lienholder to bring an action to foreclose a lien shall be extended to, and include, 60 days following service of the decision by a hearing officer regarding the claimant's claim against the Homeowner's Relief Recovery Fund. 3155.9. Within 90 days after the lienholder has recorded a lien on a single-family owner-occupied dwelling which is the primary residence of the owner, the claimant shall file with the Contractors' State License Board a statement of claim. This statement of claim shall include, but may not be limited to, the following: (a) A copy of the contract, purchase order, invoices, delivery tickets, credit application, or other documentation reflecting the claimant's contractual relationship to the general contractor. (b) A copy of any preliminary notice given

by the lienholder to the claimant, together with the proof of service accompanied thereby, if a lienholder is otherwise required to serve a preliminary notice. (c) A copy of the mechanic's lien recorded in the office of the county recorder. (d) A statement of account showing all charges, credits, and balance due, if any. (e) Proof of service of the appropriate documents described in subdivisions (a) to (d), inclusive, to both the original contractor and the owner. 3155.9. Once the statement of claim described in Section 3155.8 has been filed with the Contractors' State License Board, the board shall notify the original contractor and the lienholder of the filing of the claim. The original contractor shall file a response within 15 days after receipt of the notice. This response shall state in detail the defense against the claim and include all documents which the respondent claims support this defense. If the original contractor contends that it has not been paid in full, the original contractor shall provide a copy of all documents in support of this contention. The claimant, original contractor, and lienholder shall submit any other information to assist the hearing officer to make the determinations required by this article. 3155.10. If the original contractor fails to respond to the claim filed by the claimant, the hearing officer shall find that the owner paid the contractor in full and then determine the value of the claim based upon the documentation provided. 3155.11. The board shall set a hearing date within 60 days of receipt of the statement of claim at the office of the Contractors' State License Board nearest to the site of the work of improvement before a hearing officer appointed by the board pursuant to Section 3155.13 to hear the presentations of the claimant, the original contractor, and the lienholder. To the extent possible, all claims submitted on the same project shall be consolidated and heard in the same hearing. The Contractors' State License Board shall provide notice to the original contractor, the claimant and the lienholder of the date, time, and location of this hearing. 3155.12. At the hearing, the hearing officer shall first determine whether the claimant has made a full payment to the original contractor. If the hearing officer determines that the claimant has not paid the contractor in full, the hearing officer shall dismiss the claim and issue a finding that the lienholder may pursue foreclosure of its mechanic's lien in the appropriate court. If the hearing officer determines that the claimant has paid the original contractor in full, the hearing officer shall determine the

validity and reasonable value of the claim and, if determined to be valid, enter an order addressed to the Contractors' State License Board directing it to pay the lienholder the amount of the claim, subject to subdivision (b) of Section 3155.3. 3155.13. (a) The hearing shall be conducted in accordance with Chapter 5 (commencing with Section 11500) of Part 1 of Division 3 of Title 2 of the Government Code. (b) The hearing officers appointed by the Contractors' State License Board shall be attorneys licensed to practice in this state with at least five years of experience in mechanic's lien law. 3155.14. (a) The findings of the hearing officer shall be final and impose obligations upon the claimant, original contractor, and lienholder only to the extent that the claimant, original contractor, or lienholder agree to be bound by those obligations. However, the remedies available to a party pursuant to this article, including the right to receive payment from the fund, shall not be available to a party that does not agree to the obligations. A lienholder shall be deemed to agree to the obligations only by recording a release of the lien in the county recorder's office where the real property is located. The findings of the hearing officer may be entered into evidence in any subsequent civil action or proceeding. The findings of the hearing officer shall be served on the claimant, original contractor, the lienholder, and the board no more than 10 days after the hearing. (b) The Contractors' State License Board shall pay to the lienholder, upon receipt of an order pursuant to Section 3155.12, the amount of the claim, subject to subdivision (b) of Section 3155.3, within 10 days of receiving evidence that the lienholder has recorded a release of its lien in the county recorder's office where the real property is located. This evidence shall be submitted within 15 days after findings of the hearing officer are served. 3155.15. A finding by the hearing officer that the original contractor was paid in full by the claimant and failed to make timely payments to any lienholder on the work of improvement, except a finding made pursuant to Section 3155.10, shall be grounds for immediate suspension of the original contractor's license. The original contractor shall be given notice of a hearing to challenge the finding, which shall be conducted within 60 days of the date of the suspension, pursuant to the procedures of the Contractors' State License Board. If the finding is sustained, the contractor's license shall be immediately revoked and shall not be reinstated until the original contractor can supply to the Contractors' State

License Board a contractor's license bond as provided in Section 7071.8 of the Business and Professions Code in the sum of fifty thousand dollars ($50,000). 3155.16. The county recorder shall make available forms for the affidavit described in Section 3155.2 and a notice regarding the owner's rights under this article. The Judicial Council shall adopt forms for the affidavit and the notice. SEC. 2. No reimbursement is required by this act pursuant to Section 6 of Article XIIIB of the California Constitution for certain costs that may be incurred by a local agency or school district because in that regard this act creates a new crime or infraction, eliminates a crime or infraction, or changes the penalty for a crime or infraction, within the meaning of Section 17556 of the Government Code, or changes the definition of a crime within the meaning of Section 6 of Article XIIIB of the California Constitution. However, notwithstanding Section 17610 of the Government Code, if the Commission on State Mandates determines that this act contains other costs mandated by the state, reimbursement to local agencies and school districts for those costs shall be made pursuant to Part 7 (commencing with Section 17500) of Division 4 of Title 2 of the Government Code. If the statewide cost of the claim for reimbursement does not exceed one million dollars ($1,000,000), reimbursement shall be made from the State Mandates Claims Fund.

STATE OF CALIFORNIA -- STATE AND CONSUMER SERVICES AGENCY GRAY DAVIS, *Governor*

CONTRACTORS STATE LICENSE BOARD
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(916) 255-4000

July 17, 2000

Dear Mr. Ulrich:

Re: **Mechanics' Liens**

Thank you for sending a copy of the proposals. I have not had a chance to digest them yet. I am concerned about one point of view expressed in the memorandum. You state, on EX6 in the staff note on section 3155.1 that "In any event, commentators are unanimous that the potential for a double payment is a rare occurrence." I don't think this is true.

It is true that CSLB does not have massive evidence of double payments. Most double payment cases end up in civil court or bankruptcy without CSLB involvement. Sometimes, the lien becomes an issue only when the homeowner is selling the home and the left-over lien is an impediment. I have personally spoken to real estate professionals who regularly advise their clients to pay so that the sale can go through.
Sam Abdulaziz and Gordon Hunt told us all that removing most liens is a simple matter for an attorney. On the other hand, our Enforcement deputies have reported that fear of the cost of hiring an attorney acts against seeking legal advice. People are afraid they will have the lien *and* the cost of the attorney.

Another problem might be attorneys who don't understand liens. Every once in a while, CSLB can document a case that demonstrates double payment. I just got a report from one of our Enforcement deputies. A San Francisco contractor went bankrupt last year. At least 4 homeowners had already paid the contractor for work performed by the subs when the contractor declared bankruptcy. Faced with liens, all 4 were advised to pay by their attorneys. The amounts the homeowners claim to have paid (twice) are: $49,254; $81,050; $74,742: $170,425. I am checking further into this report and other reports of double payment. In any event, I don't think double payment is rare.

Thank you for the opportunity to participate in this process. If you have any questions or want to talk, please call me at 916-255-4116 or e-mail me at EGallagher@dca.cslb.ca.gov. I'll be in the office Tuesday but in San Diego Wednesday.

Sincerely yours,

Ellen Gallagher, Staff Counsel
Contractors State License Board

Date: Tue, 18 Jul 2000 10:55:30 -0700
To: sulrich@clrc.ca.gov
From: Abdulaziz & Grossbart <aglaw@earthlink.net>
Subject: Your Memorandum 2000-47

July 18, 2000

SENT VIA E-MAIL & US MAIL
sulrich@clrc.ca.gov

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

RE: YOUR MEMORANDUM 2000-47

Dear Mr. Ulrich:

I'm sending this again by e-mail and regular mail.

I have very quickly reviewed your memorandum and put together this letter. I did not have sufficient time in that I am traveling today. The following comments should not be deemed to be exclusive. I will give the memo a closer reading after the upcoming meeting. I did want to respond quickly to give you more general thoughts so that you and the Commission will have some discussion material. My comments will follow the order of your proposal.

At the outset, before getting into the bases of the two proposals, we have already told you about problems with the direct pay proposal and that we feel that a constitutional amendment would be required for the "Full Payment Defense." With that in mind, we make the following comments:

With respect to forms, you may consider having the Commission legislate exact language in that the future of the Contractors' Board is presently in question.

If the Commission decides to use the definition of home improvement in the Business & Professions Code, I would suggest revising that definition. In that the home improvement laws are intended to protect consumers, it seems ludicrous to have some Deputy Registrars require home improvement protection for apartment house owners. Clearly, an owner of an apartment house of 50 units is sophisticated enough to protect him/herself. That is actually commercial work and not home improvement work.

DIRECT PAY PROPOSAL

With respect to your direct pay proposal, Section 3107.2(d), we would suggest that you require a subcontractor or material supplier to provide a direct pay notice to his/her customer. In that way, one supplying a subcontractor would give a notice to his/her customer so that the customer can at least have knowledge of it and have an opportunity to dispute the notice. How would the direct pay proposal affect a lender?

Proposed Section 3107.3 itself seems to be unconstitutional. As the comment demonstrates, if the claimant does not get to the owner with its Direct Pay Notice before the owner has paid the contractor, the claimant will have lost its lien rights and will only be able to look to his or her customer. While this might seem palatable if a long period of time has lapsed, such as the time in which to record a Mechanic's Lien presently is stated in the Civil Code, what happens when you have an owner who pays promptly upon completion? This would be a real problem on many home improvement projects, including roofing and air conditioning, where the work is done in a very short period of time.

One possible solution would be to allow the Direct Pay Notice to be served using the time period for the service of a Preliminary Notice.

With respect to Business & Professions Code Section 3107.4, again you may wish to require the person giving the direct pay notice to list the name and address of his/her customer.

FULL PAYMENT DEFENSE

With respect to the full payment defense we still believe that this is unconstitutional. However, we make the following comments as well:

First, the memorandum gives a wrong impression as to the time for filing suit. The memo states that "liens are lost if an action is not commenced within 90 days after completion (or 30 days after recording notice)." First, there is distinction between the right to the lien and the lien itself. The right to record a lien is lost if not reached within the required time frame.

Second, although the lien must be recorded within that time, the action need not be commenced until 90 days after the recording of the lien itself.

In general, with respect to the good faith payment in this proposal, I'm not sure what "good faith" would mean unless you are talking about collusion between the prime contractor and the owner.

We also don't believe that the claimant is making a mutually exclusive choice. The claimant should be able to pursue a claim against both the owner and his or her customer. Why should the claimant have to give up a contractual remedy to pursue the lien remedy?

With respect to Section 3097(b), I would again question the words "except the contractor." I don't know what that means when used in conjunction with, "...all persons who have a direct contract with the owner," in that those words appear to be synonymous.

In that same Section, we would delete subsection (h). First, I do not know why a contractor should be disciplined for not preserving his/her mechanic's lien rights. Second, I have been following the Contractors' State License Board for over 25 years and have never heard of a contractor being disciplined for a violation of that Section.

The same comment applies to Section 3098(b).

With respect to Section 3104, I would add the words, "but has a relationship with a contractor or subcontractor on a particular work of improvement" at the end of the sentence.

With respect to Section 3105, "subdivision" -- would that lead one to believe that apartments are subdivisions?

As I said before, I reviewed your comments very, very quickly, and will give them a closer reading after the meeting.

Very truly yours,
ABDULAZIZ & GROSSBART
SAM K. ABDULAZIZ