Study H-821 October 11, 2006

Memorandum 2006-39

Mechanics Lien Law
(Comments on Tentative Recommendation)

The Commission has circulated a tentative recommendation on *Mechanics Lien Law* (June 2006), which proposes a complete revision of the California mechanics lien law and associated construction remedies. The tentative recommendation, which included a draft statute, was posted on the Commission's website and widely circulated for comment. The recommendation requested responsive comments by September 30, 2006.

We have received a substantial number of detailed comments on the tentative recommendation, both before and after the requested response date, and have been advised by prospective commenters that additional comments will be forthcoming shortly.

The comments that have been received to date are attached in the Exhibit to this memorandum, as follows:

Exhibit p.

- Rodney Moss, Los Angeles (8/14/06) 1
- Graniterock, Watsonville (9/11/06) 3
- Lori Nord, San Francisco (9/12/06) 12
- Sam Abdulaziz, North Hollywood (9/20/06) 13
- Howard Brown, Manhattan Beach (9/21/06) 21
- Michael Brown, Sacramento (9/21/06) 46
- Paul Crane, Los Angeles (9/25/06) 47
- Jeffrey Ward, Oakland (9/25/06) 49
- J. David Sackman, Los Angeles (9/27/06) 53
- Regents of the University of California, Oakland (9/29/06) 81
- William Last, San Mateo (9/29/06) 85
- American Insurance Association, National Association of Surety Bond Producers, and Surety & Fidelity Association of America (9/29/06) 88
- California State University, Long Beach (9/29/06) 101
- Building Owners and Managers Association (10/2/06) 105
- Association of California Surety Companies, Sacramento (10/2/06) . . . 112
- Joseph Melino, San Jose (10/2/06) 128
- Gibbs, Giden, Locher & Turner LLP, Los Angeles (10/2/06) 131

We will supplement this memorandum with any additional comments received before the October Commission meeting.

We are preparing a staff analysis of the comments, which we are producing in two separate documents. General comments, and comments addressed to the statutes governing a private work of improvement, are analyzed in Memorandum 2006-43. Comments addressed to the statutes governing a public works contract, comments on overarching issues, and comments on conforming revisions, are analyzed in Memorandum 2006-44.

We hope that by fragmenting the memoranda in this way, we will facilitate the Commission's review of this substantial body of material.

Respectfully submitted,

Steve Cohen
Staff Counsel

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August 11, 2006

California Law Revision Commission
4000 Middle Field Road
Room D-1
Palo Alto, California 94303-4739

Re: Tentative Recommendation Mechanic's Lien Law

Gentlemen:

I have been practicing in the area of Mechanic's Liens and related remedies since July of 1961 and I have written many articles and lectured for CEB and others on the subject. I have previously communicated with you. Having just received your tentative recommendation, I will give you my thoughts on the issues which you have directly raised with those persons to whom you have sent a copy of the tentative recommendation.

With regard to the section on mailed notice, it seems clear to me that overnight delivery by a private express service carrier is appropriate. The only issue is ability to prove that the notice was given and that should not be a problem with overnight delivery by a private overnight express service carrier.

With regard to proof of mailing, I believe that the reliability of mail delivery by the United States postal service is absolute. If it can be established that the item was mailed, there must be a presumption that it was received.

With regard to separate contracts on a single job, I don't have an opinion one way or the other, but the law in this area has been well established for a long period of time and therefore my recommendation would be to leave the situation as it is.

With regard to attorney's fees, I would like to see consistency between a stop notice and a mechanic's lien. Probably the basis for attorney's fees and a stop notice to a construction lender has to be bonded, escalating the risk to the party who defends or asserts a stop notice claim. Therefore the legislature added attorney's fees. Once one party is entitled to attorney's fees if the matter goes to trial, obviously it must be reciprocal. The law has long been that there are no attorney's fees allowed on a mechanic's lien claim and therefore, on balance, I would leave the law as it is.

With regard to reduction of amount of claim on a stop payment notice, it seems clear to me that the waiver form should apply equally to a stop notice payment claim as to a

Mechanic's Lien claim. I believe the legislation that you are referring to has to do with the public work of improvement and not a private work of improvement.

With regard to the day notice that suit has been filed or a stop payment notice, I do not believe that the five-day notice should be made mandatory. Practitioners regard the issue as set forth in Sunlight Electric so that, if there is no prejudice, failure to give the five-day notice has no consequence and I believe the law should remain as it is even though Sunlight Electric arose on a public work of improvement.

With regard to a statute of limitations for enforcement of bond, I don't believe that you have correctly stated the law. I believe that a surety can reduce the statute of limitations to six months by timely recording the bond, but unless that language is included in the bond, the statute of limitations is four years, contrary to what you have stated in the prelude to the tentative recommendation. There has been no requirement that an owner provide a copy of the payment bond to a claimant prior to this time and I don't believe that it would be wise to include such a provision in the new statute

With regard to cessation of labor, I wrote an article some time ago in which I suggested that the law with regard to cessation of labor on public works should be exactly the same as that on private works and that is what I believe you should set forth in the tentative recommendation. With regard to notice of cessation, you have requested comments from State agencies but I will comment nevertheless. I have not found a recorded notice of cessation by a public entity in my 45 years of practice. I don't think it would be wise to insert a provision regarding recording a notice of cessation by a public body in the tentative recommendation.

With regard to disciplinary action for failure to give preliminary notice, I believe you are absolutely correct that there is no reason to penalize a contractor for failing to give a preliminary notice if he chooses not to do so.

I am hopeful that my comments will be of some use to you and I have certainly appreciated receiving the mailings on the tentative recommendation which I have been receiving now for some substantial period of time.

Very truly yours,

MOSS, LEVITT & MANDELL

Rodney Moss

By Rodney Moss

RM:amp

EX 2

Graniterock

September 8, 2006

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

Re: Mechanics Lien Law Tentative Recommendation

Malcolm Baldrige National Quality Award 1992 Winner

Dear Commission:

Thank you for providing the opportunity for public comment on the June 2006 Mechanics Lien Law Tentative Recommendation. This letter provides the comments of Granite Rock Company ("Graniterock").

Graniterock is a construction material supplier and contractor. We have been in business in California since 1900, and our construction division holds California Contractor's License number 22. We supply materials, including concrete, asphalt, aggregate, masonry, natural stone, and other building materials to a wide range of public and private works projects throughout Central California. Our customers range in size from homeowners to large developers to State and Federal agencies. We serve thousands of preliminary 20-day notices each year, and regularly rely on our Mechanics Lien Law remedies when other payment options fail. Our construction division is one of the largest road building contractors in the state, and we have constructed engineering works from residential driveways to interstate highways and international airport runways. In addition, as a property owner we have contracted for the construction of many plants and buildings to support and grow our business operations. This history and diversity of construction experience provides us with a balanced perspective on the Mechanics Lien Law. We hope our perspective will be useful in the adoption of your final recommendations.

We have substantive comments on 14 specific issues raised by the tentative recommendation. Before offering those, we wish to say that we enthusiastically support the revision of the Mechanics Lien law and the approach taken by the Commission to the revision. Overall it appears to us the Commission has achieved its goal of making the law more simple and clear, while maintaining the balance of interests of the various stakeholders. In our view, the piecemeal nature of the past revisions to the Lien Law has resulted in confusion, needless expense to change forms and procedures for very little benefit, reversals, and unintended negative consequences from well meaning tinkering with the law. We applaud the comprehensive modernization. Our specific comments and questions follow.

• Monterey County
• San Benito County
• San Mateo County
• Santa Clara County
• Santa Cruz County
• Alameda County
• City and County of San Francisco

Material Supplier/ Engineering Contractor
License #22

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1. The Commission Should Expressly Make Clear That the Proposed Revisions to the Public and Private Works Payment Bond Remedies and the Public Works Stop Payment Notice are Not Intended to Limit Lower Tier Subcontractors and Suppliers from Exercising Those Remedies.

This is our single largest concern with the proposed revision. Under existing law, it is well settled that the persons (other than direct contractors) who can file public works stop notices and public or private works payment bond claims are generally coextensive with those that have mechanics lien rights. See, e.g. Civil Code sections 3181 (public works stop notices) and 3248 (public works payment bond); *Mechanical Wholesale v. FUJI Bank, Ltd.*, 42 Cal. App. 4th 1647 (1996). It had been argued in the past that the California payment bond law should be interpreted consistent with the Federal payment bond law (Miller Act) upon which it was originally modeled, to limit claimants to first and second tier subcontractors and suppliers. The courts have rejected that argument under the existing statutory language. *Union Asphalt, Inc. v. Planet Ins. Co.*, 21 Cal. App. 4th 1762 (1994).

Our concern with the proposed revision is that the new language allows this issue to be raised again. The proposed payment bond and public works stop payment notice statutes could be read to limit those remedies to claimants who supply labor, services, material or equipment to "the direct contractor or one of the direct contractor's subcontractors." See, e.g., proposed Civil Code section 7608; proposed Public Contract Code sections 42030(a)(1) ("pursuant to an agreement with a direct contractor") and 45090 ("direct contractor's subcontractor").

We acknowledge the term "subcontractor" is broadly defined under the proposed revision to include subcontractors of every tier. Nevertheless, an argument could be made that the phrases "direct contractor's subcontractor" and "pursuant to an agreement with the direct contractor" could be intended to modify and narrow the class of subcontractors or suppliers that have payment bond or stop notice rights. Strictly speaking, a third tier subcontractor or supplier is not a "direct contractor's subcontractor" and does not perform work "pursuant to an agreement with the direct contractor."

Since limiting these remedies to those who have a contract with a direct contractor or a direct contractor's subcontractor would be a major departure from the existing law and would decidedly change the balance of interests among current stakeholders, we assume that is not the Commission's intent. We strongly oppose any such change in the law. We suggest clarifying language be added to the

relevant sections to make expressly clear that the payment bond and public works stop notice remedies are available to lower tier subcontractors and suppliers, as has been the case historically.

2. The Notice of Intended Recording of Lien Provisions Should be Eliminated.

Proposed Civil Code sections 7420 and 7422 add a new prerequisite to the recording of a lien—a "notice of intended recording." We do not feel this additional notice adds any meaningful protection to owners, and will unnecessarily complicate the recording of liens. Under existing law the preliminary notice gives property owners the information required to protect themselves against lien claims. If an owner does not avail itself of that protection, there is likely little that can be done in response to a notice of intent to record a lien served days before the lien is recorded. In our business we have frequently used an informal notice of intent to record lien as a means to motivate payment, and our experience is this practice is seldom effective. At the stage of a project when liens are about to be recorded, an owner has either paid the prime contractor without protecting itself with releases from subcontractors and suppliers, or there is some reason the owner has not paid (default or good faith dispute). In either case, a notice that a lien is forthcoming has little effect. All the new proposed notice requirement would do would make it more difficult to record valid lien claims, put County Recorders in a difficult position with respect to verifying compliance with the notice of intent requirement, and foster litigation over compliance with the requirement. We urge sections 7420 and 7422 be eliminated.

3. Proposed Civil Code Section 7160 and Public Contract Code Section 42310 Should Provide That Subcontractors May Not Require the Waiver or Impairment of Lien Rights.

Proposed Civil Code section 7160 and Public Contract Code section 42310, limiting the ability to require lien waivers by contract, track current Civil Code section 3262. Like existing law, these sections prohibit any "owner or direct [original] contractor" from impairing lien rights. In light of the important public policy underlying these sections, it appears that the omission of subcontractors from the list of those who cannot impair lien rights in the original legislation was mere oversight. We can think of no good reason why an owner or direct contractor cannot impair lien rights of a subcontractor or supplier, but a subcontractor can. We ask that the Commission use this opportunity to correct this apparent oversight,

by providing that "No owner, direct contractor or subcontractor may... impair a claimant's rights...."

4. The Proposed Law Should Make Clear That a Notice of Completion That Does Not Meet the Requirements of Proposed Civil Code Section 7152 Does Not Shorten a Claimant's Time to Record a Lien or Enforce Other Remedies.

The proposed law does not expressly state the effect of a notice of completion that does not meet one or more of the requirements of proposed Civil Code section 7152. While that tracks the existing statute, we note that in revising the definition of the notice of nonresponsibility, the Commission added a provision stating that a late posted or recorded notice of nonresponsibility "is not effective." Proposed Civil Code section 7444(c). Our concern is that the lack of a congruent change to the notice of completion statute could be interpreted to mean the Commission intended late or flawed notices of completion to be effective. We request that Proposed Civil Code section 7152 include language stating that notices of completion that do not meet the requirements of the section are not effective to shorten the time to exercise remedies.

5. The Proposed Law Creates Uncertainty as to the Amount of Stop Payment Notice Claims, and for Public Works Projects Creates the Possibility That Stop Payment Notices for More Than Unpaid Value of the Work Performed Could be Asserted.

Unfortunately, the existing stop notice statutes are not clear on the amount that can be claimed in a stop notice. Civil Code section 3103 (private works) provides only that the stop notice must state the "amount in value...of that already done...and of the whole agreed to be done...," but does not address the amount of the claim to be asserted. The proposed revisions track this language. Since a stop notice may be filed before the claimant's entire contract is performed, the amount of the claim is properly the amount actually due and unpaid as of the date of filing, and not the entire remaining balance of the contract. Case law has filled this gap in the existing stop notice statutes by applying Civil Code section 3123, which establishes a "reasonable value of work performed" limitation for mechanics liens, to stop notices. See, *University Casework Systems, Inc., v. Superior Court*, 41 Cal. App. 3d 263 (1974) (applying reasonable value of work performed limitation of Civil Code section 3123 to a public works stop notice).

Our concern is that the public works remedies are proposed to be removed from the Civil Code (where the new counterpart to Civil Code section 3123 resides),

and there is nothing similar to Civil Code section 3123 in the Public Contract Code. This opens the door for public works stop payment notices to be asserted for amounts not yet earned by the claimant, on the argument that Civil Code provisions governing mechanics liens no longer limit public works remedies. Stop payment notices should not be for the difference between the "amount provided and the whole agreed to be provided", but for the amount earned but unpaid. Without clarity on the amount of the claim, or a limit along the lines of existing Civil Code section 3123, large stop payment notices for unearned amounts could unfairly tie-up the flow of funds on public projects. The proposed Public Contract Code provisions need to include a statute analogous to existing Civil Code section 3123, or some other clarification on the amount of the claim.

6. The "Second Chance" Notice in Support of Payment Bond Claims Should be Deleted.

The proposed revision continues a controversial hangover from the time that the preliminary notice requirement was first applied to payment bonds. Proposed Civil Code section 7612(b) and Public Contract Code sections 45060(b) and 45070. Prior to 1995, payment bond claimants were not required to serve a preliminary notice to enforce their rights. When the legislature changed this in 1995, it apparently attempted to mitigate the effect of the change by creating a late notice to the surety of an intention to make a payment bond claim, as an alternative to the preliminary notice. Civil Code sections 3242(b) and 3252(b). Claimants who neglect to serve the preliminary notice at the start of their work can be saved by filing the alternate notice to the surety at the end of the job. No similar "second chance" is provided in the law for lien or stop notice remedies.

We request that this second chance notice provision be dropped from the revision for two reasons. First, the late notice only serves to reward the neglectful claimant, while subjecting direct contractors who attempt diligently to administer an effective release and waiver program to surprise claims at the end of the job. This is even more of a problem as the legislature and public owners call the practice of withholding retention from subcontractors into question. On federally funded Caltrans projects, for instance, direct contractors are now precluded from withholding retention from subcontractors. This means more frequently subcontractors who perform work early in the life of a project are fully paid well before their subcontractors and suppliers are required to file the late notice to surety to make bond claims. This exposes direct contractors and their sureties to surprise claims at the end of the job, leaving little or no recourse against the subcontractor

who created the payment problem. There is no reason to treat bond claimants differently than stop notice and lien claimants. All should have to file the preliminary notice, and there should be no second chance alternate.

The second reason to fix this issue in the course of the comprehensive revision of the lien law is that there have been, and will continue to be, attempts to delete this late notice through piecemeal legislation (including one currently underway—see AB 411 (Yee)). Each of these prior attempts, in our opinion, has suffered from some flaw stemming from a fundamental misunderstanding of the lien law, or included other changes that either confuse the rights of the parties or attempt to change some other portion of the law that does not need changing. It would be better for the integrity to the law overall to fix this issue now rather deal with inevitable piecemeal changes in the future that could undo the fair and thoughtful systematic revision of the law. Put another way, if the Commission doesn't recommend this change, someone else will and will likely do damage to the integrity of the statutory scheme along the way.

7. The Changes to the Mailing and Proof of Delivery Requirements are Appropriate and Necessary.

The Commission has specifically requested comments on the modernization of the mailing and proof of mailing requirements for notices sent under the Mechanics Lien Law (e.g. proposed Civil Code section 7108). We support those changes, because they more accurately reflect the variety of mailing options available in business today. The increased flexibility regarding proof of mailing is particularly helpful to businesses like ours that mail thousands of preliminary notices each year.

We note a minor language difference in the listing of acceptable mailing methods in proposed Civil Code section 7108 and Public Contract Code section 42080 with respect to the listing of "Express Mail." We think the two statutes should use the same language.

8. The Proposed Revision Need Not Address the Disparity among Remedies Regarding Attorney's Fee Recovery.

The Commission has specifically requested comments on the disparity among remedies regarding attorney's fee recovery. Attorney's fees are provided for public works payment bond claims and certain stop notice claims, but not for

mechanics liens. We think this disparity is justified by the difference in commercial sophistication of the parties typically on the receiving end of the different remedies. Payment bond claims impact direct contractors and sureties, which are in the construction business and can take steps to manage the effect of the claims and the risk of attorney's fees. Bonded stop payment notices affect commercial lenders and sureties, which also have the capacity to manage the risk of payment litigation. In many cases, however, mechanics lien claims are asserted against homeowners with no experience in the construction process. It would be unfair to add to the double payment risk homeowners already face by making them responsible for a prevailing claimant's attorney's fees. We suggest that no changes be made to the attorney's fee provisions.

9. The Period of Cessation for Defining Completion of Public Works Projects Should be 60 Days.

The Commission has specifically requested comments on the proposed 30-day period of labor cessation for purposes of determining completion of a public work under Public Contract code section 42210. In our experience, the 30-day period is too short. The process of "closing out" a public works contract after site labor is complete is often a lengthy one, and agencies will not release payment to the contractor until this is completed. Starting the claims clock running before the public agency and direct contractor have agreed on final payment quantities and completed the closeout paperwork will only result in premature claims and complicate the closeout process. We think a 60-day cessation period more accurately reflects amount of time that passes between cessation of labor and expectation of final payment.

10. Proposed Civil Code Section 7432 is Ambiguous.

Proposed Civil Code Section 7432 is noted to be a restatement of existing Civil Code section 3124, which limits a mechanics lien to items included in the original contract. In our view, however, the language of the restatement has created an ambiguity. Section 7432 provides that a lien does not extend to items not in the direct contract if the item "was authorized by the direct contractor or subcontractor and the claimant had ...knowledge ... of the contract..." Does this mean that if the item ***was not authorized*** by the by the direct contractor or subcontractor the claimant may include it in a lien?

11. The Identity of the "Maker" of a Payment Should Not be Required on the Conditional Waiver and Release Forms.

The Conditional Waiver and Release Forms included in the proposed law (Civil Code section 7170 and Public Contract Code section 42360) have a blank to be completed for the "maker" of the anticipated payment. We do not believe this adds anything to the release, and it creates a problem for lower-tier subcontractors and suppliers who do not always know who will be making the payment. It is common for lower-tier subcontractors and suppliers to receive joint or single payee checks from people other than their customers, and even on a single job the payee of a check may change depending on arrangements made by parties higher in the contracting chain. Rather than have a blank on the form that frequently cannot be completed or that could be completed inaccurately, we request the blank be eliminated.

12. Proposed Civil Code Section 7208(b) Should Include Contracts with More Than One *Contractor* or Subcontractor.

Proposed Civil Code section 7208, establishing the coverage of preliminary notices, provides that separate preliminary notices are required for claimants who have contracts with more than one subcontractor. On multiple prime projects, claimants may have contracts with more than one direct contractor. The section should be amended to include contracts with more than one "direct contractor" to cover the multiple prime contract situation.

13. Proposed Civil Code Section 7210 Should be Modified to Enhance the Direct Contractor's Obligation to Timely Provide Preliminary Notice Information.

One of the biggest challenges lower-tier subcontractors and suppliers face in protecting lien rights is obtaining the information required to complete the preliminary notice form in a timely fashion. While there are in theory many sources of that information, from construction deeds of trust to building permits, as a practical matter it is exceedingly difficult to find the information within the 20 day window allowed to serve the notice. The best and most reliable source of the information is the direct contractor. Many reputable direct contractors routinely make the information available, but many contractors do not. Proposed Civil Code section 7210 imposes a legal obligation on direct contractors to provide the information, but the section does not require that it be provided in a timely manner,

and does not impose a sanction for failure to comply. The statute has no teeth. We recognize the proposed section follows existing law and the Commission has decided not to effect major substantive changes. However, this is an area where a stronger statute would further the purpose of the lien law by providing claimants the information they need to protect their statutory rights.

14. Proposed Civil Code Section 7418(d) Should Make Clear That the "Person That Contracted" is the Claimant's Customer, as Opposed to the Owner, Direct Contractor, or Someone Else.

Proposed Civil Code Section 7418(d) requires a lien claim to identify "the name of the person that contracted for the labor, service, equipment, or material." We believe the intent of that subsection is to require the identity of the claimant's customer. However, the "person that contracted" could be construed to be the direct contractor or some other person in the contracting chain that may or may not be the claimant's customer. The statute could be clarified by requiring the identity of the person who "contracted *with the claimant* for the labor, service..."

Thank you again for providing the opportunity to comment on the proposed lien law revision. We hope our comments are useful. If you would like further information regarding these comments, please do not hesitate to contact us.

Very truly yours,

GRANITE ROCK COMPANY

Thomas H. Squeri
Vice President and General Counsel
Direct Dial - (831) 768-2003

THS:slp

COMMENTS OF LORI NORD

From: Lori Nord <lnord@mjmlaw.us>
Date: September 12, 2006
To: bhebert@clrc.ca.gov
Subject: mechanics' lien law revision

Message: "EXPRESS TRUST FUND" in Section 42030 (a) (2) of the Public Contracts Code on page 144 of your report should be changed to "LABORERS COMPENSATION FUND" to be consistent with your other changes. Otherwise there will be a question as to whether the stop notice claim is limited to express trust funds because you've used laborers compensation fund throughout to be more inclusive than just express trust funds. I represent these funds in such collections so this is an important point to us.

Thanks

SAM K. ABDULAZIZ
A Law Corporation

KENNETH S. GROSSBART
A Law Corporation

BRUCE D. RUDMAN
A Law Corporation

CATHERINE R. FINAMORE

LAW OFFICES OF
ABDULAZIZ, GROSSBART & RUDMAN
A Partnership of Professional Corporations

Mailing Address: P.O. Box 15458 / North Hollywood, CA 91615-5458 / (818) 760-2000 / Fax: (818) 760-3908

September 20, 2006

SENT VIA EMAIL & FIRST CLASS MAIL
sterling@clrc.ca.gov

Nathaniel Sterling
CALIFORNIA LAW REVISION COMMISSION
4000 Middlefield Rd. Room D-1
Palo Alto, CA 94303-4739

RE: Tentative Recommendation - Mechanic's Lien Law H-821

Dear Mr. Sterling:

Thank you for giving us the opportunity to comment upon the tentative recommendation of the California Law Revision Commission regarding California's Mechanic's Lien laws. For the most part, we agree with your suggestions. Indeed, as I had stated to you personally, you have grasped this complicated area of law very quickly.

However, the project that you have undertaken is mammoth in scope. It changes locations of present law. And, although the intent was to make the law more consistent and easier to maneuver without substantive changes, we expect people to come out of the woodwork to ask for substantive changes. As always, our intent is not to allow any intrusion into a constitutionally protected right.

There are some minor changes that you are making that might have an adverse effect on the industry. There are also a few changes that you are making that trouble us, in that they invalidate a lien or stop notice claim based upon the failure of the *lawyer* for the claimant to do something rather than any statutory time bar – as an example, if a timely Mechanic's Lien suit is filed on the last possible day (90 days after the recordation of the lien), there would be only ten *calendar* days left to record a *Lis Pendens*. The county recorders are notorious for "bouncing" documents, including those that are proper, which could make it difficult to timely record a *Lis Pendens*. This is particularly true if the lawsuit itself takes a few days to be returned to the attorney following its filing. Then, if the lawyer delays recording the document for even a short period of time, the lien right may be lost. The same problem may occur with regard to the Notice of Commencement of Stop Notice Action. In that instance, you would only provide a five-day period (the present section allows ten days). With weekends and any lags in getting back the filed papers from the court, that deadline will almost ***never*** be met. Even the current ten-day period is often difficult.

These are merely examples. We will go through other concerns we have, but a modest delay by the attorney for a lien claimant who has otherwise properly perfected a lien or stop notice claim, should not invalidate the constitutional right of a lien or stop notice claim.

As an additional prefatory comment that applies throughout the new proposed scheme, we would suggest that wherever you make a reference to a section within a different Code (i.e., the *Public Contract Code*), we would ask that you identify the Code. There are numerous cross-references to sections that are not in the *Business and Professions Code* that could cause some confusion, particularly to those who do not emphasize this area of the law.

As to the substance of the tentative recommendation, our comments are as follows:

Background and Introductory Comments of the Commission:

In your Background section, on page 2, we are not sure that we would characterize all contractors as extending credit readily. The Mechanic's Lien right goes back for more than a hundred years and I would not agree that credit is extended "readily." On that same page, I would add in the last paragraph, above "Construction Contracts," that, "*if the claimant acts appropriately, the improved property stands as security.*" It clearly is not a slam-dunk.

On page 19, the Commission discusses the replacement of the term "original contractor" with "direct contractor." The industry commonly uses "prime contractor" in most instances to refer to those in privity.

As a final comment to the introductory comments, on page 51, you discuss the Summary Release Procedure following the affidavit process to release a stop notice. We are not sure that it is clear that the Summary Release Procedure would only allow for a decision by the court to determine how much should be withheld, if any. It should not include how much is owed.

Proposed Litigation:

The definition of the proposed Section 7003, defining commencement, could be interpreted as what can be claimed in a Mechanic's Lien. The proposal says that commencement starts when "material or supplies that are used, consumed, or incorporated in the work of improvement are delivered to the site." The amount claimed in a lien is limited to value provided to the property, and mere delivery does not allow for inclusion in the lien. On the other hand, the fact of delivery certainly means that commencement of the work of improvement has occurred. Does this need to be addressed to avoid confusion as to Section 7430?

It is possible that the definition of "Contract" in Section 7006 will cause confusion, particularly without a definition of subcontract (other than the reference to a subcontract in Section 7130), in that the word "contract" is used in many places including court decisions.

If the intention of Section 7016 is to be all inclusive, then we believe you should add such items as temporary services (fencing, power, scaffolding), equipment rentals, and other items that routinely are the subject of lien claims but which on their face might not appear to add value to a work of improvement.

As to Section 7102 – Contents of notice – subdivision (a)(6)(iii) requires an estimate of the demand, which may not be applicable on certain notices, such as a Notice of Completion, which is many times recorded by the "claimant."

As to Section 7106 - Address at which notice is given – we would like to see a minor change to subdivision (a)(5), which refers to notice to the surety. The subcontractor may not have a copy of the bond and may only have the information provided by the owner (beneficiary of the bond), and sometimes they provide the broker's information rather than the surety itself; thus address to the surety at the address provided by the owner or direct contractor (the reputed address) should be acceptable.

We agree that Section 7108 – Mailed notice – should allow for other forms of delivery such as express delivery services, etc.

We believe the agreement to accept electronic communications under Section 7110 should be in writing.

As to the comment to Section 7132, the designation of construction lender on building permits serves a practical purpose in that it is a matter of public record and has been referred to in case law, and is another place where the subcontractor can search for information on who they should provide Preliminary 20-Day Notice. We believe subdivision (c) should be omitted as if there is a lender at the time the permit is obtained, it should be listed.

As to Section 7150 – Completion – we believe that "acceptance by the owner" should be included in the items constituting completion. Oftentimes, the contractor will have a written document that is signed by the owner whereby they accept the work, and this should also be indicative of "completion."

As to Section 7152 - Notice of completion – we agree with the expansion to 15 days, but suggest the following:

In subdivision (a), the notice should be signed and verified by the owner, ***or the owner's authorized agent***;

In subdivision (b)(1), if the completed contract is only for a particular portion of the work of improvement, the party giving notice must state what portion is complete, and it may be a good idea to state what the person believes is not complete;

In subdivision (b)(4), we disagree with the change in the law that, "an erroneous statement of the date of completion does not affect the effectiveness of the notice if the true date of completion is on or before the date of recordation of the notice" if the Notice itself is not recorded within 15 days of the true date that "completion" occurred. As stated in your comment, the law is that a Notice of Completion is not valid if not timely recorded. The wording could lead to arguments over whether it is an erroneous date or a late notice.

Lastly, as to subdivision (b)(6), this should reflect, "to the extent notice is required." Section 7156 excludes certain persons (particularly residential owners) from the requirement to give notice.

We are concerned with Section 7154. If there are separate contracts, how is the time for completion measured in the context of a Mechanic's Lien? We believe it should be the completion of the last contract performed on the work of improvement. If there is a direct plumbing contract and a direct landscaping contract, there could be arguments that a Notice of Completion on the plumbing contract affects the landscaper's lien rights.

Also, we would like the exceptions on your page 91 to read:

"Exceptions
This document does not affect any of the following:
(1) Retentions.
(2) Extras for which the claimant has not received payment.
(3) The following ***requests for*** progress payments for which the claimant has previously given a conditional waiver and release but has not received payment:
Date*(s)* of waiver and release: _____"

As to Section 7202 – Preliminary notice requirement – to clear up any discrepancy, the Section should state, "Except as exempted under this Chapter…" As you reference, in addition to Section 7200, **there is an exception where a Notice to Surety is given.**

In Section 7216, we agree with the deletion of the reference to disciplinary action for the failure to give a Preliminary 20-Day Notice for work over $400, as we have never seen this occur. The proposed Section 7216 provides for discipline for the only practical harm to the owner that could be caused by the failure to provide the notice – the subcontractor also relinquishes its right to

record a lien, but that is not a detriment to the owner. We would like to see a subsection that requires a person who serves a Preliminary 20-Day Notice to provide an unconditional release upon final payment when they are paid for all services or material on the project, as the refusal to provide such a release by a subcontractor or material supplier is an ongoing problem in the industry.

We disagree with the omission of former section 3097(o), and the new section 7218. We believe that preliminary notices should be able to be filed with the Recorder as it currently is allowed. The Recorder can charge for that service under the present state of the law.

As to Section 7412 – Time for claim of lien by direct contractor, a claimant should also be able to record a claim of lien when work by the claimant stops. For example, what happens if they are terminated or otherwise do not complete contract?

We strongly disagree with the additional Notice in Section 7420 – Notice of intended recording of claim of lien. That is just adding another requirement which I believe is unnecessary and puts an additional burden on the one trying to enforce a constitutional right. It also shortens the time to record a lien. Moreover, practitioners will be arguing as to the enforceability of a lien if *sufficient notice* is not afforded the owner. Section 7422 should likewise be omitted.

We are concerned with the measure of proof in examining the allegation of a false claim in Section 7424. This is discussed further when dealing with the summary procedure.

Section 7430(b)(2) references the contract price (defined in Section 7008), but we would like to see an explicit reference to increases by changes in the work. **This is particularly needed because of the reference to Section 7602 that ignores change orders.**

As to Section 7456 – Priority of advances by lender – we disagree with the inclusion of subdivision (b), particularly to the extent that any advances by the lender are for interest and non-construction related-costs and loan fees. The lenders are notorious for depleting the fund for the lender's benefit by imposing such charges, particularly after default by the owner.

As to Section 7460, as indicated in our initial comments, we are concerned with the requirement that a *Lis Pendens* also be recorded within 100 days of recording the lien; in cases where the suit is filed on the 90th day, getting the conformed copy from the court, preparing and recording the *Lis Pendens* within the next ten calendar days may be impossible. A Constitutional right should not be waived by the failure to perform this ministerial act within a short window if the lien was properly perfected by the foreclosure suit. The Commission is reminded that there is presently no requirement for a *Lis Pendens* to be recorded. Thus, we suggest that phrase "100 days after

recordation of the claim of lien" be replaced with either, "20 days from commencement of the foreclosure action" or "110 days after recordation of the claim of lien."

Separately, we agree that the Notice of Extension of Credit must be signed by both claimant and owner, and that the Notice can be recorded after the 90 day period to file suit to foreclose on the lien so long as it is recorded before another person acquires rights in the property.

As to Section 7476 –Liability of contractor for lien enforcement – we would add to the end of the initial sentence the words, "and paid for by owner." The contractor should not indemnify for claims where the owner did not pay for the work. Subdivision (a) should also provide that the contractor may instead provide a Mechanic's Lien release bond issued by an admitted surety.

Section 7480 – Petition for release order – troubles us because it lumps in too many other situations than existing Section 3154. Subdivisions (a)(2), (3) and (4) require factual determinations that are too broad for a summary proceeding, and for which a jury is likely required as referenced above. As to subdivision (a)(6), the res judicata effect should not include small claims court determinations. We are concerned about a small claims judgment being considered sufficient to order the release of a lien. We do not believe that the Legislature or the constitution intended to allow such broad powers to the small claims courts.

As to Section 7504 – False stop payment notice – although this restates existing law, the reality is that will be difficult to prove. There is a difference between overstated and willfully false, and one's disputed change order claims should not invalidate a stop notice claim.

As to Section 7520(b) within what timeframe does the person have to serve the stop notice?

As to Section 7536 – Duty of construction lender – the Commission asked for comments, and as to subdivision (b)(2), it is confusing. The second sentence of subdivision (b)(2) should simply state: "However, regardless of the recording of a payment bond, the construction lender shall withhold sufficient funds to pay the claim of a direct contractor who serves the construction lender with a bonded stop notice."

In our prefatory comments we touched on concerns with Section 7550 – Time for enforcement of claim stated in stop payment notice. Subdivision (a) continues existing law and is fine. Subdivision (b) adds a private works requirement to serve a Notice of Commencement of Stop Notice Action; consistent with your modification for public works, you wish to reduce the time for service of this newly added burden from 10 days to five days to file a Notice of Commencement. One must question whether the reasons for providing such a notice on private works merit this burden. We cannot see any benefit. We do see a detriment.

The Commission solicited comments as to Section 7552. Projects straddling a county line are not as common as suits filed in the wrong county that must be moved. More common are situations where cases are filed in limited jurisdiction (requiring the filing in the "local" court) and other claims of a more significant amount are filed in the main or central courthouses. If the first court acquiring jurisdiction is a limited court, then it may not be able to be the "lead case."

Section 7726 – Escrow account – The requirement that the bank must be located in this State has a practical meaning for purposes of an action in rem.

As to Section 7834 pertaining to the additional notice prior to the Stop Work Notice, I would add the words, "in a prominent place" after the word "notice," in subdivision (a). Frankly, we also believe the time periods are way too long. Under this scheme, the owner has to be 35 days past due before the Notice can be used, and then it gets more time. The contractor suffers additional damages by waiting this period of time, and practice in the industry is to have a contract provision allowing for work to stop if payments are past due.

As to Section 7838, which deals with the immunity from liability following the Stop Work Notice, we believe that subdivision (b) should also insulate the subcontractor for liability to its sub-subcontractors and material suppliers for cancellation following the direct contractor's service of the Notice.

As to section 7840, we would suggest that a subcontractor who receives such a notice must give notice to sub-subcontractors and material suppliers below it on the project.

Public Works Contract Remedies:

Generally, we would leave this area alone in that the ones who work in this area are relatively sophisticated and have counsel. As mentioned above, where there are references to other codes, the references should be explicit. As examples, there are numerous references to sections within the Public Contract Code, which are confusing. See e.g., sections 41090, 41120, 41130, 42010, among others.

As to Section 41070, we reiterate our comment to Section 7016.

As to Section 42210 – Completion – we believe that the thirty-day period as previously included in Section 3086 is fine.

As to Section 42220 – Notice of Completion – this should not trump the definition of completion in Section 42210. That is, a later recorded Notice of Completion should not extend completion (or provide a renewed date for claimants to serve stop notices or bond claims). The Commission

may also want to define a Notice of Acceptance recorded by a public entity to be a Notice of Completion.

As to the Waiver and Release forms for public works, our same comments as to private works apply, and the exception should refer to prior requests for progress payments (that have not been paid).

As to section 44180, the public entity should not have discretion to reject or disregard a release bond from an admitted surety.

As to Section 44430, we reiterate that a five-day period to serve a Notice of Commencement of Action is too short.

Conclusion:

Overall, you have organized the law in one central place. The changes will take persons who were readily familiar with the sections codified at 3082 et seq. some time to maneuver. Likewise, we are certain other inconsistencies will be discovered in practical use of the statutes. Our primary concern is always anything that would limit or diminish the Constitutional lien right. The failure to provide a secondary Notice of Commencement, or a short period of time for a *Lis Pendens*, in our opinion, should not void an otherwise valid claim; similarly, a summary proceeding is not appropriate to discharge a lien or other lien right (e.g., stop notice), if the evidence to be considered goes beyond such incontrovertible items such as dates and lack of licensure.

Thank you again for considering our clients' positions.

ABDULAZIZ, GROSSBART & RUDMAN

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My file No. 3066

September 18, 2006

Mechanics Lien Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Dear Members of Commission:

This is a response to the Commission's request for comments from the public regarding the Tentative Recommendations of June 2006 regarding the California Mechanics Lien Laws Revisions ("Revisions."). I have divided this letter into three parts: (1) my background and experience, (2) general comments regarding the Revisions, and (3) comments regarding specific Revisions.

(1) Background and Experience

I bring the following to the Commission's attention so that the members will have an understanding of my knowledge and experience of the subject. I was a member from 1967 to 1969 of the Advisory Commission to the Senate Judiciary Committee for the revisions of the mechanics lien laws that became effective in 1971. I also participated in the writing of the first C.E.B. Book on the Mechanics Liens. I have written numerous articles and spoken to numerous organizations, including C.E.B. lectures, relating to the construction industry. I have been specializing in construction industry matters since I started practicing law in 1949. I have tried many cases with respect to construction and related issues and argued a number of times in the appellate courts on issues relating to some aspect of the construction industry.

(2) Preliminary and general comments

I commend the Commission for a fine accomplishment in the rewriting of the mechanics lien laws. I do have some comments and thoughts on various matters and will address them.

I will first address the topic that is raised by the Commission and was the subject of considerable discussion and controversy in the 1967 - 1969 meetings and hearings, that is, whether the mechanics law should be rewritten completely so as to be simplified. I was in the group that favored such an approach. This is the group referred to by the Commission as the "stakeholders." In the very early discussions with Professor Harold Marsh, who wrote the definitions, he remarked to me that he had never before encountered such a confusing and convoluted statute as existed in the California mechanics lien laws.[1] I recall a discussion with him in which he

[1] Mr. Marsh subsequently became the editor of and rewrote sections of the Uniform Commercial Code and the Corporation Code.

addressed the question of why there were so many different dates for what, in the main, involved the same issue. For example, he asked me why a general contractor was allowed 60 days to record a lien after a notice of completion and all others only 30 days? Why, he asked, were they not the same? Why did public and private projects have so many different rules?

During these hearings the California legislative counsel was able to obtain copies of the mechanics lien laws from other states and most of them were and still are much simpler than California's laws. I lost the argument based upon the same observations made by the Commission in its comments on page 12. As the Commission noted in the introductory comments, some of the present language and, I submit, procedures and time requirements, date back to 1872. In the early 1970s I and others were consulted by attorneys from several other states engaged in rewriting or adopting lien laws for their respective states. Most of the attorneys expressed dismay at the confusing and complexity of the California laws.

On page 13 of the Commission report it discusses the comments of James Acret that are appropriate. I believe Mr. Acret was a member of the Senate Advisory Committee referred to above, but regardless, his comments are well and succinctly stated and should be accepted. There is no logical reason why the lien laws need be so complicated.

I realize that the Commission considered the possibility of revisions or simplifying the statutes but its rejection is based upon the same arguments made before: let us not lose the advantage of the many years of decisions under the old and existing laws. If this concept were adopted for all statutes, it would have required California to maintain the Uniform Sales Act and not adopt the Uniform Commercial Code. Such logic would have prevented the adoption of the Corporation Code, the changes in laws on divorce and any uniform statutes adopted by California. At the hearings many years ago it appeared to some members of the committee that reliance on the earlier cases to interpret the law was and is misplaced.[2] The courts have too frequently ignored the earlier laws and the laws have been changed and interpreted by the courts in a manner inconsistent with the intentions of the legislature. The existing mechanics lien law and, as proposed by the Commission, is difficult to understand and interpret. To make them comprehensible the laws should be rewritten rather than rewriting them to maintain the existing complications.

Although the Commission has asserted that it was not rewriting the current law, but only changing language in an effort to rationalize much of what had been irrational. I have noted, however, in several instances there have been changes that are substantial. Some of the changes are significant. Moreover, some of the changes, as presently stated, are confusing. In a few

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[2] The contemplated renumbering will create new problems. In researching and writing briefs or in decisions, reference is frequently made to earlier cases in which an existing statute is noted with a comment such as "previously section XYX." With renumbering and the actual use of the older decisions, they would now be required to note "previously section ABC that was previously XYZ."

instances they are unworkable and perhaps themselves not consistent with other provisions and existing law. I have discussed these below. Further, in some instances the Commission has made significant changes and has misstated some provisions of law.

I appreciate the Commission's accomplishments and the logic in incorporating into one code a set of definitions for public works of improvements starting on page 68 and a separate set of definitions for public works starting on page 140 to be placed in a separate codes. Although there may be some logic to such division, it leads to much confusion. The separation is not nnecessary. There is very little need to divide the definitions into two different codes.[3] If it is appropriate to divide the private from the public works, it may still be accomplished by the incorporation of the definitions and referencing the other code. If separated it still would be better to simply the procedures and definitions in each of the two codes. Although located in different codes, there is little gained. There are very few instances where a code provision is applicable only to private or only to public works.

Generally the two sets of definitions are identical. I have made no attempt to identify all such repetitions. The Commission considered that it was simplifying the statutes beginning with the section on definitions on page 68, by defining in one section all references to the various terms used throughout the code. However, the provisions in the definition sections under private works, are for the most part exactly the same, word for word, as the sections relating to public works commencing with Section 41020.[4] As noted, although in different codes, they are still repetitious.

One reason for not using the same definition in two different codes is that undoubtedly at some reasonably early time, there will be amendments made to the definitions in the different sections leading to more confusion and ambiguities.

Most builders and home owners constantly are required to employ the services of an attorney for every project, large or small, to explain and interpret the lien laws. I am sure that members of the Commission have had the same experience. While I would hope that the commission would re-explore the complete revision of the lien laws to simplify them so that the average contractor, builder, or home owner — and in some instances, the court s and attorneys — could understand them, I realize that the Commission has considered the issues and that, regretta-

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[3] There are too many different articles and sections containing the word "notice." See sections 7034, 7042, 7100 - 7116, 7152-6, 7166, 7200 - 7218, 7420 - 7422, 7444, 7500 -08, 7520, 7550 -2, 7544, 7612, 7830-6, 41110, 42060-80, 42220-30, 43010-60, 44110-70,44430, 45060-70 or about 256 times. The amount of duplication in use and definitions seems overwhelming.

[4] As a matter of convenience, I will refer to the Commissions proposed sections by the use of the term "Section."

bly, it probably will not change its views with regard to this argument. The comments beginning on page 13 would indicate and cause one to believe that within the next thirty years, the laws will again need to be revised.

(3) Comments re proposed statutes

The changes recommended do, in most instances, simplify many of the statutes and make them more understandable. Certainly the restatement of the various sections on notices, as an example, is most helpful. There are, however, some ambiguities and areas that may need attention and should be addressed. In some instances the Commission has requested comments upon certain subjects. My comments are set forth, for the most part, in the following discussion of the specific sections for which comments are requested. I hope these will be helpful. In several instances I submit that there are errors that should be corrected. See, for example, my comments below with respect to Sections 7030 and 7600.

Generally I found it confusing to read Section 7204 entitled "Contents of Preliminary Notice" and observe only the one requirement in 7204(a). Although 7204(c) refers to an invoice containing certain information required by Section 7102 there is nothing to indicate that 7102 contains the requirements for a valid notice. The reader would have to know that there is another code section setting forth the requirements that is applicable to every kind of required notice . This could be confusing and misleading. I assume that in time those required to serve a preliminary notice may get used to the fact that the section relating to what is required is located in Section 7102 I recommend that Section 7204 should make some direct reference to Section 7102 for the requirements.

Direct Contractor Section 7012

The Commission has noted that presently there are many terms used to describe a contractor on a project. Almost every person engaged in the construction industry considers that the person who enters into the contract to build or erect the a project or the work of improvement is the "prime contractor" and is the person responsible for obtaining and employing all subcontractors.[5] The term "Prime Contractor" is more appropriate than "Direct Contractor." Most construction contractors use the term "contractor"and changing the nomenclature to describe this entity will lead to confusion. I doubt that contractors will change their contracts to describe themselves as "Direct Contractor" instead of just "Contractor."

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[5] In the construction industry sometime the term "prime contractor" is used in major construction projects involving many trades where one GBC assumed the responsibility for the entire project. Absent such usage, the industry invariably uses the term "contractor" as the one in charge of the building of the project and generally as having a direct contractual relationship with the owner. I prefer the term prime contractor to "original contractor" as suggested by you. My use of prime contractor is in lieu of and not different from the original contractor.

I am, moreover, also concerned over the use of the terminology that a direct contractor is a person "that has a direct construction relationship with an owner." Previously in Section 7006 a "contract "was defined as "an agreement between an owner and a direct contractor." Section 7012 defines a Direct Contractor as one that has a direct contractual relationship with an owner. Since the words "construction relationship" is very broad and unrestricted, I visualize some court concluding that a "direct construction relationship" would include an "*implied* direct contractual relationship" as well and thus conclude that such person (e.g., an employee, or sub-subcontractor, or materialman's materialman) would be entitled to assert a claim against the owner based upon quantum meruit? See also my discussion below of Sections 7026 and 7400. The insertion in the definition of the words I have italicized below would resolve any problem with the present wording:

> "Direct contractor" means a person that *has entered directly into a written or oral* contractual relationship with an owner ."

This should eliminate any doubts as who is meant and negate any implied contractual relationship.

Laborer Section 7018

Should not the definition of a "laborer" be restated so as to exclude an "employee" such as office personnel? Is not every person bestowing a service in connection with a work of improvement, regardless of their physical location, performing a service "on" such work? I am considering the sales person or secretary in the office of a Direct Contractor or Subcontractor or even a material supplier, whether physically on the job site or not. Such individuals may rightfully claim to have performed service "on" a work of improvement. Since in section 7016 you have included "construction management," do the employees of the construction manager have a right as a claimant? Does the word "on" in the definition suffice? Could a court consider "for" and "on" as the same action? I have encountered claims by draftsman in the offices of a subcontractor who have asserted such claims. Could this potential problem be resolved by a slight change in language so that the last phrase would read "*directly for and upon* the work of improvement?" Or perhaps the definition should describe such person as being one "physically engaged directly upon the work of improvement"? An alternative would define a "laborer" negatively by eliminating those not engaged in physical labor upon a work of improvement in furnishing LSEM. [6]

Material Supplier Section 7026
Persons entitled to a lien Section 7400

On page 6 beginning at line 27, the Commission acknowledges that a material supplier's supplier, is not entitled to assert a claim. Section 7400 (d) provides that a "material supplier" is

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[6] Labor, services, equipment, and materials.

entitled to a lien. The definition of material supplier in Section 7026 does not eliminate such a claim and would expressly include such a person as one entitled to a claim. Language is required to eliminate the material supplier's material supplier. Possibly it was intended that Section 7406 (defining who may authorize work) solved this problem, but I do not believe that it does. The proposed section should expressly include language such as "*and does not include a person supplying materials to a material supplier supplying materials to be used or consumed in the work of improvement.*"

Further, under Section 7400(g) who or what is a "builder"? Is not the inclusion of the term superfluous? Bus. & Prof. Code § 7026 presently defines a "contractor " as synonymous with "builder." To include as those entitled to assert a lien a "builder" and not defining or explaining what is meant, leaves a gap. Since the Commission already has included direct contractors and subcontractor, material and equipment suppliers, laborers, and a design professional, by the inclusion of the term "builder" it would indicate something different. If so, what? Any "builder" would have had to be included already as a direct contractor of subcontractor.

Payment bond Section 7030
Payment Bond Section 7600

Section 7030 states that a Payment Bond is a bond given pursuant to Section 7600. Section 7600 provides, in part, that the bond will insure against the contractor's "*failure to perform.*" This is *not* a Payment Bond: it is a Performance Bond. It is a misnomer to call it a Payment Bond. The coverages between a Payment Bond and a Performance Bond are different. A contractor or owner ordering a "Payment Bond" will receive what is frequently referred to as a Labor and Material Bond" and will not protect against a claim asserted under the first clause, that is, the "failure to perform" by the contractor. A Payment Bond will accomplish only one purpose described by Section 7600 (payment of LSEM) but it will not protect or insure the "contractor's failure to perform." That protection can be obtained only through a Performance Bond. [7] Although it has been argued under a broad interpretation of "performance" that it would include the contractor's obligation to pay the suppliers, it would seem better to require a properly identified bond.

Stop payment notice Section 7042

Since the Commission has changed the nomenclature of Stop Notice to a "Stop Work Notice," could there be confusion? I prefer the term "Notice to Withhold." Admittedly, this is just a preference that I believe it to be descriptive of what occurs upon its service. Leaving it as "stop notice" will not, however, confuse anyone. In the Commission report there are on various

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[7] The Miller Act (40 USC § 270a) requires both a performance and a payment bond to insure both performance and payment. See Conners California Surety & Fidelity Bond Practice (C.E.B. 1969) pp. 61 and 81.

occasions, references to the Stop Payment Notice as a "Stop Notice." It was a good step to eliminate that portion of Civil Code § 3103(c) of the statement of the whole amount agreed to be furnished. It had added nothing.

On page 42, the Commission requests comments regarding the omission of the amount claimed in both the mechanics lien and the Stop Payment Notice and the mandatory five-day notice. The five-day notice should be maintained as mandatory so that the lender and borrower are in a position to control the situation. If the notice is not served, they may fail take actions that would control or prevent the rising of a default situation including that caused the serving of the notice in the first place, that is, the direct contractor's default in payment.

On page 42 the Commission comments that a stop payment notice reduces the claim of lien. I do not believe this to be a correct statement of existing law. If a claimant records a mechanics lien and also serves a Stop (Payment) Notice that results in the withholding of the money by the lender, it does not reduce the amount of the claim. Only if payment is made to the claimant, will the claim on the lien be reduced.

I recognize that Civil Code § 3161 has a clause placing upon the owner the duty to withhold from the contractor any monies "due or to become due to such contractor to answer such claim and any claim of lien that may be recorded therefor" but this does not reduce or diminish the claim. The intent is clear: it is the payment of the money held under the stop notice that reduces the claim, not the mere service of it. The Commission has properly omitted this language and has correctly stated the law in the note to Section 7522. It was intended, as the Commission properly later concluded, that it is the payment to the claimant of money pursuant to a Stop Payment Notice reduces the amount of the claim.

Work of improvement Section 7046

Section 7046(a)(1) is very broad and inclusive in stating in "whole or in part."[8] Does not 7046(b) referring to "scheme of improvement" that is not defined elsewhere, now confuse the matter? Is this subparagraph meaningful? Further, "work of improvement" states the "entire structure" but subparagraph 7046(a)(1) states "whole or in part." It is inconsistent to state "entire" and then state "in part." This subparagraph is confusing and probably unnecessary.

Jurisdiction and venue Section 7052

This section refers to jurisdiction "of this part," what is meant by this? The jurisdiction of an action to enforce a stop notice has never been clear. Is the jurisdiction of the action where the project is located or the location of the offices where the stop notice was served? For example if

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[8] On various occasions the Commission uses the words "this part." This is ambiguous as to whether it means the "section" or the Article. This should be clarified.

the office of the lender is located in a different location from the project site, where is the jurisdiction? What is the "proper court" where the action on st op notice is to be brought?

I am not aware of any decision that directly determined where jurisdiction of an action on a stop notice or on a payment bond should be. It should be where the project is located, but if a stop notice is served upon a lender that is not located in the county or district where the project is located, would not the jurisdiction be in the district where the lender has its offices? If the claimant seeks both a mechanics lien and enforcement of a stop notice, where is the jurisdiction? To further complicate the situation, where would jurisdiction be if the claimant has also asserted a claim on a payment bond?

It would be helpful to specifically identify the jurisdiction in the event that a claimant seeks recovery on a stop payment notice, a bond, and a mechanics lien.

Filing and recording of papers Section 7056

A claim of lien is required to be "signed and verified" but not acknowledged. County recorders accept such claims of liens. However, the same county recorders insist upon an acknowledgment for a releases of a claim of lien There should be consistency. It seems logical that if the claim of lien is not required to be acknowledged, the same should be true of the release of such document. Could Section 7056(b) state in the opening sentence to add the words "release of lien" to the various named instruments?

Effect of act by owner Section 7057
Release of surety from liability Section 7142

It is not clear what act of an owner, whether in good faith or not, could release the surety. I am not aware of any litigation resulting from the current law, but when read together with Section 7142, it is even less clear. Is Section 7142 intended to state the only sections that do not release the surety? If it is intended, then Section 7057 is unnecessary. Also note the use of the term "performance bond" in Section 7056.

Although these sections are restatements of existing law as contained in Civil Code §3225, nevertheless, the provisions of these sections conflict with general suretyship law. The proposed sections release sureties from changes in the contract terms including the terms of payment. Civil Code §2819 provides, in part, that a surety is exonerated by any act of the creditor without the surety's consent. This would include changes in payment terms. Moreover, surety bonds generally contain a specific provision to this effect. Sureties will certainly raise objections to this change. Such conflicts should not be carried into the proposed revisions.

Section 7142(b) should not be applicable to a change in the terms of payment, except when additional security is offered or given or at least the surety notified so that it may make a

decision of whether to request additional security or to waive it.

Contents of Notice Section 7102

This section is simply too long and complicated. Although the comment states it to be new, it is a reasonable revision of existing law. I do not know if it is confusing to use the sane terminology in this section and in Section 7104 but I assume that once persons become acquainted with the form, it may not create any problems.

Service Section 7104
Service Section 7108

The revisions to Section 7104 provide that service shall be by "Personal delivery" or as provided for by Section 7108. As originally written by the committee in 1969, service of the preliminary notice was required on private works of improvement under Civil Code §3097(f) to be made by "first class, registered or certified mail." In public works section service of the preliminary notice was to be the same, by "first class mail, registered mail or certified mail . . ." When enacted, however, there was a typographical error committed by the printer regarding the service on private works by omitting the comma following the words "first class" so that it read "first class registered or certified mail."[9] The post office has informed me that any mail sent registered or certified is first class. It is incorrect to use the terms "first class registered or certified mail."

Section 7108 carries forth this error in providing for service to be by "first class registered or certified mail." I submit that the words "first class" should be omitted from Section 7108 since there is no such a thing. A simple "by first class mail" and "registered or certified mail" will suffice if that is what is intended.

The Commission probably has but if not, should review the cases of *IGA Aluminum Products v. Manufacturers Bank* (1982)130 Cal. App.3d 699 (where the preliminary notice was served was served on a bank by first class mail but not by registered or certified mail and it was held by the court not to be a valid service.

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[9] Ironically Civil Code § 3097 presently contains a conflict regarding the method of service. In the introduction to the Notice to Property Owner section, in the first paragraph describing the method of service, it is stated that the owner is entitled to a preliminary notice and that the preliminary notice shall be by *registered mail, certified mail, or first-class mail,* evidenced by a certificate of mailing." The commas are used in the definition. The terms of the statute conflict with the method described in the same code section. The Commission has, however, changed this language.

I am concerned that the provisions for notice on public projects are so different from that on private projects. In the case of a public project notice may be either by mail or personal delivery. There is no requirement for certified or registered. I agree that this is sufficient but it should be sufficient for either type of project, whether private or public.

With regard to your request in the note to Section 7108 for comments, my personal experience has been that service is very rarely an issue.[10] I would not favor the expandable means of proof of service. As stated in the preceding paragraph, I believe that any type of mailing should be sufficient.

Electronic service Section 7110

Section 7104 provides for service one of three methods, but to the listed three, there is added by Section 7110 providing for electronic communications. I do not perceive any significant value to the proposed electronic form for this means of service. Further, how is the person serving supposed to obtain permission from the recipient? If the serving party is able to obtain permission through some form of communication, it might as well serve the notice in lieu of a request to serve it electronically. If a potential claimant has the ability and opportunity to obtain such consent it might as well give the written notice. I suggest that, although we are in the electronic age of communication, no useful purpose will be served by permitting the service of a preliminary notice electronically.

Posting of preliminary notice Section 7112

Section 7112 noting an alternative method of service by posting of the notice in a "conspicuous place" is not feasible nor useful notwithstanding the Commission's earlier description of a "conspicuous place." Assume that work on a project has not commenced, there is no site: where would it be posted? Assuming the project work has commenced, such notice could be "posted" anywhere and there is no reason to believe that the person for whom it was intended would ever know about it. The comment that this posting is somehow similar to a notice of nonresponsibility or stop work notice, does not consider that the differing conditions existing at the time of posting of each of these two notices.[11] In each such instance there is usually an exist

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[10] It is also my experience that while the preliminary notice was intended to provide the owner or lender with the knowledge of which potential claimants exist, very few owners or lenders actually verify that the releases they obtain are by all those from whom they received preliminary notices. In one instance my client, a lender for more than $32 million, advised me that it simply did not keep the preliminary notices: "it was too much trouble" I was told. I have some doubt that the preliminary notice presently serves a very useful purpose .

[11] Years ago I encountered a jurisdiction in the mid west that provided for a notice that the project could not be liened if a notice was posted, leading to the job site, in the form of a bill

ing structure in existence. This would not occur where no construction has commenced.

I submit that on any occasion where service may be made by "posting" as the sole means of notification, there should also be service by mailing whether regular or certified. The only potential situation where this may not be feasible is the Notice of Non-Responsibility where the owner has no notice or knowledge of who is or will be working on the project.

Recoding notices Section 7114(e)

I believe the section to be confusing falling, as it does, in an Article describing service of the preliminary notice. It should be clarified as explained in the preliminary remarks on page 21 that it is intended that there is to be a uniform explanation of the means or manner of service of all documents and papers requiring service. My reading of the section led me to believe that the Commission is permitting the recording of a preliminary notice.

If this section is intended to describe, as explained in the preliminary remarks by the Commission, but not in the proposed statute, to describe when the various types of notices described in the section are complete, it should be clarified.

Written contracts Section 7130

Although Section 7130, incorporates existing sections Civil Code §§ 3097(l, m), it should be made clear that not all contracts between an owner and a direct contractor or between the direct contractor and its subcontractors are required to be in writing. This section is a carry over from the "Home Improvement Contracts" and the distinctions should be maintained. Simply changing the first word, "A" to "Any" possibly could resolve any conflict. Although this may appear superficial and unnecessary, I have encountered over the years situations, frequently on emergency repairs or work, where an owner and a contractor agreed for the work to be performed without any written agreement. Although we would all agree that they should put it in writing, it frequently is not written. It should not be invalidated because it was not in writing.

Proposed Public Contracts Code Section 43040 (public works) permits the preliminary notice to be served by mail or personally. Is there any significant reason why the preliminary notice on public projects should be different from those on private works of improvement? As I noted above, in the interest of uniformity and fairness the method of service should be the same. I see no reason why service should not be the same and personal service or regular mail or certified or registered mail should not be proper. On pages 21 and 23 the Commission has requested comment with regard to the subject of mailing. As I have previously noted, I have rarely encountered any difficulty with the fact of service whether from the post office or by regular first class

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board of certain large dimensions announcing that the project was a "no lien project." Presumably anyone coming to the project would see the billboard.

mail.

Section 7202 provides that the preliminary notice is to be given before a claimant asserts a claim of lien, stop payment notice, or a claim on a payment bond. Nothing in the section requires that the preliminary notice be given if no claim is asserted. On the other hand, Section 43060(b) provides for disciplinary action against a claimant if all of the conditions provided for in that section are not met including the service of the preliminary notice. As I note in my comments below regarding Section 7216(b) there is no sound reason to impose disciplinary action if a preliminary notice is not served. I believe some reference to Section 4306 should be made in Section 7202 and particularly my comments regarding the notice of Section 7204.

Building Permits Section 7132

In the Commission comments it is stated that half the cities don't provide space for the name of the construction lender. I am surprised that it is even half. Indeed, I find most communities ignore these requirements. If this is to be a requirement, should there be some form of penalty for failure to comply? I recognize the difficulty of enforcing such a provision and perhaps the provisions should just be eliminated since *de facto* they really do not exist.

Completion Section 7150

Much of the litigation involving mechanics liens arise from the two sections discussing and defining "completion" and the "notice of completion." Almost all major contractors and most construction contracts use the terms "substantial completion." California does recognize "substantial completion" in two statutes relating to the statutes of limitations governing actions for damages against builders, developers, designers, et al See Code of Civil Procedure §337.1(a) (lawsuit action limited to four years from substantial completion under certain circumstances) and §337.15 (a) (action limited to ten years from substantial completion under other circumstances).[12]

The difficulty that courts and attorneys seeking to guide their clients has been in the definition of completion as "actual completion." It is the same as defining an apple as an apple. This language is redundant and tautological and meaningless. I have rarely encountered a dispute over when a project has been substantially completed but there are many cases litigated over the issue of when there is an actual completion. On page 48 in footnote 133 the Commission referred to Craig P. Bronstein's law review article on "Trivial Imperfections." The article discusses and cites many cases that have discussed this issue and the problems created thereunder. There is no consistency between them. [13]

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[12] Civil Code § 337.15(g) also itemizes three alternatives to "substantial completion."

[13] Mr. Bronstein illustrates the distinction apparently drawn by decisions with the example of the contractor who is required to paint a wall green but paints it blue and is required to repaint

The courts have run the gauntlet and ranged all over the landscape in attempting to understand and define when there has been completion. In *Lewis v. Hopper* (1956) 140 Cal.-App.2d 365 it was the failure to supply, as required by the contract, of four soap dishes to a project that resulted in the court in deciding that project had not been completed. In my own case of *J.A. Jones Construction Co. v. Superior Court* (1994) 27 Cal.App.4th 1568, it was the failure to supply an inspection report and inspect an elevator on a multistory hotel that enabled the court to determine that the hotel was not completed and allowed a minimal recovery based upon the principal that it had supplied some material before the report was made and the elevator inspected.[14]

Essentially the distinction that seems to have been drawn between completion and non-completion is whether the project was totally completed as required by the contract. It rests upon the claimed distinction between "pickup" or "contractual" actions.

The average contractor or owner has no difficulty in determining when a project is complete. *In the construction trade "substantial completion" means when there is no more work required to be performed in accordance with the contract documents including any change orders except for punch-list, medial or "pick-up" work.*

If the Commission accomplishes nothing more, the change I suggested to "substantial completion" would improve the status of the law. *One cannot argue that existing law could be relied upon if there are no substantive changes, since there is no consistency in the law.*

On page 27 the Commission request comments upon the "separate contracts" that is the subject of Section 7154. I have had little difficulty where a Notice of Completion is recorded for a portion of a project when the project may be simply divided into multi-parts, e.g., a theme park, and each part is adequately described. The real problem arises then there is no Notice of Completion and the owner claims that there was either a cessation or a completion as to one part. Section 7154(a) is satisfactory, however, it would alleviate any potential problems if there was added to the sentence the words, "which notice shall specifically identify that portion" or similar

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it. Such work would be considered as "punch-list" or "remedial" work and the project would be considered as having been completed *before* the punch-list work was performed. Such work would not invalidate a notice of or actual completion. On the other hand, if the contractor did not paint the wall at all until *after* all other work had been finished and then painted the wall, the courts would consider the project not completed until the contractor painted the wall. See Bronstein, Loyola Law Review, p. 171, footnote 158.

[14] This case also led to the complete redrafting of the forms for releases. This problem will be discussed in the appropriate section below.

words.

Recording of Notice of Completion Section 7152(b)(4)

This proposed change could very well cause a serious problem. As presently stated, it would conflict with 7152(a) requiring notice to be recorded within 15 days of completion. However, Section 7152(b)(4) is open-ended in stating that an erroneous statement of the date appears to permit the notice to be recorded at any time including a date beyond 15 days required by 7152(a). A dishonest owner could simply take a project that is actually completed for example (say) on January 2d, record a notice of completion on February 14th reciting that the project was completed on February 1st. The "true date of completion is before the recordation" and although Section 7152(a) requires recording within 15 days, such owner is able to argue that it made an erroneous statement of the date of completion and therefore that governing date is the actual date of completion of January 2, and thus bar all claimants claims as not recorded within 30 days of actual completion.

This possibility may be easily avoided by stating in Section 7152(b)(4) the statement that an erroneous date "does not affect the effectiveness of the notice *if the recording of the notice is on or before and within (say) five days of the true date of completion.*"

The Commission has also questioned on page 40, whether a Notice of Completion is synonymous with "acceptance." There is a difference. Completion usually follows when the project work has been finished as originally planned together with any change orders increasing or decreasing the amount of work to be performed. The acceptance may occur at an earlier date resulting, usually, from a change from the original plans.[15] There is, of course, no reason why a public entity couldn't file a Notice of Completion upon the finishing of the work that was performed after the change. As stated earlier, I would retain the "acceptance" notice.

Service of Notice Section 7156

I agree that the owner should serve some notice upon those who have served the preliminary notice, but to impose the obligation of service by either express mail ($2.40 plus $.60 for delivery confirmation) or registered mail ($7.90 plus $1.35 for delivery confirmation), will result in unnecessary expenses to the direct contractor and thus the owner. Regular mail should be

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[15] On one occasion I had the situation where in the construction of a major hotel project, the owner accepted and opened the hotel for operations but subsequently continued to make numerous changes to the garage, entrance, swimming pool, the reception area, and many of the rooms. There were many liens recorded. Should the time for recording such liens have commenced when the owner took possession and commenced operations, when the building as originally designed was completed or when all changes were complete ?

sufficient. The apparent concern that a dishonest owner — as contrasted with the honest contractor — would claim service even though there was no actual notice, could be easily disproved by the abundance of others that served the Preliminary Notice and did not receive the notice from the owner.

Waivers and Releases Sections 7170 to 7176

The format proposed is certainly much more understandable although none of the releases contain a date when they are signed. I do not believe that stating "through date" with a date are the same. I will, however, confess that I am convinced that the codified waivers and releases are pretty much a waste of time and energy. The current statutory forms were as a result of my case of *J.A. Jones Construction Co. v. Superior Court* (1994) 27 Cal.App.4th 1568. The plaintiff was denied recovery because it signed a release and the trial and appellate courts decided that the signed release resulted in the loss of previously earned retentions. The legislature was besieged by contractors for a change. The problem has been, however, that because of the exceptions now incorporated into the forms, they are only a receipt as noted by the Commission in its comments on page 27:27-8 — a glorified receipt according to some descriptions. .

Most owners and lenders, although still requiring the releases, find them useless. The only advantage is that at the time of execution of any of the forms, except for the Unconditional Waiver and Release Upon Final Payment, the owners or lenders learn that there is an unpaid balance due as of the stated date. In the Conditional and Unconditional Waivers on a Progress Payment, the claimant reserves claims for extras in an unstated amount and all other potential claims in an unstated amount, including a claim breach of a contract.[16] At least in the Conditional Release on Final Payment it is required to state the amount of the disputed claims for extras. It would help if all the releases, if they are retained, should state what the claim is and the amount of the disputed claim. The conditional release ripens into and becomes unconditional upon payment. The latter two documents are the only meaningful ones. I recommend elimination of the two first release forms.

Regarding the Commission request on page 41 for comments regarding release portions of Civil Code § 3262 incorporated into Section 7166, I am unable to justify the need for this section. It is difficult to understand and even with the Commission's comments, I doubt that many do or will understand what was meant by this. I know of no decision that could have prompted this amendment. Further, subsection (3) effectively removes the use by anyone of this section. It would seem obvious that a claimant should be able to release a portion of a claim without specific

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[16] I am sure that in the experiences of the Commission's members they have learned that the largest claims are for extras, breach of contract including delay damages and payment for LSEM. These releases do not require any statement of any amounts for any of the foregoing. The releases for all practical and useful purposes are meaningless.

would seem obvious that a claimant should be able to release a portion of a claim without specific legislation authorizing it. [17]

Contents of Preliminary Notice Section 7204

Since the owner is required to serve a notice of the recording of a notice of cessation as a form of completion, shouldn't the first Notice to Property Owner include a statement to that effect? Moreover, the comments I made earlier regarding the requirement imposed upon subcontractors to serve a preliminary notice, could be included in this preliminary notice.

Disciplinary action Section 7216(b)

The Commission has requested on page 50 comments regarding the disciplinary action for the failure to give the preliminary notice. When the preliminary notice provisions were first discussed, many subcontractors and materialmen objected to it upon the basis that prospective owners would be frightened upon receiving the notice at the prospects of liens, claims, etc. Those objecting to the use of the preliminary notice were finally satisfied when there was added to its contents language that, as I recall now, stated that "this notice is required by law to be served by the undersigned as a statement of your legal rights. This notice is not intended to reflect upon the financial condition of the contractor or person employed by you on the construction project." The provision was not accepted by revision committee although I believe it still deserves consideration.

I agree that there is no reason to impose disciplinary action upon a person for not serving the notice except where it asserts a claim and failed to serve the notice. I am not aware of any contractor being subjected to such action by the CSLB for failure to serve the notice. However, in the few instances of which I am aware, the person serving the notice was able to explain that the law required it and resolve the concerns of the recipient by that explanation. Section 7216)b).

Design Professional liens Section 7304

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[17] It is regrettable that legislatures do not read carefully the legislation they enact. Business & Professions Code § 7159 that the Commission has made some revisions to as noted on page 169. Can anyone understand or explain how Section 7159(b) can provide that a "home improvement contract means an agreement, whether *oral* or written . . . . " and then provide in 7159(c)(1) for the contents of the written agreement including that it "be in writing." As long as the provision is being amended, the "oral" should be eliminated.

This section is too long and should be shortened. I have had various inquiries from designers asking questions about it and it should be restated and shortened to be more meaningful and understandable.

Although I think it is obvious, I have been asked on several occasions by design professionals if they were entitled to lien since this section provides that their lien previously recorded expires if work is commenced on the project. I have advised them that they could now record a new lien for their services as any other claimant furnishing LSEM to a project. I based that advise on Civil Code § 3081.6, your proposed Section 7304. Its intent should be clarified.

Time for recording a claim of lien Section 7412(2)

As I noted earlier, I fail to understand why the time for recording the lien by the direct contractor and all others is different (60 days v. 30) when there is a notice of completion is recorded but when there is no notice of completion recorded the time for recording of 90 days is the same. Why not the same in both situations?

Notice of intent to record a lien Section 7420

I see no reason why, in addition to every other notice, it makes sense to also require a lien claimant to give notice of an intent to record a lien. Just how long before the actual filing is such a notice required: simultaneously? The day before? Is it intended to have some effect? I foresee all potential claimants and every trade organization voicing strong objections to this proposed new section.

If it is enacted, it will be necessary to give everyone additional time to record their liens. For example, claimants who are not direct contractors, are given only 30 days to record a lien if there is a Notice of Completion. To require that such claimants must first serve a Notice of Intent to be meaningful and intended, presumably, to have some effect, will require additional time. At least the direct contractor has 60 days.

What will happen if a claimant gives a notice and the owner or contractor calls and requests the claimant to hold off while they discuss the matter? The claimant complies and waits. Must the claimant now serve a new notice? Will such claimant have time to record a lien. Inactment of this section as a prerequisite to recording a lien, may result in less negotiations for settlement of disputes.

What kind of notice is required? Does Section 7102 control? Since the proposed section requires that a copy of the notice must be attached to the recorded lien, I assume some writing will be required but what kind? How is it to be served? Most claimants do give some notice, usually admittedly in the form of a threat of a lien, but to require to require a copy to be attached to the lien, only adds to the cost of the recording. There are several code sections defining

various types of notices. Will a letter demanding payment and attaching the copy of the proposed lien be sufficient? I also foresee some difficulty with the county recorder. Is the recorder permitted to judge the adequacy of the notice? Will the recorder accept an un-acknowledged notice?

I see no necessity of this section. There is no benefit to be derived from this requirement. It serves only as a warning and by the time it is served, there usually has been any number of warnings. It is not unlike saying that, after numerous warnings, now saying "and I now really mean it."

Amount of lien Section 7430

The Commission requested comments regarding the omission of Civil Code §3123(c). This is the only section in the existing law that uses the term "prime contractor" that I have suggested, but I assume it means, in the context used by you, the "original contractor." The purpose of §3123 (requiring the owner to notify the surety) was to protect sureties so that if the cost of the project was increased beyond the penal sum of the bond, the surety could demand additional security from the principal. Such notice does put the surety on notice of an increased risk. Five percent of the contract price seems reasonable. See my comments above relating to Sections 7057 and 7142.

Proposed Section 7430(2) serves no useful purpose. Is proposed section 7430(2)(b) an effort to eliminate such claims as attorney fees and delay damages? Included as an allowable claim are breaches of a contract, but limited by the value of the LSEM furnished. It is unclear what is now eliminated or included.

Interest subject to lien Section 7442

I have two problems with the changes in this section. Although the Commission's comments are that this restates former Civil Code §3129, there is a change in that could have a substantial impact on the mechanics lien laws. The Commission has omitted from Civil Code §3129 the part that read "that every work of improvement *is deemed to have* been constructed with the knowledge of the owner or of any person having or claiming an estate therein shall have to have been constructed, performed, or furnished at the instance of such owner or person having or claiming an estate therein . . ." (Emphasis added.) The omitted portion should be retained.

It not only justifies the claim of lien for LSEM furnished to a project but once the claimant carries the burden of establishing that it furnished the LSEM, the omitted portion placed the burden upon the owner to prove otherwise. For example, in a situation where the owner employs a general contractor or a construction manager who uses subcontractors and otherwise orders materials. The presumption raised by the omitted provision gives the claimant rights to assert its claim. Otherwise, the owner may assert it never authorized the use of such subcontractors or materialmen. This section should not be omitted.

The Commission has provided in 7442(a) that the interest of the person that contracted for the work of improvement is subject to the lien and I presume it was the intent that this would include the owner of the property. However, owners are not necessarily the person contracting for the work of improvement. Consider the example I discussed previously where an owner of a parcel of land, whether improved or not, employees a management concern to make improvements. Under the contemplated provision, the fee owner of the property interest in the property would not be subject to a lien if that owner had no knowledge of the *all items in and of the LSEM* being furnished to the project. A Notice of Nonresponsibility would not be available to such owner.

Under the proposed change, eliminating the existing presumption of knowledge, the owner's fee interest would not be subject to the lien. If not destroying the very purpose of the mechanics lien laws, it would seriously hamper enforcement of the claimant's lien rights.

Priority of advances by lender Section 7456

Responding to your request for comments I don't recall the discussions regarding this section when involved in the 1969 revisions, and I don't believe I understand the existing statute. Your proposed Section 7456 refers to "optional advances for construction costs" but the original code included payment of liens as well as other costs of the work of improvement. The payment of liens or stop payment notices increases the loan and may be cause for default under the loan agreement. I believe the proposed section to be inconsistent with the understanding of most lenders who are most affected by it.

Mandatory advances can only relate to the original construction loan and the term "optional advances for construction costs" refers to loans in excess of the original loan. Any advances over the original amount stated in the original construction loan and the commitment by the lender must necessarily be optional advances under some new agreement with the borrower. Thus, the last clause in Section 7456(b) commencing with the word "provided" should be replaced with language to the effect that any loan or advances beyond the amount of the original construction loan should not have priority over any liens. Moreover, if a payment bond was issued for 75% of the original construction loan as required by Section 7452(b), it would be inadequate to cover any optional advances.

Time for Commencement and extensions to time Section 7460

Civil Code §3144(b) provides that if the lien was not foreclosed, absent an agreed upon extension, the lien was "automatically null and void." This has been changed by 7460 to provide that the "lien expires and is unenforceable." It is my belief that the original language would and should prevent the refiling of the lien. Allowing a claimant to file a mechanics lien, ignore the 90-day requirement and then being allowed to re-file it, appears unfair and unjustified. I recognize the result in *Solit v. Tokai Bank, Ltd.* (1999) 68 Cal.App.4th 1435 but I submit that the appellate

court incorrectly interpreted the law.[18]

The proposed section properly reflects current law. However, it is my belief that anyone that may be affected by the extension, should also be required to sign it. For example, the construction lender. If only the owner executes the extension and there is a break in priority, the lien claimant may be barred from asserting a lien claim against a non-consenting lender.

Dismissal for lack of prosecution Section 7466

Although I am aware of only one decided decision on under this section, it is an antiquated provision. Two years is hardly sufficient with the inability of the courts to entertain a trial time in some jurisdictions. I believe that the regular rules of the Code of Civil Procedure should be applicable and this section eliminated. There is no logic or reason to restrict the time to this two-year limitation. If the intent was to require claimants to process their claims expeditiously, the defendant may always seek an early trial date.

Liability of contractor Section 7456

Although many contracts provide that if the contractor does not defend and the owner is required to defend, that the owner is entitled to its attorney fees. It is not, however, statutory, and it should be added so as to allow attorney fees in such circumstances.

With reference on page 35 for request for comments on attorney fees, I believe that under the British legal system of imposing costs and fees on most actions, sometimes even those that are not frivolous, have a strong negative effect on frivolous or questionable actions. My comment is consistent with my belief that California law would be better served if the courts were empowered to award attorney fees in any case, regardless of contractual obligations, where the lawsuit was frivolous or, in the opinion the trial court, unjustified. Appellate courts have imposed sanctions for frivolous actions and I submit that the trial courts, which do have similar authority have been reluctant to impose them. Perhaps a provision in the lien laws permitting the award of attorney fees would be more effective.

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[18] This case is cited in the Commission Report on page 114 in connection with proposed Section 7480. Undoubtedly I am prejudiced. I was the trial court attorney and obtained a judgment denying the right of the claimant to re-file a lien that it had released upon demand and which had become "null and void" since there had not been a timely foreclosure upon it. An appeal was taken by my client, Tokai Bank, but it used a different firm to represent it on the appeal. It was then reversed. I believe it is wrong to allow a claimant to miss a statutory deadline (e.g., a statute of limitations) and escape the consequences by refiling the lien claim.

Petition for release order Section 7480[19]

I call the Commission's attention to the fact that although a mechanics lien will be recorded by the county recorder when it is signed and verified (Civil Code § 3084), the county recorders insist that a *release* of the lien be acknowledged before a notary. Is there any reason or logic by such a requirement? It would seem that the release should be signed and verified in the same manner as required for the recording of the lien.

Time of hearing Section 7486

The moving party has all the time it may desire to prepare the petition. Morever, the petitioner is only required to serve the petition *not less than 10 days* (plus five days if served by mail) before the hearing date, which is required by the proposed section to be set by the clerk for not more than 30 days from the date of filing of the petition.

The procedure is very similar to a Motion for Summary Judgment in a civil proceeding. The respondent on a Motion for Summary Judgment is granted 75 days to respond. Code of Civil Procedure §437(a). It is unfair to limit the time for the respondent under Section 7486 to respond to what is essentially a Motion for Summary Judgment. Under the existing law, at least the respondent is given between 10 and 20 days, which I still don't consider sufficient and should be extended. Civil Code §3199.

The respondent should have ample time to obtain and present its evidence so that a fair and full hearing may be conducted. One reason the courts have generally denied such motions or petitions are that the courts realize that even if there appears to be merit to the petition, the court also recognizes that the respondent does not have sufficient time to prepare a proper and complete opposition and therefore the courts are reluctant to terminate a claim based upon a petition and without a full hearing. Although the court has the authority to extend the time to respond the date of hearing beyond the original 30 days, it would appear that the court does not have the authority to extend the time for the response to be filed. According, I submit that the time for the service of the petition should be immediately upon its filing and the time for the filing of filing substantially extended. Fairness would support such extensions. It would, moreover, probably result in better briefs resulting in more reasoned decisions from the courts hearing such petitions.

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[19] At the time of my participation in the re-drafting of the lien laws that were enacted effective 1971, I and others had this procedure on private projects in since it was available on public projects. It was rejected at that time but it is a valuable but added some nine years later. As state elsewhere, however, in my discussion of Section 7486, the time limits should be extended.

Effect of court order without prejudice Section 7492

If the effect of the granting of the petition is "equivalent to cancellation of the claim of lien and its removal from the record," how can it be anything but with prejudice? How can the court order the lien's removal "without prejudice"? If the lien is cancelled — really discharged — what is the effect if the court granted the petition "without prejudice"? The claimant will have lost all rights. Although Section 7492(b) states the substance of existing law, it still is not logical and should be removed.

Stop payment notice by owner Section 7520

Although I am aware of the provisions of this section as presently contained in Civil Code §3158, I am not aware of it ever being used. Although there may have been some valid reason to have included it in the statutes, the only reason that an owner would use this provision would be when the owner, whether justified or not, wanted to excuse its failure (or refusal) to pay the direct contractor. If an owner ever used this provision, probably the project would stop upon the service of such notice. I believe it should be abolished.

Stop payment notice to owner and construction lender Sections 7520 and 7530

On private works of improvement all claimants other than the original contractor may serve a stop notice upon the owner. Civil Code § 3158. However, all persons, including the original contractor may serve it upon a lender. Civil Code § 3159. However, on public works all claimants, except the original contractor, may serve such notice on the owner. Civil Code § 3181. These distinction are retained in the proposed law. All claimants, except the original contractor may serve a stop payment notice on the owner. Section 7520.

There is, however, a substantial change relating to public projects Section 7530 retains the same provisions and permit a stop payment by all claimants to serve a stop notice to the lender on a public work of improvement. Proposed Section 7530(b), makes a substantial change in the law by providing that all persons, other than the original contractor, are limited in what they may claim in the stop payment notice. It provides that all persons giving a notice to the construction lender may only claim it for LSEM furnished to the project. This would indicate that the original contractor may file a stop notice for claims *other than* for LSEM furnished to the project, e.g., breach of contract, delay damages etc. Such claims are not presently permitted by any stop notice claimant on any project. I have no objection to the change although it would seemingly beyond the concept of the lien laws, but the change should be noted.

Objections to bond Section 7534

Neither the existing law nor the proposed law make any provisions for any procedure for resolving the objections. Although in a civil attachment proceeding, a court would have jurisdic-

tion to the sufficiency of a surety and to the surety, it does not necessarily follow that such jurisdiction would carry over to stop notice undertaking. Code Civil Procedure § Section 4822.20 ff. Some method for objection to the surety should be considered.

Distribution of claims Section 7540
Amount withheld Section 7542

Under proposed Section 7536((b)(1) the lender has the option to withhold funds upon the service of an unbonded stop notice. Nonetheless, under 7540(a)(2) it may distribute the construction funds to such unbonded stop notices. It is inconsistent to provide that if the lender *may* withhold monies based on an unbonded stop notice and then provide in 7540 for distribution to such claimants. If the lender exercises an option, not to withhold, is it logical to provide that it may distribute funds to such claimant later? Is this section consistent with Section 7542(b) limiting the liability of the lender? Is it the intent to provide, that although optional, if the lender does withhold, that the distribution to such unbonded claimants would follow those made to the bonded stop notices? If so, it should be clarified to express that intent. Further, would a lender or the borrower be in a legal position to object to the lender exercising its option to and withhold on an unbonded stop notice? What happens if the total of all the bonded stop notice claims exceeds the total amount of available funds? Shouldn't the claimants that served bonded stop notices be in a position to object to distribution to unbonded stop notice claimants? The withholding on unbonded stop notices reduces the available funds to bonded stop notice claimants.

Section 7542(b) limits the liability of the lender to only the amount of the bonded stop notices. Will this relieve the lender from any liability for its exercise of its option to honor an unbonded stop notice? This should be clarified.

You request a comment upon 7542(b) whether there is a possibility of it being repetitious of 7542(a), and I believe it is, but I also believe that 7542(b) is inconsistent with 7540 (permitting a withholding). I would agree that the surety should not be liable for more than it withholds but that if it withholds funds, whether the stop notice is bonded or unbonded, it should be held liable to the claimants to the extent of the withheld funds providing, however, that there are sufficient funds available to pay the bonded stop notices in full.

Time for enforcement of stop notice Section 7550

Regarding the request for a comment on the change, I believe that five-day notice should be mandatory. The lender and borrower should be advised of the action as soon as possible.

Dismissal of enforcement Section 7554

The comments I made with respect to dismissal for lack of prosecution Section 7466 above, are appropriate here. Two years is not sufficient. There is no reason for this requirement.

Public policy of payment bond Section 7600

Please see my comments to Section 7030 above. The terminology in the first alternative clause that the bond is security against "a direct contractor's failure to perform the contract . . . " improperly describes the bond. This first clause describes a Performance Bond, not a payment bond. The coverages of the two types of bonds are different.

Bonds lending institutions Section 7604

It appears that present Civil Code § 3237 had erroneously omitted a "not" since it makes no sense that a lender could object to a licensed insurer. The Commission comments regarding this on page 43 are quite appropriate. You have correctly changed this by adding the word "not" to prohibit an admitted surety insurer from objecting to an admitted insurer.

Security for large projects, Chapter 7

This provision was originally enacted at the request of the A.G.C. and B.C.A. so as to insure payment to the general contractor by the owner. I have had almost no experience with this provision. I am aware of a situation where a substantial general contractor who was preparing a bid on a major project where this provision would have been applicable was lead to believe that if it requested for any security to be posted for the owner's benefit under this provision that the contractor should not bother to bid. I don't know if this is a regular practice or just the experience of one concern. The same concern also informed me that it considered this section simply incomprehensible. I am curious if it is used.

Acceptance and Cessation on Public Projects

With respect to the Commission's request on page26 for comments and further discussed on page 50, regarding "acceptance" by the public agency, I do believe the present use of acceptance by the public project is necessary. The acceptance by a public agency of the project is equivalent to the acceptance by an owner in the present statute that has been eliminated by the Commission. There is, however, a significant difference. A public project is "accepted" by the administrators of public projects, and if not, should be by a formal "acceptance" in the form of a resolution or other public act. Thus, everyone is able to verify and check to determine if the project as been accepted and it does set a definite and certain date for completion. Perhaps some form of notification to potential claimants may be advisable. I would not recommend the change to eliminate acceptance on public projects.

Regarding the request for comments on page 49 regarding the recoding by a public agency of a Notice of Cessation, there is a difference between "cessation" and "acceptance." Claimants who worked in the early stages of a project tend not to monitor its progress and may very well have their rights adversely affected by a cessation of which no notice was given. In the interest of

safeguarding the rights of potential claimants, I believe that the recording of such notice would be advisable.

Stop work notice, Article 3

My problem with ths article and particularly Sections 7832 and 7834[20] relates to the question of service and posting of the notice. I recognize that under Sections 7102 and 7104 the Commission has defined all methods of service and presumably any person using the stop work notice will have knowledge of the various means of service. As I commented earlier relative to Section 7112 respecting the posting of a preliminary notice, the stop work notice article refers in various sections to serving the notice and to a posting by the direct contractor of the notice. The manner of service and the place of posting should be more explicit. There are penalties for the failure to either serve and post under Sections 7838(a), and the statute should provide specifically upon whom, how, and where it will be served and posted or at least contain a statement referring the claimant back to Sections 7102 and 7104.

Conclusion

As I stated at the outset, I am convinced that the mechanics lien laws should be completely rewritten to be simplified so as to make them understandable to all persons that use them or used by others against them. Much of the litigation arising in this field of law arises from the misinterpretation and failure of the participants to understand them. Although I know that the members of the Commission have considered this alternative, I also understand the reasoning behind not making the changes, even though I do not agree with them.

I realize that the Commission has devoted substantial time and effort and that its work is not completed. What you have accomplished is deserving of a complement for your work. I hope that the comments I have made relating to the specific sections will be helpful. I hope I have been of some assistance and if I may be of any further assistance, please do not hesitate to call upon me.

Sincerely,

HOWARD B. BROWN

HBB:ss

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[20] Why is the contractor only required to "give" a copy of the notice to the lender. At least the person being given the notice should be the same person or location as the other notices served upon the lender.

COMMENTS OF MICHAEL BROWN

From: Michael Brown <mbrown@vpn.cslb.ca.gov>
Date: September 21, 2006
To: Steve Cohen <scohen@clrc.ca.gov>

Article 7. Release Order

7480 Petition for release order
7480. (a) The owner of property subject to a claim of lien may petition the court for an order to release the property from the claim of lien, and in addition may file a complaint with the Contractors State License Board for any applicable administrative remedies, for any of the following causes:

Alternate Language -
7480
(b) This article does not bar any other cause of action or claim for relief by the owner of the property, including but not limited to filing a complaint with the Contractors State License Board for any applicable administrative remedies, nor does a release order bar any other cause of action or claim for relief by the claimant…

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FILE NO. 1000

September 21, 2006

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

Re: Mechanics Lien Law - Proposed Revision

Dear Members of the Commission:

I am writing with regard to recommendations that were published in June by the Commission with regard to the proposed Section 7480 (the present Section 3154) .

Both the present statute and the proposed statute provide that "the owner" may petition the Court for removal of a lien.

Usually each person or entity involved in the construction process is obligated to provide lien free performance by its employees and vendors. The owner needs the power to prosecute such a proceeding to clear title, particularly if the lower tier parties are unwilling to undertake to clear title. On the other hand, it is inefficient for the owner to prosecute a lien release proceeding and then charge the cost to the contractor and then perhaps for the contractor to charge the cost to a subcontractor.

In some cases the contractor or subcontractor, etc. can arrange with the owner to prosecute a lien removal proceeding in the name of and on behalf of the owner, but frequently there are major or minor disputes between the owner and contractor, etc. which make such an arrangement unwieldily.

Accordingly, I would suggest that 7480 (and present 3154) be expanded to grant standing to prosecute such a proceeding to (a) the general contractor, (b) the person

named in the lien as the person that contracted for the work, labor or material and (c) perhaps any person who may be obligated by contract to provide lien free performance.

Very truly yours,

Paul N. Crane

PNC/dk
1000/C/060921

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FILE NUMBER 9904-304

September 22, 2006

Nathaniel Sterling
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Re: Tentative Recommendation re Mechanics Lien Law (June 2006)

Dear Mr. Sterling:

This is in response to the California Law Revision Commission's ("Commission") June 2006 request for public comment concerning the Tentative Recommendation re Mechanics Lien Law. Our comments primarily respond to the Commission's specific requests. We also discuss the tentative recommendations concerning Civil Code §§3097 and 3098.

Relocation of Public Works Stop Notice Statutes (Tent. Rec., p. 16.)

We agree with the proposed relocation of the statutes governing remedies on public works from the Civil Code to the Public Contract Code. In order to be consistent, "completion" of public works should be removed from the proposed draft of Civil Code §7150. This will more clearly distinguish private works from public works, and will help to avoid any confusion with the separate definitions of "completion" of public works that appear in proposed Public Contract Code §42210, and in existing Public Contract Code §7107.

Proposed Change in Language of Public Contract Code §42210 (Tent. Rec., p. 146.)

Civil Code §3086 currently states, in pertinent part:

> "If the work of improvement is subject to acceptance by any public entity, the completion of such work of improvement shall be deemed to be the date of such acceptance; . . ."

Proposed Public Contract §42210 inexplicably alters this language so that completion occurs upon "[a]cceptance of performance by the public entity." [Emphasis added.] There does not appear to be any explanation for changing acceptance of "work" to acceptance of "performance," and the proposed statutes do not define "performance." Accordingly, the Commission should further evaluate whether this change is warranted, and that it may result in unnecessary litigation concerning the meaning of "completion."

Formal Acceptance by Public Entity Under Civil Code §3086 (Tent. Rec., pp. 25-26.)

The Commission reports that some practitioners believe the above-quoted "acceptance" language should be eliminated from Civil Code §3086(c) because it allows the owner to hold open the lien claim period and thereby force the contractor to make changes. (*See* Tent. Rec., pp. 25-26.) This ignores the distinction between subcontractor claims and disputes between the owner and the general contractor. This also fails to acknowledge that "acceptance" provides a clearly defined completion date that benefits both stop notice claimants and public entities. If adopted, this proposal would create uncertainty as to when completion occurs, and thereby increase litigation concerning stop notice deadlines.

The premise that public entities gain some advantage over contractors by withholding acceptance is mistaken. Under the existing statutes, once a work is "completed" under Public Contract Code §7107 (i.e., occupancy, beneficial use and cessation of labor, etc.) the public entity should release retention funds, and the general contractor should use those funds to pay subcontractors (as required), even if the project has not been "accepted" under Civil Code §3086.

If there is a dispute between the owner and the general contractor (i.e., contractor's claim for extra work, owner's claim for defective work, project delays etc.), the owner's most significant remedy is to withhold contract retention funds—not acceptance. Under Public Contract Code §7107 the public entity may withhold 150% of the disputed sum regardless of whether the project has been "accepted." Indeed, if a public entity refuses to accept defective work it arguably allows the general contractor additional time to work with its subcontractors to resolve the problem before stop notices are filed.

Further, the formal acceptance and notice of completion of a project are public records that provide the public entity and the stop notice claimant with a clearly defined 30 day deadline for stop notices. (*See* Civil Code §§3086, 3184, 3093 and proposed Public Contract Code §44140.) Indeed, even if there is no notice of completion, or if the notice of completion is untimely (Civil Code §3093), the subcontractor—based upon public records—still has the certainty of knowing that it may file its stop notice within 90 days of formal acceptance. *See Department of Industrial Relations v. Fidelity Roof Co.* (1997) 60 Cal.App.4th 411, 418. There is no existing alternative to these clear and beneficial deadlines. Elimination of formal "acceptance," therefore, would likely expand the scope of litigation concerning the applicable deadline for stop notices.

Harmonizing The 30 and 60-Day Cessation of Labor Provisions of Civil Code §3086 (Tent. Rec., pp. 47-48.)

In evaluating the utility of harmonizing the 30-day "cessation of labor" provision for completion of public works with the 60-day provision applicable to private works (*See* Civil Code §3086), the Commission should also consider Public Contract Code §7107, which governs

the release of contract retention funds, and which also provides for completion upon a 30-day cessation of work.[1]

Notice of Cessation of Labor Under Civil Code §3086 (Tent. Rec., pp. 48-49.)

We respond to the Commission's four specific questions concerning the utility of the "notice of cessation" provision under Civil Code §3086:

1. Is the notice of cessation intended to apply to a public work?

   This is resolved by the provisions of Public Contract Code §7107, which only applies to public works, and which specifically authorizes a notice of cessation as one means to establish project completion under §7107(c)(4).

2. Does the notice of cessation have a major effect on a public work?

   The 60-day effect may be significant. A timely notice of cessation requires the subcontractor to file its stop notice within 30 days of the recording of the notice. Otherwise the stop notice is due within 90 days of completion (i.e., 120 days from the initial work stoppage). (*See* Civil Code §3184.)

3. Why would a public entity record a notice of cessation if completion is deemed to have occurred on the 30th day after cessation of work regardless of whether or not the notice of cessation is recorded?

   The public entity may wish to expedite the deadline for stop notices under Civil Code §3184. This may, for example, allow the public entity to more quickly account for stop notice claims arising from work performed for a defaulting general contractor.

4. If the public entity records a notice of cessation on the 45th day of work stoppage, do the statues of limitation begin to run at that time, or do they continue to run from the 30th day?

   Under Civil Code §3184 stop notices must be filed within 30 days of the recording of either a notice of cessation or a notice of completion. At least one case interprets this statute, in the context of the notice of completion, to hold that the limitation period begins to run anew from the date of recording. *See, e.g., Department of Industrial Relations v. Fidelity Roof Co.* (1997) 60 Cal.App.4th

[1] We understand that the Commission is only discussing the possibility of harmonizing the 30-day cessation of labor provision for completion of public works (*See* Civil Code §3086 and proposed Public Contract Code §42210) with the 60-day provision applicable to private works (Civil Code §3086 and proposed Civil Code §7150), and has not proposed any revisions in this area.

411, 418. Thus, if the notice of cessation were recorded on the 45th day of work stoppage, the deadline for stop notices would run on the 75th day after the work stoppage rather than the 120th day.

The notice of cessation in the public works context is not a procedure that "causes more problems than it solves." (*See* Tent. Rec., p. 49.) Rather, as with the provisions for formal acceptance and filing of a notice of completion, this procedure provides additional certainty to both owners and contractors with respect to applicable deadlines.

Proposed Revisions to Civil Code §§3097 and 3098 (Tent. Rec., pp. 72-97; pp. 142-155.)

Finally, we note that the proposed revisions to Civil Code §§3097 and 3098 may not fully achieve the goal of making these statutes more usable. (*See* Tent. Rec., p. 15.) We agree that Civil Code §3097(i)-(l) and §3098(b) are arguably misplaced and should be relocated to separate code sections. However, while the remaining provisions of Civil Code §3097 and §3098 are lengthy, they also provide the information necessary for filing a Preliminary 20-Day Notice in a single location. The proposed revisions to Civil Code §3097, for example, would scatter this basic information over 12 separate code sections ranging from proposed Civil Code §7034 to proposed Civil Code §7218. Thus, with the exception of Civil Code §3097(i)-(l) and §3098(b), we believe the remaining provisions of Civil Code §3097 and §3098 should remain in single code sections, or at least be located in sequential order and in close proximity to each other.

We hope that our comments assist the Commission in completing its work. Please contact us if you have any questions.

Very truly yours,

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September 27, 2006

Via E-Mail and Overnight Delivery

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

Comments from California State Council of Laborers Legislative Dept. and Construction Laborers Trust Funds for Southern California on Tentative Recommendation for Mechanics Lien Law

Dear Members of the Commission:

The following comments to the Tentative Recommendation of the California Law Review Commission for Mechanics Lien Law are made on behalf of the California State Council of Laborers Legislative Department (Laborers), and the Construction Laborers Trust Funds for Southern California (Laborers Funds). The Laborers Funds are multi-employer employee benefit plans in the construction industry; what are referred to in your Tentative Recommendations as "express trusts" and "laborers compensation funds." They provide a variety of benefits to laborers in the construction industry, the persons for whose benefit the mechanic lien law was enacted before California was even admitted as a state in the United States.

The Laborers were the sponsor of the last significant revision of the mechanic lien law, in 1999. SB 914, authored by S. Sher, enacted as Ch. 795, Stats 1999, was meant to keep the mechanic lien law from being preempted by the Employee Retirement Income Security Act (ERISA) § 514, 29 U.S.C. § 1144. The undersigned was primarily responsible for drafting SB 914, and testifying on its behalf through the legislative process. Our comments are directed primarily at maintaining the intent and effect of SB 914 in the proposed revisions to the mechanic lien law. We also address provisions which were left out when the public works portion of the law was separated from the private works in the Tentative Recommendation.

The Tentative Recommendation inadvertently undoes the intended effect of the 1999 legislation, and may leave the mechanic lien laws vulnerable to being again challenged as preempted by ERISA. This is a complicated area of the law, which requires a good deal of analysis. The Tentative Recommendations also separate the provisions regarding public works from the provisions regarding private works. While this may be desirable from the standpoint of organization, the proposed changes have inadvertently left out from the public works law several provisions intended to apply to both public and private works. The entire law should stay true to

the constitutional mandate to the Legislature that "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." Cal. Const., Art. XIV, § 3.

Our comments follow. Enclosed also are the actual changes we propose to the Tentative Recommendation, the Prepared Statement I submitted in Support of SB 914 (explaining the intent of that bill), the decision of the California Supreme Court in *Betancourt v. Storke Housing Investors*, and the decision of the Ninth Circuit in *Southern California IBEW-NECA Trust Funds v. Standard Industrial Electric*, both upholding the law as not preempted by ERISA.

I am available for questions, discussion or further input, at the address, phone and e-mail listed here. The best way to contact me is at this e-mail address: jds@racclaw.com

Thank you for your consideration.

Sincerely,

J. David Sackman, of
Reich, Adell, Crost & Cvitan

following: Comments (enclosed as separate file with e-mail)
encl: Proposed Changes to Mechanic Lien Code Revisions
Prepared Statement in Support of SB 914
Decision of CA Supreme Court in *Betancourt v. Storke Housing Investors*
Decision of 9th Circuit in *So. Cal. IBEW-NECA Trust Funds v. Standard Ind. Electric*

cc: Mike Quevedo, Southern California District Council of Laborers
Jose Mejia, Cal. State Council of Laborers
Ric Quevedo, Construction Laborers Trust Funds for Southern California
John Miller, Cox Castle & Nicholson
Alexander Cvitan, Reich, Adell, Crost & Cvitan

THE NEED FOR, AND PURPOSE OF, THE 1999 LEGISLATION

The stated purpose of the 1999 legislation was to "restore the protection created by the mechanic's lien law adopted at the first legislative session of this state, refined and expanded over a century and a half, for the just pay due to workers on construction jobs, without discrimination as to the manner in which the pay is allocated, whether union or nonunion, in cash or a combination of cash and benefits." Stats 1999, ch. 795 § 9. This hails back to the original purpose of the law, which is older than the state itself.

California adopted a mechanic lien law in its first legislative session (which was held before the state was formally admitted to the Union). 1850 Cal. Stat. 211-13, ch. 87 §§ 1-4. *See generally*, Sackman, Lien On: The Story of the Elimination and Return of Mechanic Lien, Stop Notice and Bond Remedies for Collection of Contributions to Employee Benefit Funds, 20 BERK. J. EMP. & LAB. L. 254-85 (1999) (*Lien On*); Lucile Eaves, A HISTORY OF CALIFORNIA LABOR LEGISLATION, 233-243 (UC Press 1910). The mechanic lien statute was among the pro-labor laws elevated to a place in the 1879 Constitution, Art. 20 § 15, and can now be found (with nearly identical language) in Art. 14, § 3 of the California Constitution:

> "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."

What was simply another law thereby became a Constitutional mandate to the Legislature, to make sure that laborers were protected by a perfect lien procedure. *See* Connolly Development, Inc. v. Superior Court, 17 Cal.3d 803, 808, 132 Cal.Rptr. 477, 55 P.2d 637 (1976), *appeal dismissed*, 429 U.S. 1056 (1977).

In the last half-century, employee benefits such as pension, health and vacation, have emerged as a major element of that compensation. "In the construction industry, employees receive more of their compensation in the form of retirement and savings benefits than in any other industry." U.S. Dept. of Labor, *The Editor's Desk: Importance of Retirement Benefits in Compensation*, MONTHLY LABOR REVIEW (8/2/1999). *see also*, Sackman, Restoring Mechanic's Lien, Stop Notice and Bond Protections, 23 LOS ANGELES LAWYER, 19, 20 n. 35 (June 2000); *Lien On*, at 282 n. 185.

Recognizing the importance of fringe benefits to workers, the U.S. Supreme Court held that fringe benefit contributions are included in the "value of labor" guaranteed by these remedies. U.S. ex. rel. Sherman v. Carter, 353 U.S. 210, 217-18, 77 S.Ct. 793, 1 L.Ed.2d 776

(1957).[1/] The *Carter* decision was soon followed by California Courts. *See* *Dunlop v. Tremayne*, 62 Cal.2d 427, 42 Cal.Rptr. 438, 398 P.2d 774 (1965) (holding fringe benefits included in priority under Code Civ. P. § 1204); *Bernard v. Indemnity Ins. Co.*, 162 Cal.App.2d 479, 329 P.2d 57 (1958) (holding fringe benefits included in protections of payment bonds for public works). The California Legislature codified these decisions when it first explicitly included fringe benefit contributions in the labor covered by mechanic liens, in 1965. 1965 Cal. Stat. 2149, ch. 737, § 1.[2/] This maintained the original purpose of the mechanic lien law, by making sure that fringe benefits, as well as cash wages, were protected by these remedies.

Ironically, the threat to this protection came from another law designed to protect fringe benefits of workers. The Employee Retirement Income Security Act (ERISA) was enacted to protect pensions and other fringe benefits of workers. 29 U.S.C. § 1001(b); Pub. L. 93-406, title I, Sec. 2, Sept. 2, 1974, 88 Stat. 832. Congress capped ERISA with a broad preemption section, declaring that "the provisions of [ERISA] shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 1003(a) of this title and not exempt under section 1003(b) of this title." ERISA § 514(a), 29 U.S.C. § 1144(a). In 1980, Congress added provisions to ERISA, explicitly stating a federal cause of action to collect delinquent benefit contributions, in the Multi-Employer Pension Plan Amendments Act of 1980. Pub. L. 96-364, 94 Stat. 1209, *et. seq.*

Early decisions interpreting the preemption provision of ERISA emphasized its broad scope. *See* *Metropolitan Life Insurance Co. v. Commonwealth of Massachusetts*, 471 U.S. 724, 789, 105 S.Ct. 2380, 85 L.Ed.2d 728 (1985) (ERISA would "displace all state laws that fall within its sphere, even including state laws that are consistent with ERISA's substantive requirements.") The broad sweep of preemption decisions by the U.S. Supreme Court reached their apex with *Pilot Life Insurance Co. v. Dedeaux*, 481 U.S. 41, 107 S.Ct. 1549, 95 L.Ed.2d 39 (1987). The Court there held that "The deliberate care with which ERISA's civil enforcement remedies were drafted and the balancing of policies embodied in its choice of remedies argue strongly for the conclusion that ERISA's civil enforcement remedies were intended to be exclusive." 481 U.S. 41, 54.

1/ The *Carter* case was decided under the Miller Act, 40 U.S.C. § 270a. The Miller Act provides the equivalent of mechanic liens, on federal jobs, "a claim under the bond in lieu of the lien upon land and buildings customary where property is owned by private persons." *Illinois Surety Co. v. John Davis Co.*, 244 U.S. 376, 380, 37 S.Ct. 614, 61 L.Ed. 1206 (1917).

2/ The provision which is now Civil Code § 3111 was originally added as subsection (d) to Code Civ. P. § 1182. What are now §§ 3110 and 3111 were placed in their current sections as part of an reorganization of the mechanic lien statutes in 1969, which did not change their substance. 1969 Cal. Stat. 2761, ch. 1362, § 2.

Against this backdrop of decisions, the California Supreme Court faced the question of whether ERISA preempted California's mechanic lien statute in Carpenters Southern California Administrative Corp. v. El Capitan Development Co., 53 Cal.3d 1041, 282 Cal.Rptr. 277, 811 P.2d 296, *cert. denied*, 502 U.S. 963 (1991) (*El Capitan*) In a split decision, the El Capitan majority relied on the Supreme Court cases which "interpreted broadly the statutory term 'relate to'." 53 Cal.3d at 1048. The majority took this term literally, noting that "All that is necessary to invoke ERISA's statutory preemption provision is that the state law in question 'relate to' an ERISA plan." Id. at 1047. The majority held that Civil Code § 3111, as then written, was preempted by ERISA.

This prevented workers from having their fringe benefits collected through the remedies of mechanic liens, stop notices, and payment bonds. The importance of these remedies in the construction industry cannot be overstated. Fringe benefits, which now form a large part of a laborers total compensation package, were left out from the protection of the statute. *See Lien On* at 278-82.

Subsequent to the *El Capitan* decision, the U.S. Supreme Court changed its analysis of ERISA preemption. The turning point was New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Insurance Co., 514 U.S. 645, 654, 115 S.Ct. 1671, 131 L.Ed. 2d 695 (1995) (*Travelers*). The Court held that "We simply must go beyond the unhelpful text and the frustrating difficulties of defining its key term, and look instead to the objectives of the ERISA statute as a guide to the scope of the state law that Congress understood would survive." 514 U.S. 645, 656. The Court in Travelers also stated the rule, conspicuously absent from its prior holdings on ERISA preemption, that the analysis must begin with "the starting presumption that Congress does not intend to supplant state law." Id. at 654.

In California Division of Labor Standards v. Dillingham Const., 519 U.S. 316, 117 S.Ct. 832 (1997), the Court went farther, and held that a law has a "reference" to a plan, only "Where a State's law acts immediately and exclusively upon ERISA plans, . . . or where the existence of an ERISA plan is essential to the law's operation." 519 U.S. 316, 325.

Another important Supreme Court decision was Mackey v. Lanier Collections Agency & Service, Inc., 486 U.S. 825, 108 S.Ct. 2182, 100 L.Ed.2d 836 (1988). The Court there held that since "ERISA does not provide an enforcement mechanism for collecting judgments. . . . Consequently state law methods for collecting money judgments must, as a general matter, remain undisturbed by ERISA, ..." 486 U.S. 825, 834. The key to preemption was whether the law "singles out ERISA employee welfare benefit plans for different treatment under state garnishment procedures." 486 U.S. 825, 830.

It was these newer U.S. Supreme Court decisions which provided hope that the California statute could be redrafted to avoid ERISA preemption. The 1999 legislation was drafted in light of *Travelers*, *Dillingham* and *Mackey*, to avoid preemption. The California Legislature stated its purpose in the 1999 amendments in the chaptered statute itself:

> "The Legislature finds and declares that the purpose of this act is to restore the protection created by the mechanic's lien law adopted at the first legislative session of this state, refined and expanded over a century and a half, for the just pay due to workers on construction jobs, without discrimination as to the manner in which the pay is allocated, whether union or nonunion, in cash or a combination of cash and benefits. The intent of the Legislature in enacting this act is to clarify that the protections offered in this title are meant to cover the entire compensation package of employees, and not to single out or treat differently any particular form of compensation." Stats 1999, ch. 795 § 9.

The changes were "not intended to alter the substantive law governing mechanic liens" but to "reinstate the ability of laborers and employee trust funds to use state mechanic liens . . . to obtain payment of unpaid wages and fringe benefits." Senate Rules Committee, Analysis of SB 914 (4/28/99).

The bill added a new subsection (b) to Civil Code § 3089, defining a "laborer" to include assignees of all or part of a claim of a laborer, such as employee benefit plans. Stats 1999, ch. 795 § 4. This recognized the holdings in *Carter* and *Bernard*, *supra*, that employee benefit plans are equitable assignees of the portion of an employee's compensation paid in the form of benefits. A non-ERISA assignee may also take advantage of this section, to the same extent that they would have "standing under applicable law to maintain a direct legal action, in their own name or as an assignee, to collect any portion of compensation owed for a laborer, ..." Thus, as in *Dillingham*, the current mechanic lien law "functions irrespective of the existence of an ERISA plan." 519 U.S. 316, 328. Since Civil Code § 3110 refers back to the definition of a "laborer" in § 3089, it effectively includes employee benefit plans and the other "assignees" referred to in the new Civil Code § 3089(b).

Civil Code § 3111 was amended to be more expansive and general. Stats 1999, ch. 795 § 7. It now refers back to Labor Code § 1773.1, the portion of the prevailing wage law defining the total employee compensation required. This eliminated any distinctions between the type of benefits included in compensation, whether through ERISA plans or non-ERISA arrangements, and whether required by a collective bargaining agreement, or a non-union employment agreement. It thus has "no effect on any ERISA plans, but simply take them into account" in defining the employee compensation entitled to statutory protection. *WSB Electric v. Curry*, 88 F.3d 788, 793 (9th Cir. 1996) (Labor Code § 1773.1 and other provisions of prevailing wage law

are not preempted).

The key to the 1999 amendments was to make sure that the law does not "single out ERISA employee welfare plans for different treatment" from similarly situated parties. *Mackey*, 486 U.S. 825, 830. Instead, it protects "the just pay due to workers on construction jobs, without discrimination as to the manner in which the pay is allocated, whether union or nonunion, in cash or a combination of cash and benefits." Stats 1999 ch. 795 § 9. Similarly, the revisions to the law under consideration here, should not "single out" ERISA plans for any different treatment, but instead preserve the original intent to protect all compensation due laborers.

At about the same time that the 1999 legislation was being considered, the theory behind it was validated by a Ninth Circuit decision, holding that the stop notice and payment bond remedies of California law were not preempted. *Southern California IBEW-NECA Trust Funds v. Standard Industrial Electric*, 247 F.3d 920 (9th Cir. 2001). Recognizing that "[t]he previously expansive preemption language prior to *Travelers* has been tailored to better fit Congress' policy intentions" the Ninth Circuit held that the California stop notice and bond remedies were not preempted by ERISA. 247 F.3d at 929 (citations omitted). In doing so, it expressly overruled its own decision in *Sturgis v. Herman Miller, Inc.*, 943 F.2d 1127 (9th Cir. 1991), which had held, as *El Capitan*, that the California mechanic lien law was preempted. Id. A copy of that decision is included here.

The 1999 legislation itself was vindicated, when the California Supreme Court held that the new Civil Code § 3110 was not preempted by ERISA. *Betancourt v. Storke Housing Investors*, 31 Cal.4th 1157, 82 P.3d 286, 8 Cal.Rptr.3d 259 (2003). The *Betancourt* decision relied heavily on the 1999 amendments, to distinguish its prior decision in *El Capitan*. The Court chose to distinguish, rather than overule, the *El Capitan* decision. It also distinguished Section 3111 from Section 3110, declining to rule on whether Section 3111 was still preempted.

> "Unlike section 3111, which we discuss further below, section 3110 is a mechanic's lien law of general application and does not itself refer to ERISA plans. . . . As noted, though the Court of Appeal did not address this, in 1999 the Legislature amended the definition of 'laborer,' which is referenced in section 3110, to include an express trust fund. (§ 3089, subd. (b).) The amendment to section 3089, however, is 'intended to give effect to the long- standing public policy of this state to protect the entire compensation of laborers on works of improvements, regardless of the form in which that compensation is to be paid.' (§ 3089, subd. (b).) We conclude that section 3110 is not 'specifically designed to affect employee benefit plans.' (*Mackey v. Lanier Collection Agency & Serv.* (1988) 486 U.S. 825, 829, 108 S.Ct. 2182, 100 L.Ed.2d 836 (*Mackey*).) Section 3110 does not 'act[ ] immediately and *exclusively* upon ERISA plans,' or is 'the

> existence of ERISA plans ...essential to the law's operation.' (*Dillingham, supra*, 519 U.S. at p. 325, 117 S.Ct. 832, *italics added*; *Southern Calif. IBEW-NECA Trust v. Standard Indus.* (9th Cir.2001) 247 F.3d 920, 926 (*Standard Industrial*) [payment bond statute "not necessarily limited to ERISA plans"; no impermissible reference].)"

Betancourt v. Storke Housing Investors, 31 Cal.4th 1157, 1166-6782 P.3d 286, 8 Cal.Rptr.3d 259 (2003). This decision, which is attached here, should be carefully read. Any new legislation must meet the same test to avoid ERISA preemption.

We note that, after the 1999 amendments, Civil Code § 3111 is actually redundant. Since benefit funds are included within the definition of "laborer" in Section 3089, and thus included among those who can claim a lien under Section 3110, there is no need for a separate section just for benefit funds. In fact, because Section 3111 arguably "singles out" benefit plans, it should be eliminated as a separate section to avoid further ERISA preemption arguments.

Our proposed changes to the Tentative Recommendation reflects the above concerns. Any provision which "singles out" ERISA funds or "laborer compensation funds" for different treatment should be eliminated, as we tried to do in the 1999 legislation. The compensation to laborers in the form of fringe benefits should continue to be protected in the same manner, with the same procedures, as cash wage compensation.

THE PARITY OF PROVISIONS ON PUBLIC AND PRIVATE WORKS

The stop notice and bond remedies available on public works derive from the mechanic lien remedy on private works. *See generally, Lien On*, at 256-59. The stop notice on public works derives from the same procedure on private works, based in turn on the mechanic lien. Former Code Civ. P. § 1184, 1885 Cal.Stat. 144, ch. 152 §2; *see also*, *Bates v. County of Santa Barbara*, 90 Cal.543, 546-47 (1891) (describing the procedure). The purpose of such a stop notice "is analogous to that underlying the entire scheme of mechanics liens, ..." *Clark v. Beyrle*, 160 Cal. 306, 311, 116 P. 739 (1911).

The payment bond remedy was developed in response to court decisions holding that a lien could not be placed upon public property.[3/] Bond Act of 1897, Stats 1897 p. 201. The intent of the Bond Act was to maintain the same protection on public works as on private works. *See Globe Indemnity Co. v. Hanify*, 217 Cal. 721, 730, 20 P.2d 689 (1933); *French v. Powell*, 135 Cal. 636, 639, 68 P. 92 (1902) .

Both the stop notice and payment bond statutes have been considered part of the fulfillment of the constitutional mandate to the Legislature to provide mechanic lien procedures. *See Clark v. Beyrle*, *supra*; *Goldtree v. City of San Diego*, 8 Cal.App. 505, 508-10 (1908) (stop notice in then Code Civ. P. § 1184 was fulfillment of constitutional mandate for "speedy and efficient enforcement of such liens"); *French v. Powell*, *supra* (intent of Bond Act was to fill gap left by removing public property from mechanic liens). They have therefore always been interpreted together.

Currently, the provisions for remedies on private and public works are contained in the same Title of the Civil Code, and contain a common set of definitions. For example, the current provision describing who may assert a claim on a payment bond on public works, Civil Code § 3248, refers back to the provision describing who may assert a stop notice, Civil Code § 3181, which in turn refers back to the provision describing who may assert a mechanic lien in § 3110, which in turns refers to a "laborer," which is defined in § 3089. They are all part of the same "integrated statutory scheme." As the Ninth Circuit put it:

> "The mechanic's lien sections, Cal. Civil Code §§ 3110 and 3111 are also part of California's integrated statutory scheme. Section 3111, which allows employee benefit trusts to avail themselves of the mechanic's lien, is by incorporation also the section which allows them to avail themselves of the stop notice and payment bond remedies" *Southern California IBEW-NECA Trust Funds v. Standard Industrial Electric*, 247 F.3d 920, 928 n. 13 (9th Cir. 2001).

3/ *Mayrhofer v. Board of Education of the City of San Diego*, 89 Cal. 110, 26 P. 646 (1891).

We do not question the decision to put the provisions regarding public works remedies into the Public Contracts Code. However, the same parity of definitions and interpretations should be maintained, since both public and private remedies are based on the same constitutional mandate.

Two problems are created by the separation of public from private works remedies in the Tentative Recommendation. First, some provisions, previously common to both, are now stated differently between the Civil and Public Contracts Code (or may be interpreted differently in the future). Second, some provisions, previously common to both, have been omitted from the Public Contracts Code.

To address these problems, we suggest a thorough review of all provisions previously common to both, to make sure they are carried over into the new Public Contract Code with the same meaning. We address here only certain provisions important to the Laborers Trust Funds.

In addition to the specific proposals we present here, we also suggest that language be included in the Comment section, to make sure the public and private remedies are interpreted the same in the future, even if they have been separated. We suggest a Comment to this effect, such as:

> *By separating the provisions for remedies under public works into a different Code from the provisions for remedies under private works, it is not the intent of this legislation that they be interpreted differently. Rather, the intent of this legislation is to continue current law, in which the provisions for remedies under public works are interpreted identically with the corresponding provisions for private works, to the greatest extent possible. Both arise from the same mandate, under the California Constitution, Art. XIV § 3, to provide such remedies for unpaid laborers and material suppliers. See, e.g., N.V. Heathorn, Inc. v. County of San Mateo, 126 Cal.App.4th 1526, 1534-35, 25 Cal.Rptr.3d 400, (1st. Dist. 2005) ("lien rights of those who provide labor and materials is protected through constitutional mandate in both the public and private spheres."); Southern California IBEW-NECA Trust Funds v. Standard Industrial Electric, 247 F.3d 920, 928-29 (9th Cir. 2001) (remedies for public and private works part of the same "integrated statutory scheme" to be interpreted the same).*

ANALYSIS OF PROPOSED CHANGES

1. Private Works - Civil Code

Definitions - Sections 7014, 7018 and 7020

First of all, the term "laborers compensation fund" is confusing. It sounds too much like "workers compensation fund." We suggest the more accurate term, "laborers benefit fund." Changes are made throughout the legislation accordingly, and we will use that term hereafter in these comments.

In the Tentative Recommendation, there are separate definitions for "express trust fund" and "laborers benefit fund." The term "express trust fund" is actually part of the definition of a "laborers benefit fund." A laborers benefit fund may, but does not have to be, an express trust fund. For example, "vacation pay" is often deducted from employee paychecks and sent to a separate account. This may be an express trust fund, but may simply be a separate savings account in the employee's name. We therefore suggest deleting the separate definition of "express trust fund" and instead incorporating those terms into the definition of a "laborers benefit fund" in § 7020. The important provision, enacted in the 1999 legislation, is the reference and incorporation of "employer payments" under prevailing wage law, Labor Code § 1773.1.

For the definition of "laborer" in § 7018, we suggest maintaining, as much as possible, the current language in Civil Code § 3089, including subsection (b), which was added in the 1999 legislation. Including laborers benefit funds, or express trust funds, to whom a portion of a laborers compensation was assigned, within the definition of a "laborer" was at the heart of the 1999 legislation. This was the basic reason the California Supreme Court found that the law, as amended, was not preempted by ERISA:

> "[I]n 1999 the Legislature amended the definition of 'laborer,' which is referenced in section 3110, to include an express trust fund. (§ 3089, subd. (b).) The amendment to section 3089, however, is 'intended to give effect to the long-standing public policy of this state to protect the entire compensation of laborers on works of improvements, regardless of the form in which that compensation is to be paid.' (§ 3089, subd. (b).) We conclude that section 3110 is not 'specifically designed to affect employee benefit plans.' . . . Section 3110 does not 'act[ ] immediately and *exclusively* upon ERISA plans,' or is 'the existence of ERISA plans ...essential to the law's operation.'"

Betancourt, 31 Cal.4th 1157, 1167 (citations omitted).

Therefore, it is essential that the definition of "laborer" continue to include "laborers benefit funds." Otherwise, the statute may again be vulnerable to a claim of ERISA preemption.

Article 3 - Laborers Compensation Fund - Sections 7070 and 7072

This Article should be eliminated entirely. By setting aside laborers benefit funds into their own article, with provisions specific to them, these provisions are vulnerable to an attack as preempted by ERISA. In upholding the 1999 legislation, the California Supreme Court noted that its prior decision "holding that [former] section 3111 was preempted relied heavily on the fact that the section is 'designed to affect [ERISA plans] specifically.'" *Betancourt*, 31 Cal.4th 1157, 1161, *quoting El Capitan, supra*, 53 Cal.3d at p. 1049.

There should be no provisions or remedies specific to laborer benefit funds or ERISA funds. Rather, they should be included, and treated the same, as other assignees of a portion of a laborers compensation. That was the main thrust of the 1999 legislation, which should not be undone here.

Note that most of the substantive provisions in this article appear elsewhere in our proposed changes. Section 7070 is put back in the definition of a "laborer" in proposed § 7018, as it is currently in Civil Code § 3089. Section 7072 is incorporated into the notice provisions of the following Article, as it is now in Civil Code § 3097.

Article 4 - Notice - Section 7103

Section 7103 of the Tentative Recommendations tends to "single out" laborers benefit funds for special treatment. A similar provision unique to benefit funds, former Civil Code § 3111.5, was eliminated entirely as part of the 1999 legislation. Stats 1999, Ch. 795, § 8.

Instead, our proposal is to make it clear that the notice required is for *any* failure to pay laborers their full compensation. This may include the benefit payments to a laborers benefit fund, the wages due directly to the laborer, or both. Again, the type of payments included is derived from prevailing wage law, Labor Code § 1773.1.

The substance of the items to be included in the notice has been changed in the Tentative Recommendations. The purpose of this notice is to give the laborers (and their representatives) the information necessary to pursue a mechanic lien claim, and also to alert the construction lender (if any) to the possibility of such a claim. We therefore propose restoring the list of information from Civil Code § 3097(k), to meet this purpose.

Preliminary Notice - Disciplinary Action - Section 7216

The proposed Section 7216 of the Tentative Recommendations again "singles out" laborers benefit funds, by providing a remedy only as to them. This is changed in our proposal to include *any* failure to pay the full compensation due a laborer, which may include contributions to a laborers benefit fund. As we now propose, disciplinary action may be brought against a contractor who fails to give the notice required when its laborers are not paid in full, and that failure results in a claim which is not paid.

Who Is Entitled to Lien - Sections 7400 and 7402

Proposed § 7402 of the Tentative Recommendations should be deleted. Again, this provision would be specific to laborers benefit funds, and thus vulnerable to attack on the basis it is preempted by ERISA for "singling out" ERISA funds for special treatment.

Instead, the substance of this provision should be incorporated into the proposed § 7400. This provision, from current Civil Code § 3089(b), incorporates the principal that assignees can stand in the shoes of their assignor to assert a lien, to the same extent they would under applicable law. As with the 1999 legislation, this incorporates the holdings of U.S. v. Carter, 353 U.S. 210 (1957) and Bernard v. Indemnity Insurance Co., 162 Cal. App. 2d 479 (1958) that benefit plans are effectively assignees of a portion of the compensation due the laborers, and have standing as such. So laborers benefit funds should have standing to assert mechanic liens, just as assignees of other mechanic lien claims. "The general rule is that an assignment of a debt carries with it the security." U.S., for the Use of Fidelity National Bank of Spokane, v. Rundle, 100 F. 400, 403 (9th Cir. 1900) (assignee has standing to assert claim against Heard Act bond). "[A]n assignment which is sufficient to transfer the debt must carry with it the mortgage or other lien." Union Supply Co. v. Morris, 220 Cal. 331, 339, 30 P.2d 394 (1934) (supplier who received assignment of claims from other suppliers and subcontractors had standing to file lien for combined claims).[4/]

4/ Arguably, there was a split in authority on this issue. *Compare* Union Supply Co., *supra, with* Mills v. LaVerne Land Co., 97 Cal. 254, 32 P. 169 (1893) (right to record a mechanic lien, as opposed to the lien itself, may not be assigned). *See also* Koudmani v. Ogle Enterprises, Inc., 47 Cal.App.4th 1650, 1659, 55 Cal.Rptr.2d 330 (1996) (lien/bond rights may be assigned); Dept. Ind. Rel. v. Fidelity Roof Co., 60 Cal.App.4th 411, 426-27, 70 Cal.Rptr.2d 465 (1997) (statutory assignment to Labor Commissioner allowed it to bring stop notice and bond claims); Bernard v. Indemnity Ins. Co., 162 Cal.App.2d 479, 487, 329 P.2d 57 (1958) (assignment of payment bond claim on public works). To the extent there was any split, the 1999 amendments resolved it by clearly stating that any valid assignee had standing to enforce the lien. Again, labor benefit funds should not be singled out in this regard, but this principle of standing should be the same for all claimants.

The change to § 7402 we propose thus gives standing to assert a lien to all assignees of the listed persons, to the same extent they would have standing under "applicable" law. This includes, but is not limited to, laborers benefit funds. This is consistent with the current state of the law, and thereby does not "single out" laborers benefit funds for any special treatment.

Personal Liability - Section 7474

Proposed § 7474 continues the intent of current Civil Code § 3152. The fact that these lien rights are expressly stated not to have an effect on the direct claims against a delinquent contractor is critical in protecting the law from a preemption claim. This makes it clear that the mechanic lien law does not interfere with any other legal rights, including federal legal rights such as those arising under ERISA. We note that the current § 3152 refers to the entire "title" which includes the provisions for stop notices and payment bonds on public works. However, this provision was not carried over to the Public Contracts Code sections in the Tentative Recommendations, as discussed below.

We suggest adding language to the end of this section to deal with the common situation where a contractor becomes delinquent on all of its jobs. When a judgment is entered in a "personal action" which includes the delinquency for several jobs, and a partial collection of that judgment is made, which job is the money collected to be applied to? The property owner on each mechanic lien claim would of course like all the money to be applied to the claim on their property. However, the equitable solution (and common practice) is to pro-rate the collection among the jobs, in the proportion they bear to the total judgment. For example, if there is a single judgment for $10,000 in a "personal action" against a delinquent contractor, and five pending mechanic lien claims for $2,000 each, then a collection of $1,000 would be credited $200 to each mechanic lien claim.

2. Public Works - Public Contracts Code

To the extent that the Tentative Recommendations as to public works follows the provisions regarding private works, we have the same concern that it be kept safe from ERISA preemption, as discussed above. To the extent that the Tentative Recommendation as to public works omits provisions applicable to private works, we are concerned that the parity of public/private provisions is disturbed. There are several provisions which currently apply to both private and public work remedies, but which were not carried over into the Government Code provisions of the Tentative Recommendations.

Definitions - Sections 41050, (new) 41075 and 41080

Under current law, the definitions in Civil Code §§ 3082-3098 apply to both the remedies for private works and the remedies for public works. Since the public works remedies of stop notices and payment bonds were meant to be applied in the same manner as private mechanic liens, to the extent possible, this uniformity of definitions should be preserved. However, by separately stating the definitions for public works remedies in the Public Contracts Code, the Tentative Recommendations changes some of these definitions and omits others. This is a drafting problem which should be addressed across all definitions. We suggest that the Public Contracts Code definitions simply refer back to the Civil Code definitions, wherever possible. Our comments and suggestions are limited to the definitions we are most concerned with - "express trust fund," "laborer" and "laborers compensation fund."

As with the parallel provision proposed for the Civil Code, the separate definition of "express trust fund" in Public Contracts Code § 41050 should be eliminated. See the discussion under Civil Code § 7014 *supra*.

The Tentative Recommendations totally omit any definition of "laborer" in the Public Contracts Code. This could effect a substantive change in the law, by changing the description of who can assert a stop notice or payment bond claim on public works. We suggest then, adding a definition of "laborer" in new § 41075, which refers back to the definition of "laborer" in Civil Code § 7018. See our changes and discussion of the definition of laborer in Civil Code § 7018. Alternatively, the definition of "laborer" could be repeated verbatim, from our proposed Civil Code § 7018.

As discussed above, the term "laborers compensation fund" is confusing, and we suggest the term "laborers benefit fund." As with the definition of "laborer" we suggest that the definition of "laborers benefit fund" simply refer back to the same definition in Civil Code § 7020. See our changes and discussion of the definition of "laborers benefit fund" in Civil Code § 7020. Alternatively, the definition of "laborers benefit fund" could be repeated verbatim, from our proposed Civil Code § 7020.

Who May Use Remedies - Section 42030

As discussed above, the definition of who may assert stop notice and payment bond claims should match the definition of those who may assert a mechanic lien, as under current law. The only difference in the description of who may assert such a claim should be whether they provide the labor or materials to private or public works.

Accordingly, we propose redrafting § 42030 to match Civil Code § 7400 as much as possible. The corresponding provision under current law, Civil Code § 3181, simply refers back to the mechanic lien definitions, adding only that the labor or material be on a public works. We therefore suggest copying proposed Civil Code § 7400, as much as possible, into the proposed Public Contracts Code § 42030. See our comments and proposed Civil Code § 7400 as to the changes we suggest in that section.

Miscellaneous - Sections 42040, 42080 and (new) 42110

Most important here, we have added a new proposed § 42110. This is based on current Civil Code § 3152. That current section provides that " Nothing contained *in this title* affects the right of a claimant to maintain a personal action to recover a debt against the person liable therefor either in a separate action or in the action to foreclose the lien, nor any right the claimant may have to the issuance of a writ of attachment or execution or to enforce a judgment by other means." (*Emphasis added.*) It then goes on to describe how enforcement of the separate "personal action" is to be coordinated with these claims. Note that the section refers to "this title" which includes the remedies of stop notice and bond claims on public works, as well as those on private works. In the Tentative Recommendations, this section is carried over into proposed Civil Code § 7474, affecting only private works. However, no provision was proposed to carry over these provisions into the proposed Public Contracts Code revisions. This is a significant omission. Without it, stop notice and bond claims could be held to affect direct actions against the delinquent contractor, contrary to current law. We therefore propose importing the language from proposed Civil Code § 7474 (in turn derived from § 3152) into a new Public Contracts Code § 42110. See also our comments on proposed Civil Code § 7474.

The Tentative Recommendations propose a new § 42040, dealing with jurisdiction and venue. While the proposal correctly states current law, we suggest adding language to deal with the situation where one of these claims may be joined with federal claims in federal court. This is common for claims brought by the Laborers Funds, since their direct cause of action against a delinquent contractor arises under federal law, 29 U.S.C. §§ 185(a) and 1145, and may be joined with state claims such as these, under the supplemental jurisdiction of federal courts. 28 U.S.C. § 1367(a). However, existing Civil Code § 3214 (Pub. Cont. Code § 4440 in the Tentative Recommendations) allows a public entity to implead all actions for stop notices on a single project, into the first-filed action. We propose language to allow these claims brought in federal court to be implead into the first-filed state action (even if the federal action was filed first) as a condition of allowing federal jurisdiction over the public entity. It is our position that the federal courts have jurisdiction over stop notice claim against public entities already, but this proposed languages clarifies the procedure to be followed to allow all the claims to be dealt with together.

The Tentative Recommendations also propose a new § 42080, specifying how notice is to be given. The proposal requires a return receipt to prove mailing. It is our experience, however, that contractors who are delinquent in their obligations for labor and materials, will often refuse to accept certified mail, or are not even at their listed address, because they have shut their doors for lack of funds. This should not frustrate notice to remedy the very delinquency of these contractors. Therefore, we propose adding a provision which allows notice to be proven by sending it (in the manner already specified) to the current address listed with the Contractors State License Board. *See* Bus. & Prof. Code §§ 7083 (contractors required to notify Board of change of address) and 7080.5 (Board required to publicly post current address of all contractors).

Preliminary Notice - Sections 43010, 43030 and 43060

Public Contracts Code § 43060 in the Tentative Recommendations has two problems. First, it is directed specifically to "compensation due a laborers compensation fund." This singles out such funds for special treatment and thus opens the statute to attack as preempted by ERISA This should apply instead to *any* compensation due a laborer, *including, but not limited to*, that payable to a laborers benefit fund. We have proposed language to that effect, and also conformed the reference from "laborers compensation fund" to laborers benefit fund" as discussed above.

The second problem with proposed § 43060, is that it refers to certain preliminary notice to be given, without carrying over the provisions requiring the information to be noticed. The proposed § 43060 is drawn from current Civil Code § 3097(h). That subsection refers to the failure to provide certain information where laborers are unpaid, specified in Civil Code § 3097(c)(6).[5/] The point of this notice is to alert the construction lender (or on a public works, the public entity) to the possibility of a claim. The point of the disciplinary action is to provide a remedy where a mechanic lien (or on a public works, a stop notice or bond claim) results from the failure to give such notice. If the provision for disciplinary notice is to be incorporated into public works remedies, the corresponding information should also be incorporated.

We therefore propose modifying proposed Public Contracts Code § 43030 to match the notice required on private works, under proposed Civil Code § 7204(b). This language, in new subsection (5), is based on Civil Code §§ 3097(c)(6). The language of § 43060(b) is modified to refer to the information in § 43030(5). With these modifications, a contractor will be required to

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5/ "*(6) If the notice is given by a subcontractor who has failed to pay all compensation due to his or her laborers on the job, the notice shall also contain the identity and address of any laborer and any express trust fund to whom employer payments are due. If an invoice for materials or certified payroll contains the information required by this section, a copy of the invoice, transmitted in the manner prescribed by this section shall be sufficient notice.*" Civil Code § 3097(c)(6)

provide the information, as under current law, and will be subject to discipline if a stop notice or bond claim results from its failure to do so.

We have also proposed a change to § 43030(4), to specify the "public works contract" rather than the "site" of improvement. This reflects how public entities actually identify the project internally. We have also proposed conforming language to refer to "laborers benefit funds" rather than "laborers compensation funds" as discussed above.

3. Conforming Provisions

We propose that language in the Business & Professions Code §§ 7071.5 and 7071.10 be conformed to refer to "laborers benefit fund" in proposed Civil Code § 7020 rather than an "express trust fund" in the section we ask be deleted. We note that these provisions in the Business & Professions Code were also modified as part of the 1999 legislation, for the same purpose. Chapter 795, Stats 1999, §§ 1 and 2. See the discussion of Civil Code §§ 7014, 7018 and 7020, above.

CONCLUSION

The Laborers Trust Funds ask that the above comments and enclosed Proposed Changes be carefully considered. This is a complicated area of the law, which requires careful study and simplification. Above all, the final result must remain true to the constitutional mandate to the Legislature that "***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.***" Cal. Const., Art. XIV, § 3.

Proposed Changes to Mechanic Lien Code Revisions

Deletions are in ~~strikeout type~~. Additions are in **bold type**. Comments are in *italic* enclosed by [*brackets*], meant for the Commission only, not to be included in the official comments.

Civil Code Part 6 - Private Works of Improvement

Chapter 1, Art. 1

~~§ 7014. Express trust fund~~

~~7014. "Express trust fund" means a laborers compensation fund to which a portion of a laborer's total compensation is to be paid pursuant to an employment agreement or a collective bargaining agreement for the provision of benefits, including, but not limited to, employer payments described in Section 1773.1 of the Labor Code and implementing regulations~~.

[*To be incorporated instead in the definition of "laborers benefit fund."*]

§ 7018. Laborer

7018. "Laborer" means a person who, acting as an employee, performs labor on, or bestows skill or other necessary services on, a work of improvement. **"Laborer" also includes any person or entity, including a "laborers benefit fund" described in Section 7020, to whom a portion of the compensation of a laborer is paid by agreement with that laborer or the collective bargaining agent of that laborer. To the extent that a person or entity defined here has standing under applicable law to maintain a direct legal action, in their own name or as an assignee, to collect any portion of compensation owed for a laborer, that person or entity shall have standing to enforce any rights under this Part to the same extent as the laborer. This section is intended to give effect to the long-standing public policy of this state to protect the entire compensation of laborers on works of improvement, regardless of the form in which that compensation is to be paid.**

[*Language from Civil Code § 3089(b) put back in.*]

§ 7020. Laborers ~~compensation~~ **benefit** fund

7020. "Laborers ~~compensation~~ **benefit** fund" means a person, including an express trust fund, ~~to which a portion of the compensation of a laborer is paid by agreement with the laborer or the collective bargaining agent of the laborer~~ **to which a portion of a laborer's total compensation is to be paid pursuant to an employment agreement or a collective bargaining agreement for the provision of benefits, including, but not limited to, employer payments described in Section 1773.1 of the Labor Code and implementing regulations.**

~~Art. 3 - Laborers Compensation Fund~~

[*Delete as a separate article.*]

~~§ 7070. Standing to enforce laborer's rights~~

~~7070. (a) A laborers compensation fund that has standing under applicable law to maintain a direct legal action in its own name or as an assignee to collect any portion of compensation owed for a laborer, has standing to enforce rights under this part to the same extent as the laborer.~~
~~(b) This section is intended to give effect to the long-standing public policy of the state to protect the entire compensation of a laborer on a work of improvement, regardless of the form in which the compensation is to be paid.~~

[*Delete. Should be part of definition of laborer.*]

~~§ 7072. Notice of overdue laborer compensation~~

~~7072. (a) A contractor or subcontractor that employs a laborer and fails to pay the full compensation due the laborer or laborers compensation fund shall, not later than the date the compensation became delinquent, give the laborer, the laborer's bargaining representative, if any, and the construction lender or reputed construction lender, if any, notice that includes all of the following information:~~
~~(1) The name and address of any express trust fund to which employer payments are due.~~
~~(2) The total number of straight time and overtime hours on each job.~~
~~(3) The amount then past due and owing.~~
~~(b) Failure to give the notice required by subdivision (a) constitutes grounds for disciplinary action under the Contractors' State License Law, Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code.~~

[*Delete in this Article. Move, with revisions, to Art. 4 - Notice.*]

Art. 4 Notice

[*Add the following section:*]

§ 7103 Notice of overdue laborer compensation
(a) A contractor or subcontractor that employs a laborer and fails to pay the full compensation due the laborer, **including any employer payments described in Section 1773.1 of the Labor Code and regulations adopted thereunder** ~~or laborers compensation fund~~ shall, not later than the date the compensation became delinquent, give the laborer, the laborer's bargaining representative, if any, and the construction lender or reputed construction lender, if any, notice that includes all of the following information:

~~(1) The name and address of any express trust fund to which employer payments are due.~~
~~(2) The total number of straight time and overtime hours on each job.~~
~~(3) The amount then past due and owing~~.

(1) The name of the owner and the contractor.

(2) A description of the jobsite sufficient for identification.

(3) The identity and address of any laborers benefit fund to which employer payments are due.

(4) The total number of straight time and overtime hours on each job.

(5) The amount then past due and owing.

(b) Failure to give the notice required by subdivision (a) constitutes grounds for disciplinary action under the Contractors' State License Law, Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code.

[*Additions and deletions indicated are from the proposed § 7072. Changes are made to conform with the substance of current Civil Code § 3097(k), which the original proposal departed from.*]

Chapter 2

§ 7216. Disciplinary action

7216. A licensed subcontractor is subject to disciplinary action under the Contractors' State License Law, Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code, if all of the following conditions are satisfied:
(a) The subcontractor does not pay all compensation due to **any of its laborers for labor on the work of improvement** ~~a laborers compensation fund~~.
(b) The subcontractor fails to give preliminary notice or include in the notice the information required by subdivision (b) of Section 7204.
(c) The subcontractor's failure results in the **laborer(s) or** laborers ~~compensation~~ **benefit** fund**(s)** recording a claim of lien, filing a stop payment notice, or asserting a claim against a payment bond.
(d) The amount due the **laborer(s) or** laborers ~~compensation~~ **benefit** fund is not paid.

[*Should apply to any failure to pay full compensation due a laborer.]*

Chapter 4 - Art. 1 - Who is Entitled to Lien

§ 7400. Persons entitled to lien

7400. A person **(or their assignee)** that provides labor, service, equipment, or material authorized for a work of improvement, including but not limited the following persons, has a lien right under this chapter:
(a) Direct contractor.
(b) Subcontractor.
(c) Material supplier.

(d) Equipment lessor.
(e) Laborer.
(f) Design professional.
(g) Builder.
(h) An assignee of a persons described in subsections (a) through (h), above, to the extent that such person or entity has standing under applicable law to maintain a direct legal action, in their own name or as an assignee, to collect any portion of the payment for labor, service, equipment, or material.

[*Language from current Civil Code § 3089(b)*].

~~§ 7402. Lien right of express trust fund~~

~~7402. An express trust fund has the same lien right under this chapter as a laborer on a work of improvement, to the extent of the compensation agreed to be paid to the express trust fund for labor on that work of improvement only~~.

[*Delete. Accounted for instead in new § 7400(h).*]

Art. 6 - Enforcement

§ 7474. Personal liability

7474. (a) This chapter does not affect any of the following rights of a claimant:
(1) The right to maintain a personal action to recover a debt against the person liable, either in a separate action or in an action to enforce a lien.
(2) The right to a writ of attachment. In an application for a writ of attachment, the claimant shall refer to this section. The claimant's recording of a claim of lien does not affect the right to a writ of attachment.
(3) The right to enforce a judgment.
(b) A judgment obtained by the claimant in a personal action described in subdivision (a) does not impair or merge the claim of lien, but any amount collected on the judgment shall be credited on the amount of the lien, **pro-rated according to the percentage that the lien is to the total judgment.**

[*Final language designed to deal with common situation where the judgment includes claims on other jobs, or other unrelated claims*].

PUBLIC WORKS

Public Contracts Code Part 6

Chapter 1

[*Delete § 41050*]

~~§ 41050. Express trust fund~~

~~41050. "Express trust fund" means a laborers compensation fund to which a portion of a laborer's total compensation is to be paid pursuant to an employment agreement or a collective bargaining agreement for the provision of benefits, including, but not limited to, employer payments described in Section 1773.1 of the Labor Code and implementing regulations.~~

[*No Definition of Laborer. So add:*]
§ 41075. Laborer

"Laborer" has the same meaning as Civil Code § 7018.

§ 41080. Laborers benefit ~~compensation~~ fund

41080. "Laborers benefit ~~compensation~~ fund" has the same meaning as Civil Code § 7020. ~~means a person, including an express trust fund, to which a portion of the compensation of a laborer is paid by agreement with the laborer or the collective bargaining agent of the laborer~~.

Chapter 2
Article 1

§ 42030. Who may use remedies

42030. (a) Except as provided in subdivision (b), ~~any of the following persons that has not been paid in full~~ **a person (or their assignee) that provides labor, service, equipment, or material authorized for a work of improvement, and has not been paid in full, including but not limited the following persons,** may give a stop payment notice to the public entity or assert a claim against a payment bond:
~~(1) A person that provides labor, service, equipment, or material for a public works contract pursuant to an agreement with a direct contractor.~~
~~(2) An express trust fund, to the extent of the compensation agreed to be paid to the express trust fund for labor on that public works contract only.~~
~~(3) A person described in Section 4107.7.~~
(1) Subcontractor.

(2) Material supplier.
(3) Equipment lessor.
(4) Laborer.
(5) Design professional.
(6) Builder.
(b) A direct contractor may not give a stop payment notice or assert a claim against a payment bond under this part.
(c) An assignee of a persons described in subsection (a), above, to the extent that such person or entity has standing under applicable law to maintain a direct legal action, in their own name or as an assignee, to collect any portion of the payment for labor, service, equipment, or material.

[*This is designed to match the language in proposed Civil Code § 7400, as much as possible.*]

§ 42040. Jurisdiction and venue
42040. The proper court for proceedings under this part is the superior court in the county in which a public works contract, or part of it, is to be performed. **An action may be joined with federal claims brought in a United States District Court for the district in which the public works contract, or part of it, is to be performed, and the State of California consents to such jurisdiction, provided that the claims shall be allowed to be impleaded in a superior court pursuant to § 44440, regardless of whether the state or federal action is commenced first.**

[*See comments on purpose of additional language.*]

§ 42080. Mailed notice
42080. The following provisions apply to notice given by mail under this part:
(a) Notice shall be given by registered or certified mail or by another method of delivery providing for overnight delivery.
(b) Notice is complete when deposited in the mail or with an express service carrier in the manner provided in Section 1013 of the Code of Civil Procedure.
(c) Proof that the notice was given in the manner provided in this section shall be made by (1) a return receipt or a photocopy of the record of delivery and receipt maintained by the United States Postal Service, showing the date of delivery and to whom delivered, or in the event of nondelivery, by the returned envelope itself. (2) proof of mailing certified by the United States Postal Service, or (3) a tracking record or other documentation certified by an express service carrier showing delivery of the notice.
(d) In the case of a direct contractor or subcontractor, notice is sufficient when sent, in the manner described in subsection (a), to the most current address listed with the Contractors State License Board; proof of delivery shall not be required, only proof of mailing.

[*See Bus. & Prof. Code §§ 7083 (contractor required to notify Board of address change) and 7080.5 (Board required to publicly post current addresses of contractors).*]

[*Add the following section:*]

§ 42110 Remedies Not Exclusive
(a) This Part does not affect any of the following rights of a claimant:
(1) The right to maintain a personal action to recover a debt against the person liable, either in a separate action or combined with an action under this Part.
(2) The right to a writ of attachment. In an application for a writ of attachment, the claimant shall refer to this section. The claimant's assertion of any remedies under this Part does not affect the right to a writ of attachment.
(3) The right to enforce a judgment.
(b) A judgment obtained by the claimant in a personal action described in subdivision (a) does not impair or merge any claim under this Part, but any amount collected on the judgment shall be credited on the amount of a claim under this Part, pro-rated according to the percentage that the claim under this Part is to the total judgment.

[*Based on Proposed Civil Code § 7474, which is based on current Civil Code § 3152, which applies to stop notice and bond claims as well as lien claims.*]

Chapter 3

§ 43010. Preliminary notice prerequisite to remedies
43010. (a) Except as otherwise provided by statute, preliminary notice is a necessary prerequisite to the validity of a stop payment notice or a claim against a payment bond under this part.
(b) Preliminary notice is not required of a laborer or a laborers **benefit** ~~compensation~~ fund.
(c) Preliminary notice is not required of a claimant that has a direct contractual relationship with the direct contractor.

§ 43030. Contents of preliminary notice
43030. A preliminary notice shall state with substantial accuracy all of the following:
(1) A general description of the labor, service, equipment, or material provided or to be provided.
(2) The name and address of the person providing the labor, service, equipment, or material. (3) The name of the person that contracted for the labor, service, equipment, or material.
(4) A description of the **public works contract** ~~site~~ sufficient for identification.
(5) If preliminary notice is given by a subcontractor that has not paid all compensation due to a laborer or laborers compensation fund, the notice shall include the name and address of the laborer and any laborers compensation fund to which payments are due.

[*The change to subsection (4) reflects the fact that stop notice and payment bond remedies relate to the public work contract, not the site. Subsection (5) is from Proposed Civil Code § 7204(b)*].

§ 43060. Disciplinary action for failure to give notice
43060. A licensed subcontractor is subject to disciplinary action under the Contractors' State License Law, Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code, if all of the following conditions are satisfied:
(a) The subcontractor does not pay all compensation due to **any of its laborers for labor on the**

work of improvement ~~a laborers compensation fund~~.
(b) The subcontractor fails to give a required preliminary notice **or include the information required in § 43030(5)**.
(c) The subcontractor's failure results in the **laborer(s) or** laborers **benefit** ~~compensation~~ fund filing a stop payment notice or asserting a claim against a payment bond.
(d) The amount due the **laborer(s) or** laborers **benefit** ~~compensation~~ fund is not paid.

CONFORMING PROVISIONS

BUSINESS & PROFESSIONS CODE

The following changes are to the existing law, not the Tentative Recommendation.

Bus. & Prof. Code § 7071.5 (amended). Contractor's bond
SEC. ____. Section 7071.5 of the Business and Professions Code is amended to read:

7071.5. The contractor's bond required by this article shall be executed by an admitted surety in favor of the State of California, in a form acceptable to the registrar and filed with the registrar by the licensee or applicant. The contractor's bond shall be for the benefit of the following:
(a) Any homeowner contracting for home improvement upon the homeowner's personal family residence damaged as a result of a violation of this chapter by the licensee.
(b) Any person damaged as a result of a willful and deliberate violation of this chapter by the licensee, or by the fraud of the licensee in the execution or performance of a construction contract.
(c) Any employee of the licensee damaged by the licensee's failure to pay wages.
(d) Any person or entity, including **a laborers benefit fund** ~~an express trust fund~~ described in Section ~~3111~~ **7020** of the Civil Code, to whom a portion of the compensation of an employee of a licensee is paid by agreement with that employee or the collective bargaining agent of that employee, damaged as the result of the licensee's failure to pay fringe benefits for its employees, including, but not limited to, employer payments described in Section 1773.1 of the Labor Code and regulations thereunder (without regard to whether the work was performed on a private or public work). Damage to a laborers benefit fund ~~an express trust fund~~ is limited to actual employer payments required to be made on behalf of employees of the licensee, as part of the overall compensation of those employees, which the licensee fails to pay.

Bus. & Prof. Code § 7071.10 (amended). Qualifying individual's bond
SEC. ____. Section 7071.10 of the Business and Professions Code is amended to read:

7071.10. (a) The qualifying individual's bond required by this article shall be executed by an admitted surety insurer in favor of the State of California, in a form acceptable to the registrar and filed with the registrar by the qualifying individual. The qualifying individual's bond shall be for the benefit of the following persons:
(1) Any homeowner contracting for home improvement upon the homeowner's personal family residence damaged as a result of a violation of this chapter by the licensee.
(2) Any person damaged as a result of a willful and deliberate violation of this chapter by the licensee, or by the fraud of the licensee in the execution or performance of a construction contract.
(3) Any employee of the licensee damaged by the licensee's failure to pay wages.
(4) Any person or entity, including **a laborers benefit fund** ~~an express trust fund~~ described in

Section ~~3111~~ **7020** of the Civil Code, to whom a portion of the compensation of an employee of a licensee is paid by agreement with that employee or the collective bargaining agent of that employee, that is damaged as the result of the licensee's failure to pay fringe benefits for its employees including, but not limited to, employer payments described in Section 1773.1 of the Labor Code and regulations adopted thereunder (without regard to whether the work was performed on a public or private work). Damage to a **laborers benefit fund** ~~an express trust fund~~ is limited to employer payments required to be made on behalf of employees of the licensee, as part of the overall compensation of those employees, which the licensee fails to pay.
(b) The qualifying individual's bond shall not be required in addition to the contractor's bond when the qualifying individual is himself or herself the proprietor under subdivision (a) or a general partner under subdivision (b) of Section 7068.

THE REGENTS OF THE UNIVERSITY OF CALIFORNIA
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September 27, 2006

VIA FEDEX

California Law Review Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Re: Recommendations - Mechanics Lien Law

Dear Commission:

This office, in representing The Regents of the University of California, has handled thousands of stop notice cases involving public works located through the state. We believe that we are uniquely qualified, from the perspective of a public owner, to evaluate the proposed changes to the mechanics lien and stop notices laws.

We commend the excellent work of the Commission. We believe the proposed changes will simply and clarify a complex and confusing area of the law. The Commission's proposed revisions to the stop payment notice provisions of the code are well written and far clearer than the current text.

We offer the following comments to the Commission's tentative recommendations to the mechanics lien law.

1. Public Contract Code § 42030: Who may file a stop payment notice. We suggest rewording subparagraph (a) of this proposed section to clarify that a claimant need not be under contract with the direct contractor to file a stop payment notice. The following revised language is recommended: "A person that provides labor, service, or material for a public works contract relating to an agreement with a direct contractor."

2. Public Contract Code § 42040: Jurisdiction and venue. The proposed wording would appear to allow venue in a location where only a small portion of the work may have been

fabricated. We recommend revising this section to read: "The proper court for proceedings under this part is the superior court in the county in which a public work contract identifies the location of the work."

3. Public Contract Code § 42080: Notification/Overnight Delivery. Overnight delivery is a standard method of mailing notices for litigation and should be incorporated into the mechanics lien law.

Electronic Notice: In proposed Civil Code § 7110, the Commission provides new options for mechanic's lien claimants to give notice via electronic record should a person consent to receive notice in this fashion. We recommend including a similar option for stop notices for the same reasons listed by the Commission for mechanics lien issues: reduced flow of paperwork, reduced time for notice, reduced cost of delivery, enhanced opportunity for monitory. Also, this would allow for a more efficient transfer and internal tracking of paperwork.

Proof of Mailing: As a comment, the University has had a high degree of reliability with the mail delivered by the United States Postal Service.

4. Public Contract Code § 42210 (including acceptance and cessation): Acceptance. There exists some possible confusion between the terms "acceptance" and "completion." The terms are generally interchangeable. We recommend revising proposed Public Contract Code § 42210(a) to read: "the date of actual completion identified in the notice of completion by the public entity."

The Commission states that a public entity may file a notice of completion at substantial completion. University practice, however, is to file a notice of completion upon full completion, not substantial completion. To maintain uniformity, we recommend the phrase "completion occurs upon acceptance" be replaced with "completion occurs upon the date identified by the public entity in the notice of completion." in proposed Civil Code § 7150(b).

Cessation of work: We recommend that Public Contract Code § 42210 be revised to eliminate subsection (b). The Commission has eliminated any provision for a notice of cessation in the public sector. See Civil Code §§ 3086, 3184, and proposed Public Contract Code § 44140. Because it is recorded, a notice of cessation is a convenient method for notifying all parties that work under the public works contract has ceased. Use of a notice of completion in lieu of a notice of cessation, as proposed by the Commission for the private sector, would lead a party to believe the project is complete and accepted as such, although the reverse may be the case. A notice of completion also triggers certain obligations and deadlines for sureties and other parties that may be undesirable where only cessation has occurred.

We also recommend changing the completion term to 60 days from cessation of work, as opposed to 30 days. There is no apparent reason for variance from the 60-day provision in private works. The complexity of today's projects necessitates this extension to the time period. We recommend adding the following section defining cessation:

> § 42211: Cessation: For the purpose of this part, cessation of a public works contract occurs at cessation of labor for a continuous period of 60 days.

5. Public Contract Code § 42221: Notice of Cessation. We recommend adding a provision for a notice of cessation as currently allowed in private works per Civil Code §§ 3086(c) and 3092 and public works in § 3184. We recommend that § 42210 be revised to include "(c) recordation of a Notice of Cessation after cessation of labor for a continuous period of 60 days." This would also alert potential claimants that cessation has occurred. It would also allow for the same time period from recordation of a notice of completion within which a claimant may give notice or commence an action. An additional code section is required to define the notice of cessation. The following wording is suggested:

> § 42221. Notice of Cessation. A public entity may record a notice of cessation. The notice shall include all of the following information: (a) The name and address of the public entity. (b) A description of the site sufficient for identification, including the street address of the site, if any. If a sufficient legal description of the site is given, the effectiveness of the notice is not affected by the fact that the street address is erroneous or is omitted. (c) The name of the direct contractor for the public works contract. (d) The date on which labor ceased, and a statement that cessation of labor has been continuous until recordation of the notice. (e) A statement briefly describing the remaining work.

6. Public Contract Code § 42230: Recordation of notice. We recommend that this section be revised to include notices of cessation. In lieu of "(a) A notice of completion is recorded," we would use the following language: "(a) A notice of completion or cessation is recorded."

7. Public Contract Code § 42340(a): Releases. The University has encountered a significant amount of confusion in regards to releases provided in the form of a revised stop payment notice. These revised notices typically fail to indicate how much should be withheld after a stop notice is partially released. In order to avoid any misunderstandings, we recommend the Commission consider revising this section to include a requirement that any partial release expressly state the amount that should be withheld after receipt of the partial release.

8. Public Contract Code § 44140: Time for giving notice. We recommend that this section be revised to allow for recorded notices of cessation. We would replace the section with the following: "A stop payment notice is not effective unless given within 30 days after recordation of a notice of completion or a notice of cessation, or if a notice of completion or a notice of cessation is not recorded, within 90 days after completion or cessation."

9. Public Contract Code § 44180: Release bond. There appears to be a typo in this section. We recommend insertion of the word "in" in the clause: "or enforceability of the claim stated 'in' a stop payment notice."

We thank the Commission for this opportunity to comment on the proposed revisions. Should further comment or queries be allowed, please contact me directly.

Sincerely,

Holly E. Ackley 1st

Holly E. Ackley
University Counsel

nt

152076.3

COMMENTS OF WILLIAM C. LAST, JR.

From: wclast@lastlawfirm.com
Subject: mechanics lien law
Date: September 29, 2006
To: scohen@clrc.ca.gov

Steve:

You sent me the tentative changes to the mechanic's lien laws. I have reviewed the tentative recommendations for revisions to the mechanic lien statutes. As background, I am attorney who has practiced construction law for over 28 years. I represent owners, designers, general contractors, subcontractors and suppliers. Currently, ninety-five percent of my practice is construction litigation. Approximately sixty percent of my cases concern public works projects. The vast majority of my litigation practice concerns lien laws.

The following are my comments concerning certain portions of the tentative recommendations for revisions to the mechanic lien statutes:

Mailed Notice: I believe that allowing service of the requisite notices by express mail and other private express mail carriers would be an improvement. This brings service of such notices into the 21st century. The existing statutes require service by certified or register mail with return receipt requested. Use of express mail or private express mail allows for a method to track the delivery or rejection of the delivery by the recipient. As a practical matter, it is far easier to use express mail than certified or register mail with return receipt requested. There must be, however, some method for proving service.

Proof of services: I believe that proof of service must be established by a return receipt or some other similar documentary evidence. The mail service is not reliable enough to conclude that by simply putting a notice in the mail the recipient received it. I am also concerned about potential abuses by unscrupulous contractors (and there are plenty of them) who claim they served the document by mail but actually did not. I believe there must be some means to ensure that notice was actually served on the date in question.

Definition of completion for public works: As a construction law practitioner this is a major concern. I am currently representing a subcontractor in a payment bond claim wherein the issue of acceptance vs. cessation. The general contractor went bankrupt before the project was completed. However, subcontractor did stay on and complete its work. After the project was completed and being used by the public owner, but before formal acceptance, defects in the work were discovered. The owner, payment bond surety and subcontractor argued over who was a fault. Months passed before the work was remedied by the owner using a different contractor. The public owner formally accepted the project and shortly thereafter the subcontractor filed a lawsuit against the payment bond surety. The surety now claims that there was a sufficient cessation of

work to trigger the running of the time for filing the lawsuit. We are arguing that the owner used the facility so cessation is not the issue but rather formal acceptance. Based on my current case I am concerned about the following: (1) what constitutes acceptance, must it be a formal acceptance by the governing board of the public entity? I believe that formal acceptance is currently required. (2) How does cessation of work relate to a project that is being used and occupied after the work is completed, but there is remaining punchlist (typically minor remedial/corrective work or completion of minor items) work? (3) How does occupancy and a cessation of work impact a situation where the public body intends to formally accept the project but has yet to do so? I believe that any potential for uncertainty must be removed from statute as well as the revisions. If cessation of work for 30 days possibly constitutes completion then cessation must be defined. Is it when there is a cessation after a project is 50% complete or is when a delay in completing the punchlist work occurs? While I represent general contractors and subcontractors, it difficult for a subcontractor to determine when there is a cessation of work. It is fairly clear when a general contractor defaults, work stops and then the original contractor is replaced by another general, but less so when there is only punchlist work remaining to be completed. At a minimum, the time period should be extended from 30 to 60 days. Ideally, there should be definition cessation for a public works projects.

Attorney's fees: I believe that existing statutory scheme relative to attorney's fees on mechanic's lien actions should remain unchanged. If the right to recover attorney's fees is extended to mechanic's liens, homeowners who are sued by parties who they are not in privity will have a greater burden placed on them by lien laws. Fees should be allowed for public and commercial projects. Attorney's fees are recoverable in payment bond claims. Public works projects are generally larger and they take place in a commercial environment. As a result, there is no greater burden placed on the parties by allowing the award of attorney's fees and costs. I believe, for that reason, fees should be awarded in public works stop notice actions.

Five day notice for stop notice actions: I rarely send the notice. While I believe that I understand the purpose by the statute, I believe eliminating the requirement will not have any impact on the parties who are impacted by the action. Eliminating the requirement will also eliminate the possibility of an appellate court holding that the notice is mandatory.

General comments: As a whole the tentative recommendations clean-up the current statutory scheme. However, if the recommendations are adopted into law individuals and entities impacted by the changes will have to be informed of the changes and given a reasonable period of time to changes their current practices.

If you would like further elaboration on the foregoing comments please do not hesitate to contact me.

Thank you,
Bill Last

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September 29, 2006

Mr. Nathaniel Sterling
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Re: Comments on Tentative Recommendation to Mechanics Lien Law

Dear Mr. Sterling:

The American Insurance Association ("AIA") is a national trade association representing insurance companies writing all lines of property and casualty insurance, including those issuing surety bonds. The National Association of Surety Bond Producers ("NASBP") is an international association of professional surety bond producers and brokers. The Surety & Fidelity Association of America ("SFAA") is a national trade association of companies licensed to write fidelity and surety bonds. Together, these organizations represent the agents that market and the sureties that write the vast majority of surety bonds in the United States and in California.

AIA, NASBP, and SFAA commend the California Law Review Commission on undertaking the complex task of simplifying and modernizing the California mechanics lien law and associated construction remedies. AIA, NASBP, and SFAA have reviewed the tentative recommendation of the California Law Revision Commission relating to these statutes and now submit jointly the following written comments, which are categorized for convenience into general and specific comments. General comments are those comments that should be considered applicable to the treatment of a particular subject or issue throughout the entirety of the tentative recommendation; specific comments are those comments that pertain only to the identified section of the tentative recommendation. The specific comments address the two bond Chapters first and then the bond related provisions of the other Chapters.

General Comments

Admitted Surety. In many instances, the tentative recommendation proposes requirements for bonds issued by admitted sureties. Other provisions, however, are less clear and refer to "sufficient sureties" or do not specify a qualification standard. We

believe that regulatory oversight of sureties is sound public policy and protective of public owner and taxpayer interests. The Bond and Undertaking Law, Code of Civil Procedure §995.311, assures that admitted surety insurers execute bonds on public projects. Participants on private projects deserve equivalent protection. We strongly urge consideration of a uniform requirement that an admitted surety insurer execute all bonds called for in the mechanics lien law and associated statutes.

Partial Bonds. In several places in the tentative recommendation, as indicated below, bonds are required in amounts less than 100% of the contract or claim amount. The rationale for requiring bonds in amounts less than 100% of the contract or claim amount is not apparent from the existing statutes or the tentative recommendation. If the rationale is predicated on cost savings in bond premiums, such rationale is misplaced. Sureties calculate their premiums based on the full amount of the contract price or claim, not on the bond amount. Therefore, requirements for "partial" bonds do not save premium dollars. Moreover, "partial" bonds mean that bond beneficiaries are receiving less bond coverage, since the surety's obligation is limited to the stated bond sum. To that end, we suggest that all statutory surety bonds be for no less than 100% of the contract or claim amount.

Attorneys Fees. We support the American Rule under which each litigant pays its own fees. In construction disputes, the fees and expenses can often equal or exceed the amount legitimately in dispute. Almost all litigants, though, firmly believe that they are right and will prevail. The knowledge that they will nevertheless pay their own fees is a check on continuation of uneconomic litigation and an incentive to both parties to settle. If there is to be a fee shifting provision, however, it should be a prevailing party provision similar to proposed §45080(c). This is consistent with California public policy favoring mutuality of fee shifting provisions, see Cal. Civil Code §1717 converting all one-sided contractual fee shifting provisions into prevailing party provisions.

Notice. The manner in which the current mechanics lien law addresses notice requirements is highly technical and complex. The tentative recommendation attempts to simplify some of these requirements, but we recommend that the California Law Review Commission consider further changes to unravel the considerable complexities and enhance understanding of these notice requirements, particularly as to types and service of notice. For example, service of notice could be treated in a less proscriptive manner, such as provided under the Federal Miller Act. Under the Federal Miller Act, service of notice may be accomplished by "any means that provides written, third-party verification of delivery to the contractor at any place the contractor maintains an office or conducts business or at the contractor's residence..."(see 40 USC § 3133). The notice requirement in the Federal Miller Act was revised and modernized in 1999 to permit different delivery methods, including by electronic means, so long as the means of delivery provides for "written, third-party verification." In addition, if timely receipt of written notice is admitted, the manner of its delivery should be irrelevant. Only if receipt is contested should the claimant have to show it used a method that complied with the statute.

We support a requirement that notice be sent to a party's address listed on the bond or contract involved, but there should be a backup or default provision so that if no address is listed the person giving the notice can rely on publicly available information. For sureties, that could be the address listed with the California Department of Insurance and for contractors, the address listed with the Contractors State License Board. Both state agencies include those addresses on their Internet sites.

Definitional Practices. Undertaking the difficult task of simplifying and harmonizing separate statutes intended to address different situations requires exacting attention to the use of defined words and phrase to ensure that such definitions result in the same meaning or result in all contexts of use. As will be discussed more thoroughly below, the tentative recommendation establishes common definitions of words and phrases for use throughout the statutes comprising the mechanics lien law and associated construction remedies. In doing so, the tentative recommendation may create unintended results. For example, the tentative recommendation creates a definition of "labor, service, equipment, and material" which include "skills", "surveying" and "construction plans" in the definition. Would this definition permit design professionals or others who do not work on the construction site to make claims against the contractor's payment bond furnished under Chapter 6?

Specific Comments – Bond Chapters

PRIVATE WORK OF IMPROVEMENT

CHAPTER 6. PAYMENT BOND

§ 7600. Public policy of payment bond

This section restates the second sentence of current §3236, but without the first sentence the second sentence just seems to state the obvious. The Owner does not need legislative sanction to require a bond to protect against the direct contractor's default (a performance bond) or the direct contractor's failure to pay for labor or material (a payment bond). The title to the new section refers to a "payment bond" but the text address both performance and payment.

The first sentence of §3236 states that by recording a copy of the contract and payment bond the owner insulates him or herself from double liability. That is, the owner's only liability is to pay the balance of the contract funds still in his or her hands, and the payment bond surety will pay any excess owed to the lien claimant. The second sentence makes it clear that there is no negative implication that the owner cannot also shift to the direct contractor and its surety the obligation to meet all of the contractor's obligations including performance obligations owed to the owner. The first sentence of §3236 will be part of new §7602.

Commenters recommend that §7600 be revised to read as follows:

> **§7600 Public Policy of Performance and Payment Bond**
>
> 7600. Notwithstanding §7602, an owner may require a performance bond, a payment bond, or other security as protection against a direct contractor's failure to perform the contract or to make full payment for all labor, service, equipment and material provided pursuant to the contract.

§7602. Limitation of Owner's Liability

The intent of §7602 is to limit the owner's obligation to a mechanics lien claimant to the unpaid balance the owner holds under the direct contract if the owner requires and records a payment bond of at least 50% of the contract price. Commenters support this intent, but suggest that the provision should be improved in three ways.

First, as worded, the owner's liability is limited to "the contract price" whereas the intended limit is the unexpended balance of the contract. It would be clearer to spell out that the owner's liability to the lien claimant is limited to the unexpended balance when the owner receives notice of the lien claim.

Second, the bond should be for 100% of the contract amount not 50%. The cost of performance and payment bonds is based on the contract amount not the penal sum of the bond, and there will be no additional cost to the direct contractor, and therefore to the owner, to provide a 100% bond.

Third, the requirement that the bond be from "sufficient sureties" is unclear. At the time the bond is recorded, there will be no one to object if the sureties are not "sufficient," and by the time lien claims are filed it will be too late to remedy any deficiency. Other statutes require that payment bonds be provided by an admitted surety insurer, a term defined in the Bond and Undertaking Law at Code of Civil Procedure §995.120, and that term should be used in §7602 in place of "sufficient sureties."

§7604. Bond required by lending institution

Commenters agree that the intent of the current statute is to bar after the fact questioning of a bond from an admitted surety insurer and that the proposed change corrects an error in existing Civil Code §3237.

§7606. Payment bond

In order to qualify as a bond that prevents mechanics liens from attaching to the owner's property, the bond has to meet the requirements described in this section. The way the section has been re-written, however, changes this section from a definition of what qualifies as a "payment bond" under this part of the Code to a substantive provision dictating the coverage of a payment bond. As a substantive provision, it is both incorrect

and harmful. There are many payment bonds that are not conditioned on "the payment in full of the claims of all claimants." For example, a supplier on a job could be concerned about payment and insist in the negotiation process that the contractor or subcontractor to whom the material will be furnished provide a bond to guaranty payments to that specific supplier.

Commenters suggest that the terms of current §3096 be retained and the provision moved to the definitions in Article 1. That is, the provision should say, "Payment bond means a bond that is conditioned on the payment in full . . . ." Also, instead of "good and sufficient sureties" as used in current §3096, the provision should require the bond to be from an admitted surety insurer for the same reasons discussed in connection with §7602 above.

§7608. Limitation on part

We assume that the intent of the phrase "to the direct contractor or one of the direct contractor's subcontractors" is to limit coverage of the payment bond to claimants who furnished labor, service, equipment, or material to the direct contractor or to a first tier subcontractor of the direct contractor. The definition of "subcontractor" in §7044, however, includes anyone with a contractual relationship with another subcontractor.

A direct contractor can monitor its own subcontractors and try to assure that they pay their obligations on the project. It is much more difficult to monitor more remote subcontractors, and the direct contractor's bond should not extend beyond the debts of the direct contractor or of a first tier subcontractor. Section 7608 should make that distinction clearly and unambiguously. Commenters recommend that subsection (a) be revised to state:

> (a) This part does not give a claimant a right to recover on a direct contractor's payment bond given under this chapter unless the claimant provided labor, service, equipment, or material to the direct contractor, or to a subcontractor in privity of contract with the direct contractor, for use in performance of the contract between the direct contractor and the owner.

§7610. Statute of limitations against surety on recorded bond

Commenters support the revisions to the substance of current Civil Code §3240 but suggest that the title of §7610 should be changed to reflect the revision. The new Title would be "Statute of limitations for suit on recorded bond."

§7612. Notice prerequisite to enforcement

The preliminary notice and the post completion notice serve two different functions, and compliance with them should not be in the alternative. The preliminary notice tells the direct contractor who is working on the project and potentially may make a claim if not

paid. During contract performance, the direct contractor can be sure that releases are provided or steps are taken to assure payment to persons who gave the preliminary notice. If the preliminary notice is not mandatory, however, there will be potential bond claimants who do not provide it. The direct contractor, therefore, will continue to be exposed to liability to persons that it may not know are furnishing material, equipment or services to a subcontractor on the project.

The other weakness of the preliminary notice is that it is given early in the job before the potential claimant knows whether it will be paid or not. If the notice is mandatory, it will become a matter of routine and literally hundreds of such notices will be received at the beginning of even a modest sized job.

The post completion notice is designed to tell the direct contractor if a first tier subcontractor has not paid its bills so that the direct contractor can withhold final payment until the bills are paid or can use the retained subcontract balance to pay the bills. Thus, the point of the post completion notice is to inform the direct contractor that a failure to pay has occurred.

The proposed §7612 and the current Civil Code §3242 state the notice requirement in the alternative and seriously undercut the utility of both notices. The direct contractor cannot depend on receiving a preliminary notice from all potential claimants or a post completion notice from everyone with a bond claim. If they can be provided in the alternative, neither notice serves its purpose.

Some states require both a preliminary notice and a final notice if the subcontractor or supplier is unpaid. Other states, require one or the other. Commenters recommend that §7612 be revised to change "any of the following conditions" to "both of the following conditions." If that is not acceptable, it would be better to delete the post completion notice and require only a preliminary notice.

PUBLIC WORK OF IMPROVEMENT

CHAPTER 5. PAYMENT BOND

§45010. Payment bond requirement

The Bond and Undertaking Law at Code of Civil Procedure §995.311 requires that bonds on public works contracts be executed by an admitted surety insurer. There have been cases in which public entities failed to verify that the surety was admitted in California, and the public entity was held to be liable to the claimant. See, for example, *Walt Rankin & Associates, Inc. v. City of Murrieta*, 84 Cal.App.4th 605, 101 Cal.Rptr.2d 48 (2000). Section 45010 does not purport to change that requirement, but it would help to make public employees aware of the necessity that the surety be admitted if subsections (a)(1)

and (a)(2) were revised to state, "a payment bond executed by an admitted surety insurer."

If subsection (b) refers to change orders or extra work ordered pursuant to the contract, then the original payment bond should protect persons who do this "supplemental" work. If it refers to a separate scope of work not required under the original bonded contract, then subsection (b) should be deleted. A supplier or subcontractor working for the direct contractor or a subcontractor on a public project is going to assume that there is a payment bond in place to protect it, and a new bond should be required unless the original bond protects the suppliers and subcontractors.

§45020. Consequences of failure to give bond

If the law requires a bond and no bond has been provided, then the public entity should not compound the violation by disbursing funds to the contractor. If the contractor is able to get a bond and the failure was just an oversight, the contractor can provide the bond in a matter of days and there will be no disruption to the job. If the contractor does not qualify for the bond, the contract should be defaulted and re-let. In either case, the public entity should retain all funds remaining under the contract to protect itself and to protect potential payment bond claimants.

The Commission asked if the phrase "as required by statute" is too broad. There are numerous statutes requiring bonds on public projects, and it should not matter which statute required the bond. Either the law was followed or it wasn't, and if it wasn't, no contract funds should be released until the contractor has complied.

§45030. Bond requirements

Under §42030(a)(1), a claimant on a payment bond must have furnished labor, service, equipment or material "pursuant to an agreement with a direct contractor." This seems to limit claimants to suppliers or first tier subcontractors in privity with the direct contractors. On the other hand, §45030 says the bond covers the failure of the direct contractor or a subcontractor to pay such a claimant. A subcontractor cannot fail to pay someone in privity with the prime contractor.

Commenters do not believe the statutes intend to limit claimants to those in privity of contract with the direct contractor. In that case, §45030 is acceptable as proposed and the correction should be made in §42030. However, if the intent is to limit claims to the direct contractor's obligations, "or a subcontractor" should be deleted from §45030(b). Finally, if the intent is to limit claims to obligations of the direct contractor or a first tier subcontractor, §45030(b) should be revised to say, "if the direct contractor, or a subcontractor in privity with the direct contractor, fails to pay . . . ."

§45040. Construction of bond

Section 45040 should be deleted. None of the three subsections are logical or reasonable if applied to a public works payment bond.

Subsection (a) requires that the bond be construed against the surety and in favor of the beneficiary. On a public project, however, the bond form is selected by the public owner and included in the bid documents. The surety has no ability to modify its terms or the terms of the relevant statutes. In addition, the party primarily liable on the bond is the bond principal, the direct contractor. The bond cannot be construed against the surety without also construing it against the direct contractor. As between the direct contractor and the claimant, there is no reason to "construe" the bond in favor of one party and against the other. Presumably, the origin of this provision was the assumption that the bond is an insurance obligation and is drafted by the surety. That assumption is simply incorrect.

Subsection (b) should be modified to say that the principal and surety are not discharged by a breach of the prime contract. Commenters agree that a payment bond claimant should not lose its statutory protection because the public owner breaches the construction contract. On the other hand, if the beneficiary itself breaches its obligations, the principal and surety on the bond should be able to assert the beneficiary's own breach as a defense. For example, if a subcontractor fails to perform and the direct contract has a valid claim for costs incurred to correct or complete the subcontractor's work, the subcontractor cannot avoid liability for the consequences of its own actions by suing on the bond instead of the subcontract.

Subsection (c) is clearly contrary to a great deal of the rest of Chapter 5 because it would seem to permit the claimant not to give the required notices or sue within the required time periods and then argue that §45040(c) excuses compliance with these conditions on recovery. Subsection (c) should be deleted.

§45050. Statute of limitations

The substance of §45050 is acceptable but it would be easier to understand if the cross reference to §44140 were replaced by the actual time limit.

§45060. Notice required

See comments above under §7612

§45070. Notice to principal and surety

Subsection (a) contradicts §45060 by requiring post completion notice whether or not the preliminary notice was given.

Subsection (d) does not take into account that many bond forms do not require, or have a space for, the surety's address to which notice can be given. There should be a default for notice to the surety at the address available from the Department of Insurance web site if no address is provided in the bond.

§45080. Action on bond

Commenters support the prevailing party fee provision of subparagraph (c) if there is to be a fee shifting provision. See discussion under Attorneys Fees in the General Comments section.

§45090. Limitation on chapter

If "one of the direct contractor's subcontractors" means a first tier subcontractor in privity with the direct contractor, it properly limits coverage of the payment bond. It would be preferable to remove any ambiguity by substituting "a subcontractor in privity with the direct contractor."

Specific Comments – Other Chapters

PRIVATE WORK OF IMPROVEMENT

CHAPTER 1. DEFINITIONS AND GENERAL PROVISIONS

Article 1. Definitions

§ 7026. Material supplier

Section 7026 (a) should require that the materials or supplies must be substantially consumed in the work of improvement. Capital equipment or supplies that are not consumed in the project, but can be used on many projects, such as tools or forms for walls or curbs, should not be covered. Paragraph (b) is a significant presumption, but the contractor or surety should be able to rebut it by showing that the material or supplies were not substantially consumed on the project.

Article 2. Miscellaneous provisions

§7057. Effect of act by owner

The payment bond protects third parties, and subcontractors or suppliers who relied on the payment bond should not lose their protection because of an act of the owner. The direct contractor's performance bond, however, protects only the owner, and if the owner breaches the contract, the statute should not prevent the direct contractor and its surety from asserting the breach as a defense to the extent otherwise permitted by law.

Article 4: Notice

§ 7102. Contents of Notice

See Comment on Notice under General Comments.

§ 7106. Address as which notice is given

See Comment on Notice under General Comments.

§ 7114. When notice complete

See Comment on Notice under General Comments.

Article 6. Bonds

§ 7142. Release of surety from liability

The payment bond protects third parties, and subcontractors or suppliers who relied on the payment bond should not lose their protection because of an act of the owner. If there is a basis to rescind the bond, however, it would have to involve fraud or misrepresentations by the claimant, or by the owner if the owner is seeking to enforce the bond, and the statute should not bar rescission under those circumstances. Rescission of the bond should be deleted from subparagraph (c).

If a bond is provided to comply with a statute, the bond cannot reduce the claimant's rights as provided by the statute. Otherwise, however, the parties should be free to include whatever conditions they choose. The statutes recognize numerous conditions such as notice of claims and suit limitations. There is no need for subparagraph (d), and it will lead to attempts to void proper notice or limitations provisions. Subparagraph (d) should be deleted.

Article 8. Waiver and Release

§§7160 – 7176

The waiver and release Article effectively prevents the parties from agreeing to anything other than a receipt for payment received. Barring a blanket waiver in advance of commencing work as against public policy is one thing, but once a project is underway, the parties to a contract or subcontract should be able to reach a partial settlement including a release of all claims to date. Section 7162 requires use of the forms set out in §§7170 and 7172, but they each have an Exception for "the right to recover compensation for labor, service, equipment, or material not compensated by the payment." There should be greater freedom of contract for the parties to the construction project.

CHAPTER 2. PRELIMINARY NOTICE

§ 7206. Effect of preliminary notice

To correctly restate the paragraph preceding current § 3097 (d), § 7206 (b) should read as follows: A design professional who has furnished services for the design of the work of improvement and who gives a preliminary notice as provided in this section not later than 20 days after the work of improvement has commenced shall be deemed to have complied with subdivision (a). The way § 7206 (b) is currently rewritten could lead the reader to believe that a regular payment bond on the contract would cover the design professional when in fact it may not.

§ 7208. Coverage of preliminary notice

The final word in subparagraph (b) should be subcontractor, and not contractor.

CHAPTER 4. MECHANICS LIEN

Article 2. Conditions to Enforcing a Lien

§7400 Persons entitled to lien

Equipment lessor and Builder are not defined in §7100. Equipment lessor would seem to be obvious, but if a Builder is to have a lien right, the term should be defined.

§ 7428. Release bond

Section § 7428 (b) should also specify that the release bond will never be responsible for any amount greater than the penal limit listed on the bond; to include costs, interest, and any attorney fees for which the bond may be found liable. This will clarify that the surety is not responsible to pay any amount once the penal limit has been paid out. If the surety can't rely on the penal bond limit being just that, the highest amount it will ever pay out, then there will be no way for the surety to determine its exposure to effectively write the bond.

CHAPTER 5. STOP PAYMENT NOTICE

Article 1. General Provisions

§7500. Stop payment notice exclusive remedy to reach construction funds

A payment bond surety responsible for the obligations of a contractor or subcontractor should be authorized to give notice that further payments not be released to the contractor or subcontractor. At least, this section should not prevent the surety from exercising

contractual, statutory or common law rights that otherwise exist to have contract funds held for use in paying contract obligations.

§ 7510. Release bond

See comments to § 7428.

Article 3. Stop Payment Notice to Construction Lender

§ 7532. Bonded stop payment notice

As noted in the comment to § 7428, and § 7510, and for the same reasons, a line should be added that the bond will never be responsible for any amount greater than the penal limit listed on the bond. § 7532 seems to say this at the end, but an extra sentence clarifying this intent will save a lot of court time and unneeded expense.

PUBLIC WORK OF IMPROVEMENT

CHAPTER 1. DEFINITIONS

§ 42080. Mailed Notice

See Comment on Notice under General Comments

§ 42100. Liability of surety

See comments for § 7142.

CHAPTER 4. STOP PAYMENT NOTICE

Article 1. General Provisions

§ 44130. Giving of stop payment notice

See Comments on Notice under General Comments.

§ 44180. Release bond

The penal sum of the bond should be an explicit limit to the surety's obligation.

Article 3 Waiver and Release

§§42310 – 42390

The waiver and release Article effectively prevents the parties from agreeing to anything other than a receipt for payment received. Barring a blanket waiver in advance of commencing work as against public policy is one thing, but once a project is underway, the parties to a contract or subcontract should be able to reach a partial settlement including a release of all claims to date. Section 7162 requires use of the forms set out in §§7170 and 7172, but they each have an Exception for "the right to recover compensation for labor, service, equipment, or material not compensated by the payment." There should be greater freedom of contract for the parties to the construction project.

Article 4. Enforcement of Payment and Claim Stated in Stop Payment Notice

§44110. Stop payment notice exclusive remedy to reach contract funds

A payment bond surety responsible for the obligations of a contractor or subcontractor should be authorized to give notice that further payments not be released to the contractor or subcontractor. At least, this section should not prevent the surety from exercising contractual, statutory or common law rights that otherwise exist to have contract funds held for use in paying contract obligations.

We welcome the opportunity to discuss all or any of these comments further or to provide additional input as requested.

Sincerely,

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September 29, 2006

Via E-mail

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

Re: Comments to June 2006 Mechanics Lien Law Tentative Recommendations
OGC File No. 06-1548

To Whom This May Concern:

The Commission seeks comments regarding its June 2006 Tentative Recommendation involving changes to mechanics lien law and associated construction remedies, including, but not limited to stop notice provisions. What follows is the California State University's ("CSU") response to the Commission's request for comment. As directed, the CSU advises the Commission where it approves the tentative recommendation and details where it believes the tentative recommendation should be omitted or modified.

At the outset, we note that we believe the proposed changes will be, on the whole, a great benefit in both the public and private works contexts. With regard to particular provisions in the Recommendation, CSU makes the following comments:

1) **Mailed Notice** (p. 21): CSU has no objection to alternative methods for delivery of notices, so long as they include some type of delivery confirmation or other "proof of receipt."

2) **Proof of Mailing** (p. 23): No comment.

3) **Acceptance by Public Entity** (p. 25-26): No comment.

4) **Time for Recording Notice of Completion** (p. 26): CSU approves the recommendation, but seeks clarification as to whether "15 days" is 15 calendar days or 15 business days.

5) **Notice of Recordation** (p. 26): Assuming this provision applies in the public works context, CSU objects to the proposed requirement that an owner provide a potential line claimant with a copy of the notice of completion as it would put a more onerous burden on the CSU than is currently in place.

6) **Notice by County Recorder** (p. 27): Again, assuming this provision applies in the public works context, CSU objects for the reason stated above.

7) **Separate Contracts on Single Job** (p. 27): CSU approves this recommendation. In fact, it would go slightly further in suggesting that public agencies, including the CSU, be permitted to file a Notice of Completion "except for" distinct, incomplete work elements.

8) **Contract Change** (p. 29-30): CSU approves this recommendation.

9) **Notice to Construction Lender** (p. 30-31): CSU approves this recommendation.

10) **Attorneys' Fees** (p. 35): No comment.

11) **Invalid or Unenforceable Claim of Lien** (p. 35-36): CSU approves the proposed remedies.

12) **Stop Payment Notice** (p. 39): CSU approves this recommendation.

13) **Amount of Claimant's Claim** (p. 39): CSU approves of a requirement that a stop notice state the claimant's demand after deducting all just credits and offsets.

14) **Claim for Contract Changes and Breach of Contract** (p. 40): CSU objects to this recommendation. Allowing stop notice claims to include claims for contract changes, breach of contract, or any other items outside of the current statutorily permissible amounts would unnecessarily tie-up project funds. Additionally, the potential for abuse of this provision by stop notice claimants is high.

15) **Sureties on Bond** (p. 41): CSU approves this recommendation.

16) **Release of Notice or Reduction of Amount of Claim** (p. 41): The Commission assumes in this section that "general statutory waiver and release forms are inapplicable to a claimant's release of a stop payment notice or reduction of the amount claimed in the notice." CSU's understanding is that the amendment to Civil Code section 3262 actually permits claimants to use alternative forms; it does not exclude entirely the use of existing forms. CSU seeks clarification from the Commission on this point.

17) **Duty to Withhold Funds** (p. 41-42): No comment.

18) **Enforcement of Payment of Claim Stated in Notice** (p. 42): CSU takes no position on whether the five-day notice requirement should be made mandatory.

19) **Bond Underwriter Licensed by Department of Insurance** (p. 43): CSU approves this recommendation.

20) **Public Works Contract** (p. 45): CSU approves the relocation of public works contract remedies to the Public Contract Code from their current location among the mechanics lien provisions of the Civil Code. This change will go far towards meeting the Commission's goals of simplifying these provisions and making them more user-friendly.

21) **Notifications** (p. 45): CSU objects to the recommendation that notice to a public entity be addressed to the "disbursing officer" of the public entity. In the CSU system, each of the 23 campuses appoints a contract administrator as the individual responsible for managing construction projects on the respective campuses. That individual maintains the central depository and/or files relative to each construction contract. Requiring that notice be addressed to a "disbursing officer" - or in the CSU's case, a procurement officer - contradicts the manner in which the CSU manages its contracts.

22) **Cessation of Labor** (p. 47): CSU takes no position on whether the law governing a public work and a private work should be harmonized such that both have the same period of time for completion by cessation of labor.

23) **Notice of Cessation** (p. 48-49): CSU takes no position on this recommendation as it rarely records a notice of cessation.

24) **Notice of Acceptance** (p. 49-50): CSU approves this recommendation.

25) **Notification of Stop Payment Claimant** (p. 51): CSU approves this recommendation. In fact, CSU contends that the cost of such notice is actually higher than the recommended $10 and on this basis, would request that the Commission consider requiring payment of $20 or higher.

26) **Preserve Status Quo** (p. 54): Current law mandates that the CSU require a 100% payment bond in all construction contracts over $5,000. Bonds in this low an amount are difficult to obtain, and CSU believes this circumstance decreases the availability of competitive bidders on its public works contracts. CSU requests that the Commission recommend raising the contract amount to over $25,000 for the CSU's construction projects. This would bring the CSU in line with other public entities, including, for example, the California Community Colleges and the Los Angeles Unified School District.

Should you have any questions regarding the above, please do not hesitate to contact me via e-mail or at 562/951-4478.

Sincerely,

Andrea M. Gunn
University Counsel

cc: Jim Corsar
Karen Yelverton-Zamarripa

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HANSON BRIDGETT
MARCUS VLAHOS RUDY LLP

September 29, 2006

Nathaniel Sterling
Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303

Re: *Comments to Mechanics Lien Law Revisions*

Dear Mr. Sterling:

Pursuant to my conversation with the Commission today, I have enclosed a hard copy of the Building Owners and Managers Association Comments regarding proposed changes in the Mechanics Lien Laws, which I e-mailed to the Commission earlier today.

Thank you for your time and attention.

Very truly yours,

E. Charles Cordes

E. Charles Cordes

ECC:js

Enclosure

Building Owners and Managers Association

Comments on the Proposed Changes to the Mechanics' Lien Law

Submitted to the California Law Revision Commission on behalf of BOMA by
E. Charles Cordes, Esq., Hanson, Bridgett, Marcus, Vlahos & Rudy

September 29, 2006

A. Article 7 Release Order

1. Scope of § 7840

The petition for a release order authorized by section 7480 should be expanded to allow for reduction of an overstated lien in addition to complete removal of an invalid lien. It its current state, section 7480 provides only for complete removal of the lien where (1) the lien action was not timely filed, (2) the lien was recorded with intent to slander title or affects a subsequent purchaser without notice, (3) the lien has been paid in full, (4) none of the claimed labor or materials was supplied to the property, (5) the claimant was unlicensed, or (6) the petitioner can demonstrate res judicata against the claimant.

The most common problem a property owner faces is not a wholly invalid lien, but rather an overstated lien. There is currently no statutory vehicle by which an owner may bring an action attacking the amount of contractor's lien at the outset of an action. In *Lambert v. Superior Court* (1991) 228 Cal.App.3d 383, the Court of Appeals concluded that an owner's due process rights required that it have recourse to a motion filed early on in the mechanics' lien action in which it may seek to remove an invalid lien. Such motions, dubbed "*Lambert* motions," are often aimed at reducing the amount of the lien rather than eliminating it entirely. But some trial courts struggle with the scope of their authority under *Lambert,* in part because of ambiguous language in the decision. In *Lambert,* the contractor sought $28,369 in unpaid change order work along with $88,958 in delay damages. The court found that delay damages are not recoverable in a mechanics' lien action. It remanded the matter to the trial court to reconsider the underlying motion "to remove the lien." Implicit in the *Lambert* ruling was a finding that only the delay damages portion of the lien was unrecoverable. However, its "remove the lien" language leads litigants in *Lambert* motions to argue either that the lien must be wholly removed if even a part of it is provably false or that the lien cannot be touched at all unless it is proved to be wholly false. This "all or nothing" reading of *Lambert* was rejected by the Court in *Basic Modular Facilities, Inc. v. Ehsanipour* (1999) 70 Cal.App.4th 1480, 1485, where it observed that nothing in *Lambert* would bar a trial court from reducing an excessive lien to its property amount.

We believe that section 7480 should be modified to expressly authorize reduction of an overstated lien consistent with *Lambert* and *Basic Modular*. Lien amounts unrecoverable under current Civil Code sections 3123 and 3140 should not be allowed to remain as part of lien simply because the unauthorized amounts do not wholly eliminate the lien. Nor is it an acceptable argument that an overstated lien may be reduced upon summary judgment or at trial. It is a matter of timing. As the *Lambert* court observed, overstated liens put pressure on owners by dramatically increasing the cost and collateral requirements for "bonding around" the lien, sometimes beyond the owner's ability to pay. (228 Cal.App.3d at 386.) Due process requires a "speedy" means for property owners to attack unsupportable liens. (*Connoly Development v. Superior Court* (1976) 17 Cal.3d 803, 820-823.) Moreover, the amount of reduction is limited by the Mechanics' Lien Law itself. A contractor may only recover the contract price or reasonable value of the labor and materials supplied, whichever is less, minus any duplicative subcontractor claim. (Civil Code §§ 3123 and 3140.)

2. Timing of Hearing § 7846

The timing requirements of section 7846 should be modified to provide a faster resolution of the petition. The proposed timing requirements are geared to former Civil Code section 3154, which assumes there is no pending lien enforcement action, the lien having become invalid by operation of law. Some title insurers will disregard a recorded lien where it can be shown that no timely lien enforcement action was filed. In such case, the need to remove a lien is arguably less urgent. But the revised statute contemplates applications being filed within an enforcement action on grounds that implicate the speedy remedy required by the court in *Connoly, supra.* In this context, the carry-over notice and hearing provisions of section 3154 make less sense. For example, a petition may involve a detailed factual inquiry, such as where the claimant's intent to slander title forms the basis of the removal petition, and yet section 7486 allows the petitioner to serve its petition as late as 10 days before the hearing. The contractor must then swiftly respond to the petition or show good cause to the court to extend the hearing date. On the other hand, the statute envisions as many as 75 days from the time the petition is filed to the time the court issues a ruling. This seems like an unduly long time where, for example, a false lien may wholly stop a pending sale of property.

A proper balance between the property owner's right to a speedy remedy and the contractor's right to defend the application is preferable. For example, the petition could be subject to the timing requirements of CCP section 1005, which would typically provide the contractor with an actual copy of the petition earlier than the service deadline under section 7846. A two-week extension, or other reasonably short extension could be had upon a showing of good cause. But, in keeping with the dictates of *Connolly*, the court's ruling should be linked to hearing on the matter, perhaps no later that ten court days if the matter is taken under submission.

3. Burden of Proof at Hearing § 7846

Under the Mechanics' Lien Law, the lien claimant has the burden of proving the validity of the lien. (*Basic Modular, supra,* 70 Cal.App.4th at 1485.) Existing section 3154, on which section 7846 is modeled, is silent as to the burden of proof and it must be presumed that the lien claimant has the ultimate burden of proof. Section 7846 now affirmatively shifts the burden of proof to the property owner. This is inconsistent with a long-standing, governing premise of the Mechanics' Lien Law. Moreover, section 7860 petitions will often be made early on in an action, or with no pending action at all, and the property owner will not have access to the contractor's records in order to fully assess the lien claim. It is more consistent with current law, as well as the practical ability to marshal evidence, for the petitioner make an initial showing calling into doubt the validity of the lien, but that the ultimate burden remain on the contractor to demonstrate the lien's validity. (*Cf.* CCP § 405.32 (burden on lis pendens proponent to show probable validity of claim).)

B. Attorney's Fees

The Tentative Recommendation states that "Existing law allows attorney's fees in some types of stop notice and payment bond enforcement actions, but not for enforcement of a mechanics lien.

The Law Revision Commission seeks public comment concerning the disparity of treatment." (Tentative Recommendation at p. 35.)

We recommend that maintaining the status quo is the best approach to apportioning the risk of funding prevailing-party attorney's fees in mechanics' lien actions. Statutory attorney's fees provisions in stop notice and payment bond enforcement actions are tied to bond surety obligations. A bond surety modulates the fee risk through its bond cost. And its obligation for attorney's fees is traditionally entailed in the nature of the obligation undertaken. In contrast, a property owner's chief obligation is to timely pay its prime contractor. To the extent the project owner has undertaken the risk of attorney's fees in a construction dispute, it will be the subject of a provision in its contract with the prime contractor. But it is often the case that an owner who has paid its prime contractor for completed work ends up defending lien actions from subcontractors despite the owner's good faith efforts to monitor and collect lien waivers in support of progress and/or final payments. It is also the case that private works prompt payment penalty statutes provide for recovery of attorney's fees in the more egregious situations of failure to pass through funds. Thus, to the extent that an owner improperly withholds funds, it is already at risk for attorney's fees. But to the extent that the project owner has paid the prime contractor in good faith only to discover that the now-insolvent contractor has not passed through the funds to its subcontractors, the project owner should not be subject to the risk of having to pay claimants' attorney's fees. The current arrangement is stable and workable. There is no compelling reason to shift such risk to property owners.

C. Article 8 Waiver and Release §§ 7160 - 7176

We suggest that the conditional and unconditional progress payment waiver forms (§§ 7170 - 7172) be revised to specifically call for a beginning and ending date range for the services being released. Existing statutory waiver and release forms (see Civil Code § 3262) provide that services are being released "through" a certain date, which is not usually the date the form is executed. This "date-through" language is carried through to the current form. The forms can become ambiguous where, for example, a contractor is terminated for failing to pass through the project owner's progress payments to its subcontractors. The owner may enter into direct contracts with the subcontractors and pay for later work. The subcontractor may be reluctant to release all work through the later date when it retains a claim against the prime contractor on earlier work. Accordingly, listing a beginning and ending date for the work released will make tracking of payments easier when disputes arise.

D. Abandoning Notice of Increase in Contract Price § 7430

We agree that current Civil Code section 3123(c), requiring that "[t]he owner shall notify the prime contractor and construction lenders of any changes in the contract if the change has the effect of increasing the price stated in the contract by 5 percent or more," need not be carried over into the new statutes. The provision is unnecessary for at least two reasons. First, it is superfluous. A prime contractor is equally able to know the magnitude of contract changes and a construction lender will typically require notice of contract changes independent of any statutory obligation on the part of the property owner. Second, it is not followed in practice because there is no apparent penalty for violating the provision.

E. Contents of a Claim of Lien § 7418

Section 7418 requires the claimant to provide "[a] statement of the claimant's demand after deducting all just credits and offsets." We believe that the claimant's statement should provide more detail regarding the "just credits and offsets" than a single amount purporting to be the total value of labor and materials provided to the project. A great deal of effort is often expended in mechanics' lien litigation simply obtaining a claimant's breakdown of amounts comprising its lien. For example, in the case of a prime contractor's lien, it is impossible to discern from the lien itself what part of the total claim corresponds to particular subcontractors and suppliers, and how much of the claim corresponds to fees and general conditions, home office overhead, delay, interest, or other categories of costs which may or may not be recoverable by way of a mechanics' lien. Often property owners are well into litigation before this information is obtained. Since contractors are best equipped to know the categories of costs that make up their lien claims, we believe that section 7418 should be revised to require that a lien claim include a breakdown of costs by general category so that not only the sum, but its parts may be known. We believe the end result of such a requirement would be a beneficial transparency to the lien amount leading to a clearer understanding of the claim's validity. As an alternative to requiring such information in the lien itself, we suggest adding a provision requiring the contractor to provide an itemization of lien amounts upon request from the property owner.

F. Forfeiture of Lien for False Claim § 7424

Section 7424 provides that a claim of lien may be forfeited upon a showing that it was made with intent to slander title or to defraud. This provision is ambiguous as to the time at which the claimant's intent must exist. For example, a lien claimant may discover after it has recorded a lien that all or part of its lien claim was false when recorded or has since become false. We believe that a lien claimant who later discovers that all or part of his lien is false or unsupportable should be obligated to record a release or partial release of lien. Leaving a false lien in place after discovery of its falseness should put the lien claimant at risk for loss of his lien under section 7424 and for damages under section 7426. We suggest section 7424 be modified to provide that a lien claim contains erroneous information whenever the lien claimant has facts which would indicate that all or part of its claim of lien is false or unsupportable, and that a lien claimant's willful maintenance of a false lien after discovery of such information may constitute intent to slander title or to defraud.

G. Notice of Intended Recording of Claim of Lien § 7420

We believe that section 7420 should be revised to define a required period of time between the claimant's service of notice and the claimant's right to record a mechanics' lien. The purpose of a defined period between the claimant's notice of intent to record a lien and the actual recording is to allow the property owner time to respond to the impending lien if it considers the claim false or invalid. As noted in *Connoly, supra*, a property owner may move for injunctive relief to preempt the recording of an invalid lien. (17 Cal.3d at 822.) The property owner should have a

reasonable time in which to move the court to prevent recording of a lien that it considers false or invalid. We suggest that notice be provided no earlier than ten calendar days before the lien may be recorded if notice is made by personal delivery, twelve calendar days if notice is made by express or overnight mail, and fifteen days if given by regular mail, certified mail, or the procedure set forth in CCP § 415.20. (*See* § 7104 regarding manner of notice.)

H. Interests Subject to Lien § 7442 and the Notice of Nonresponsibility § 7444

We believe that section 7442 should be modified to make a landlord's notice of nonresponsibility under section 7444 more effective. In practice, the "participating owner" doctrine has become so broad that many landlords do not bother to post a notice of nonresponsibility even where the tenant is contracting for improvements contemplated and paid for solely by the tenant. Section 7442(b) provides that a noncontracting owner, i.e. a tenant's landlord, who has "knowledge" of the improvements may be responsible for mechanics' lien claims. This implies that the landlord's mere awareness that its tenant is contracting for improvements makes the owner's fee interest subject to lien. In practice, the landlord is very often going to have mere awareness of tenant improvements, for example, the owner may have approved a tenant's request that changes be allowed or the owner's managing agent may observe that improvements are being made. This level of involvement should not be the source of lien liability. We believe that the lease agreement between the landlord and tenant should govern. If the lease itself does not require improvements to be made, or require the owner to pay for all or part of tenant-defined improvements, then a notice of nonresponsibility should be effective. An owner is not a "participating" owner by having mere awareness of tenant improvements. Direct owner involvement through its lease with the tenant should be the touchstone. Owners who do not so involve themselves in tenant improvements should be able to insulate themselves from mechanics' lien risk. Section 7442 should be modified to specify the degree of noncontracting owner involvement required for the owner's fee interest to be at issue.

I. Definition of Completion § 7150

The definition of completion of a private work of improvement should be clarified and simplified. Omitting the owner's "acceptance" as a form of completion makes sense because in practice there is typically no moment of formal acceptance. However, given the number of cases assessing completion as a factual event, and the variety of rulings based on differing factual scenarios, it can be little more than guesswork for a property owner to know when completion has occurred, and thus when it should record a notice that is timely. If during the course of litigation the trier of fact decides the project was not quite complete at the time or recording, or was actually finished much earlier, otherwise invalid claims of lien may become valid. In practice, many owners do not bother with notices of completion because they are subject to so much retrospective modification. We suggest that a definite milestone be added to the definition of completion so that an owner may have a fixed moment on which to base its notice of completion. Our proposed milestone is the time at which the applicable authority gives the owner approval to occupy the building. We believe that that such a specific, easily verifiable date for completion would increase the utility and certainty of calculating lien recordation deadlines and decrease the amount of factually intensive litigation around issues of completion.

Association of California Surety Companies

925 L Street, Suite 220, Sacramento, CA 95814 (916) 441-4166

September 29, 2006

Mr. Nathaniel Sterling, Executive Secretary
California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, CA 94303-4739

Dear Mr. Sterling,

I am pleased to present to you the comments and suggestions of the Association of California Surety Companies to the Tentative Recommendation on the Mechanics Lien Law issued by the California Law Revision Commission.

It is apparent that the Tentative Recommendation is the result of many hours of study by many highly qualified and dedicated commission attorneys. For that work and dedication, we thank you.

The members of our association participated in company meetings and association meetings at which the latest memorandum of the commission on the mechanics lien law was studied.

We feel well qualified to provide input to the commission as to the effect of the provisions on surety companies operating in California.

Much of the input in our comments was provided by Charles Philipps, Esq. Charles has been representing surety companies and others involved in mechanics lien law cases for over 2 decades.

If there are any questions concerning our comments, please direct them to me at 916-441-4166, Bill Peterson at 605-977-7715, or Mr. Philipps at 415-927-9449.

Submitted by,

Jerry Desmond

Gerald J. Desmond, Esq.
Secretary/Treasurer

COMMENTS OF ASSOCIATION OF CALIFORNIA SURETY COMPANIES ON CALIFORNIA LAW REVIEW COMMISSION - MECHANICS LIENS

The Association of California Surety Companies applauds the commission on its simplification of the mechanic's lien law and the law for recovery on public works projects including stop payment notices and payment bonds. It is understandable that the input of sureties is necessary for the commission in that many of the provisions of the proposed law affect the surety industry which has significant interest in the construction industry in its facilitation of the construction process on public and private projects.

Some of the issues discussed below are not pertinent to sureties, but they are valid observations of the proposed law which is an attempt to balance the interests of all involved in the construction process so that the result is an overall fairness rather than favoring one player to the detriment of the others or *vice versa.*

PRIVATE WORKS

CHAPTER 1 DEFINITIONS AND GENERAL PROVISIONS

DEFINITIONS ARTICLE 1

Section 7016 defining labor, service, equipment or materials requires some rework as this is a new definition. This new definition should specifically exclude persons who merely advance funds for labor as provided by existing case law which excludes these potential claimants [See *Primo Team, Inc. v. Blake Construction Co.,* 3 Cal. App. 4th 801 (Cal. Ct. App. 1992)] and also exclude claimants which are not licensed contractors and which only supply workers for the project, pay the workers' wages and employment benefits, provide workers' compensation insurance, and are responsible for the workers' tax withholding. The latter would be a change in the law to overrule the decision in *Contractors Labor Pool, Inc. v. Westway Contractors, Inc.*, 53 Cal. App. 4th 152, 156 (Cal. Ct. App. 1997). Suggested language is a second sentence to the section: **"Persons who advance or lend funds for the payment of labor, or persons who supply workers for the project and are not licensed contractors, are not suppliers of labor for a work of improvement."**

Section 7026 adds a new subsection (b) which contains language overruling existing case law. [*Consolidated Elec. Distributors, Inc. v. Kirkham, Chaon & Kirkham, Inc.*, 18 Cal.

App. 3d 54 (Cal. Ct. App. 1971)] Section (b) provides that: **"Materials or supplies delivered to a site are presumed to have been used or consumed in the work of improvement. The presumption established by this subdivision is a presumption affecting the burden of proof."** This change could facilitate claims of dubious nature against sureties. Sureties do not have representatives on the project site as general contractors do. Sureties are not privy to the plans and specifications and the general project requirements for materials. Material supplier claims against payment bonds only arise when the general contractor is unable to resolve these claims, most often the result of the general contractor's insolvency. Therefore, sureties are not in the same position as general contractors to know if the materials for which payment is claimed were used in the project or were identified to the project but used elsewhere.

Under current law the claimant must prove that the materials were actually used in the project. The reason for the rule is based upon the basic underlying public policy of the right to a lien set forth in the state constitution so that the property owner would not be unjustly enriched at the expense of laborers and material suppliers. Proof of use in the project is not a great burden for material suppliers as shown by the court opinion in *Consolidated Elec. Distributors, Inc. v. Kirkham, Chaon & Kirkham, Inc.*, 18 Cal. App. 3d 54 (Cal. Ct. App. 1971).

It is not always true that goods delivered are used in the project. Many construction goods are fungible. This is especially true with respect to electrical materials such as wire, conduit, connectors, etc. These products can be used by the electrician on virtually any project. These products are also easily transportable from site to site. In analyzing payment bond claims, sureties and general contractors which might be liable for the cost of the materials if the subcontractor defaults in payment, often find that the cost of the materials supplied is far greater than it should have been for the work undertaken by the subcontractor. The current burden of proof is not excessive on suppliers if they keep competent records regarding the transaction which is as it should be. On the other hand, specialty items supplied to the project do not need this protection as the items can be easily identified from the plans and specifications. These are usually doors, hardware, lighting packages, larger electrical items such as panels and subpanels. In fact this is the evidence submitted in *Consolidated Elec. Distributors, Inc. v. Kirkham, Chaon & Kirkham, Inc.*, 18 Cal. App. 3d 54 (Cal. Ct. App. 1971) on which the court found for the claimant. This section (b) is not needed as it would overrule the current case law in California requiring that the materials must actually be used in the project which is the fundamental underlying basis of the constitutional protection for labor and material claimants. While the change in the law may be acceptable to general contractors, sureties do not have first hand knowledge or witnesses who can testify regarding the day to day activities on the project, the specific nature of the materials used therein or sufficient information regarding the plans and specifications to overcome or rebut the presumption

provided by the law, thus making every material supplier claim against a surety valid based on the presumption whether the claim is truly valid or not..

Subdivision (b) of §7062 is new and claims to be a clarification of the interrelation between the rights of claimants under the lien law and the rights of claimants under the bonds provided in the Subdivision Map Act. The new section reads **"This part does not limit, and is not affected by, improvement security provided under the Subdivision Map Act, Division 2(commencing with Section 66410) of Title 7 of the Government Code."** Sureties need clarification on this new language. Is the commission saying that on subdivision projects, claimants have rights under the new Part 6 and the Subdivision Map Act? Or is the commission saying that the new Part 6 does not control the improvement security posted under the Subdivision Map Act? The purpose of this subsection is not clear to sureties and the subsection needs to be explained or redrafted as sureties are involved on both of these issues. Rules for recovery on, and the release of payment security [not available under Part 6], under the Subdivision Map Act are not consistent with Part 6. Thus, sureties propose that Part 6 should state that it has no application to the recovery on the payment security given under the Subdivision Map Act.

NOTICE ARTICLE 4

Sections 7100-7116

In Article 4, commencing with §7100, the commission has made substantial changes to the notice provisions, including the manner, contents and address to which notices are given and has also considered notice by electronic means. These provisions apply to all notices on private works, not just to the preliminary notice.

Section 7106 (b) (5) is of interest to sureties as it provides the address to which notice are sent to sureties. The section reads **"(5) If the person to be notified is the principal or surety on a bond, at the address provided in the bond for the service of notices, papers, and other documents."** The commission's notes indicate that all bonds are required to contain this address information under C.C.P. 995.320. This is true. However, in practice not all bonds have the address or a place for the address on the payment bond. Many public works bonds are part of the specification package. These bond forms are prepared by the public agency or its architects. Under the proposed legislation there is no safe harbor provision to deal with this issue for claimants or sureties. Often claimants are not provided with a copy of the bond, even after a request for a copy, so whether the address is on the bond or not, it is not known to the claimant. Sometimes only the name of the surety is provided.. Further, this subdivision also applies to the principal on the bond. Seldom is the principal's address on the bond even though, admittedly, it is required by the bond and undertaking statute. There should be a safe harbor provision in the statute which serves sureties and claimants such as contained

in current Civil Code §3227 which the commission has abandoned. Section 3227 has worked well for both claimants and sureties. The reason for this significant change is not explained. Furthermore, the word "principal" should be removed from this subsection (b) (5) as the principal's address in seldom on the bond

BONDS ARTICLE 6

Sections 7140-7144

Section 7140 specifically makes the Bond and Undertaking Law (C.C.P. 995.010 et.seq.) applicable to Part 6. This is the current state of the law, however, an exception should be made just as provided in the Probate Code §8487 that **" Except to the extent this Part is inconsistent . . ."**

Section 7142 "Release of Surety from Liability" is a restatement of the current Civil Code §3225. However, the title of this section is a misnomer. This section does not release the surety of liability, rather it sets forth what will **not** release the surety. The title should be rewritten to indicate that there is "No Release of Surety from Liability". Note that this provision applies all bonds mentioned on Part 6 including the payment bond, stop notice bond, release of stop notice bond or release of mechanic's lien bond. Is this really the intent of the commission? Or should this section more properly only apply to the payment bond? .

Section 7144 "Construction of bond" is again a restatement of current §3226. But here is the problem. Read literally, the current statute as well as the proposed statute states **"The sole conditions** [sic] **of recovery on the bond are that the beneficiary is a person described in Article 1 (commencing with Section 7400) of Chapter 4 and has not been paid the full amount of the claim."** The problem here is that this section applies to a payment bond, a stop notice bond, a release of stop notice bond or a release of mechanic's lien bond. However, it makes little sense when applied to a stop notice bond as the claimant there is the lender who is not a person described in §§7400 et. seq. Strict interpretation of this statute would make the recovery on a release of stop notice bond or release of mechanic's lien bond unconditional to an unpaid claimant. This means that even if the claimant did not give the requisite preliminary notice, it could recover on the payment bond or a release bond. In other words, even if there was a complete defense to the payment claim, mechanic's lien claim or stop notice claim due to lack of a preliminary notice, the claimant could still recover. This is not the intent of the law. Section 7144 [3226] conflicts with the statutes providing for recovery on a payment bond that a preliminary notice is required in certain instances, recovery on a release of lien bond, i.e., §7428 that "the bond shall be conditioned on payment of any judgment the claimant recovers on the lien." There are conditions for recovery on the lien

including the giving of the preliminary notice and proof that the materials, etc. were used in the project. Then how can §7144 mandate that there are no conditions for recovery on the release of lien bond? The same is true for a release of stop notice bond §7510. A similar result would occur for a payment bond when the claimant is required to give a preliminary notice or a notice under §7612(b). The inescapable conclusion is that this section as originally drafted was poorly worded and should be rewritten to state that: ". . . the sole conditions of recovery are that the claimant has complied with all of the provisions of Part 6 applicable to the claim and that the claimant has not been paid the full amount of the claim for labor, service, equipment or material."

COMPLETION ARTICLE 7

Sections 7150-7156

This area is a problem for both sureties and contractors. The Notice of Completion is important because the notice commences the time for claimants to act. The proposed statute, Section 7152, extends the time for recording a notice of completion from ten (10) days after actual completion to fifteen (15) days. Current case law provides that if the Notice of Completion is not recorded within the statutory time the notice is void and ineffective. The ten-day period was too short. In fact, Caltrans stopped recording notices of completion a number of years ago because it could not record within the ten days. Fifteen days may not be long enough either. Twenty days would be better. Section 7152(b)(1) is too limiting in the need for the information on the Notice of Completion in the case where the Notice of Completion is only for completion of a particular portion of the work. The information in Section 7152(b)(1), i.e., the name of the direct contractor and a description of the work, should be on all Notices of Completion.

Section 7156 of the proposed law provides that the owner must "give" a copy of the notice to the direct contractor and anyone who has given the owner a preliminary notice. This section does not apply to owner-occupied residences of four or fewer residential units. The first problem with this statute is that it is not clear if it follows the notice rules of §7100 et. seq. The use of the word "give" is strange. Should be changed to ". . . shall provide notice of the recording of a notice of completion in accordance with §7104 by providing a recorded copy to . . ." Additionally, this notice provision will not be followed because it is cumbersome in the manner of service and the fact that service of the recorded notice must be given immediately. Many recorded notices of completion will be declared void because no immediate mailing was performed. The notice must be given in accordance with §7108, certified or overnight delivery. Service aside, at a minimum ten days should be given as the period for mailing the recorded notice. The solution to this dilemma is to write the statute in the alternative, i.e., either record the

notice of completion or provide notice of the notice of completion, whether recorded or not, under §7104-7108.

CHAPTER 4 MECHANICS LIEN

Section 7428 Release Bond [mechanic's lien]

The only change in the proposed statute is to reduce the amount of the bond from 150% of the claim of lien to 125% to be consistent with the stop notice release bond amount. The reason is to have consistency in the statutes. Surety experience is that by the time lien claims released by bonds are litigated that the total amount due on the lien, including interest is closer to the 150% amount. The reason for the 125% release bond on stop payment notices is that 1255 of the claim is the precise amount withheld on stop notices. No money is withheld on a mechanic's lien.

AMOUNT OF LIEN ARTICLE 3

Sections 7430-7434. There are no substantive changes in these sections but the current law is not in the spirit of the original intention of the mechanic's lien provision in the state constitution was to provide that the property owner would not be unjustly enriched at the expense of laborers and material suppliers. The mechanic's lien remedy is equitable not contractual. Therefore, damages for claims based upon contracts, such as rescission, abandonment and breach of contract do not have any place in the lien law. Property should not be subject to liens or judgments based on liens which arise out of contract disputes between direct contractors and their subcontractors or suppliers. Direct contractors need not worry because they have contractual rights with the owner which can be pursued irrespective of the mechanic's lien law. Turning the mechanic's lien law into the status of a contract claim is totally contrary to the constitutional mandate of the mechanic's lien right.

California Constitution Article XIV § 3. Mechanics' liens

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.

If the statute is intended for some other purpose, i.e., to allow recovery for labor and materials in spite of a rescission, abandonment or breach of contract, that is within the spirit of the lien law, but the section is poorly drafted if that is its intent.

GENERAL PROVISIONS ARTICLE 1

Section 7502(b) changes existing law to add as damages which can be included in a stop payment notice ". . . an amount due as a result of rescission, abandonment, or breach of contract." This conforms the stop payment notice remedy with the mechanic's lien remedy on these damages. See comment above under §§7430-7434.

Section 7506(b) specifies to whom the stop payment notice to the lender should be sent. The pertinent language is: **" . . . shall be given to the manager or other responsible officer or person at the office or branch of the lender administering or holding the construction funds."** Locating the branch or office of a construction lender in California is a difficult proposition.. Most national banks do not handle construction loans at a branch or office open to the public. Somewhere in the bowels of the bank, often out of state, resides the construction loan servicing department. Considering that if you give the notice to the wrong branch or office, the stop payment notice is ineffective, makes this notice provision draconian. This section also internally conflicts with §7106 which requires notice to be given to the lender at the address shown on the construction loan agreement or the construction deed of trust. This is also problematic. No claimant will obtain the construction loan agreement short of a subpoena. The construction deed of trust would require a visit to the recorder's office. A great number of subcontractors and material suppliers are just not that sophisticated to obtain the exact address to which the stop payment notice is to be given. If the stop payment notice contains all of the information mandated by §7102, the construction lender should have no problem identifying the construction loan. Just consider the fact that sureties receive claims every day without a bond number. If the information mandated by §7102 is provided, the surety should have no problem locating the bond file. Compare if the statute required a claimant on a payment bond to serve the claim on the manager, etc. of the branch office of the surety which issued the bond or forfeit its claim on the bond. My guess is that there would be an uproar. I see no difference with the notice to the lender on a stop payment claim.

Section 7510 Release bond [stop payment notice]

The commission has clarified the law by requiring an admitted surety insurer to conform to the release of lien bond statute. However, in drafting 7510(b), the commission (apparently unintentionally, as the Commentator's notes do not discuss the removal) removed the following language from the current law**". . . not exceeding the penal obligation of the bond . . ."** This language must be reinserted in the proposed statute.

ENFORCEMENT OF CLAIM STATED IN STOP PAYMENT NOTICE ARTICLE 5

Sections 7550-7560. These sections are a restatement of existing law with minor non substantive changes. The commission has asked for comment on the five (5) day notice of the commencement of an action on a stop notice, i.e., whether it should be mandatory. If mandatory, this notice would be another draconian reason to defeat stop payment notice claims by lenders. Current case law supports this section a directory only. **The obvious reason (which is not discussed by the commission) for the five (5) day notice is to alert the owner or lender than suit has been filed on the stop payment claim. Otherwise, after the expiration of the time to sue on the stop payment notice, the lender or owner could disburse the funds to the direct contractor. With this notice either would do so at its peril.**

PAYMENT BOND CHAPTER 6

Sections 7600-7612. The commission comments that it has not made a substantive change in the language of current Civil Code §3235 & 3236, but it did by interpreting the current law to require that the owner record both the contract and the bond prior to commencement of work. There is no problem with recording the contract prior to the commencement of work, but recording the bond before commencement will take real planning and foresight. This is especially true in view of the definition of commencement provided in §7003(a). Bonds, if requested, invariably follow the execution of the contract in the scheme of things are rarely delivered to the owner before commencement of the work. Compare current Civil Code §3240 which allows the surety to record the bond before completion. What we need here is some time frame for the owner to record the bond. Perhaps within thirty days of commencement or within thirty days of receipt of the bond whichever is later. After all, most construction projects which are bonded have a duration of six months or more. Additionally, the recording of the payment bond should also satisfy the requirement of the surety under §7610.

In section 7610, the commission has retained the right of the surety to limit the statute of limitations to six months after completion of the work but only if the bond is recorded conditioned upon the bond being recorded before completion, i.e., current Civil Code §3240. Sureties support this but also suggest that the requirements and rights of this section should be available to the surety as against any claimant, if the owner provides, in accordance with the notice provisions of this Part, a copy of the payment bond to the claimant who gave the owner a preliminary notice and who in turn is provided with a copy of the payment bond prior to completion of the work of improvement.

Section 7612 retains the notice prerequisites to enforcement of a bond claim under the current law of either a preliminary notice or the late notice under Civil Code §3242. Sureties are not in favor of continuing the provision for the late notice as it is totally counter intuitive to the framework of the lien and payment bond law. The purpose of the preliminary notice is so that the owner and direct contractor know who is supplying labor and material to the project and so that each may take the appropriate steps to make sure that all in the downstream chain are paid. To allow a material supplier to a subcontractor or a subcontractor to recover payment by giving a notice long after the debt became due without any other notice is not equitable. Under the current rule, a material supplier could provide materials in January of 2005, not be paid, know that it has not been paid, and then in June of 2006 give a notice that it has not been paid and recover from the direct contractor the amount due after the direct contractor has paid the subcontractor **in full** shortly after the direct contractor's receipt of payment from the owner upon completion. keeping in mind that the direct contractor must comply with the prompt payment statutes. If this claimant knew that it was not paid and the account was 90 overdue, there has to be some responsibility and obligation on the part of an unpaid party to present its claim at an earlier date than 15 days after a recorded notice of completion or 75 days after completion. Compare the Miller Act (Federal Projects) notice required 90 days after last supplying labor or material.

PROMPT PAYMENT STATUTES CHAPTER 8

ARTICLE 1 PROGRESS PAYMENT

Sections 7800-7822 govern prompt payment of progress and retention payments among owners, direct contractors and subcontractors on private works and works contracted by public utilities. Prompt payment statutes are to encourage, if not mandate , that the construction funds flow down the construction ladder in a timely fashion. Sureties are not part of this scheme as sureties do not receive funds from owners and are not part of the ladder or flow. Sureties only become involved when someone has not paid in accordance with the scheme. Simply put, the public policy behind the prompt payment

statutes has no application to sureties who are governed by independent rules for the handling of claims under the insurance code. Therefore, so that there is no misunderstanding on this issue, the sureties suggest an added §7804 "This chapter does not apply to, or create any liability, against any surety which provides a bond, or on any bond provided by a surety, pursuant to Part 6 of Division 4 of this Code."

PUBLIC WORK OF IMPROVEMENT

CHAPTER 2 GENERAL PROVISIONS

ARTICLE 1 MISCELLANEOUS PROVISIONS

Section 42020 is of interest to sureties. Subdivision (a) of this section repeats the verbiage in the private works statutes that: **"This part does not limit, and is not affected by, improvement security provided under the Subdivision Map Act, Division 2(commencing with Section 66410) of Title 7 of the Government Code."** Again, the exact meaning and intent of this section is not clear. What sureties require is a clear statement that "**This part does not apply to an improvement security, etc."** If that is the intent. Subdivision (b) repeats the verbiage in the private works statutes that: **"The Bond and Undertaking Law (C.C.P. 995.010 et.seq.) applies to a bond given under this part**. Once again, we recommend that the phrase **"Except to the extent this Part is inconsistent . . ."** be added to the beginning of this subsection.

Section 42030 sets forth who may use the remedies of a stop payment notice and payment bond claim. Once again, we recommend that language be inserted to eliminate .

"Persons who advance or lend funds for the payment of labor or persons who supply workers for the project and are not licensed contractors may not give a stop payment notice or assert a claim against a payment bond under this part or any other provision of this code that provides for a payment bond."

Section 42010 " Liability of surety" is the same verbiage as is contained in §7142 for private works discussed above. Note that this provision applies all bonds mentioned in this Part, i.e., the payment bond and release of stop payment notice bond. Is that the intent of the commission?

ARTICLE 2 COMPLETION

Sections 42210-42230 forth the events constituting the completion of a public work. These events are taken from the current law which unfortunately is not a model of clarity. Sureties believe that the proposed law may need some work. Additionally, the commission completely eliminated the concept of a recorded Notice of Cessation of Work on a public work. This should be corrected by adding " or cessation" in §§42220 and 42230 wherever the word "completion" appears and adding a subsection (c) to §42210 making the recordation of a Notice of Completion or Cessation, the completion of a public work. Subsection (b) containing the 30 day period should be extended to 60 days. Notices of Cessation are used by sureties to commence the time period for filing stop payment claims and bond claims when there is a performance default on a public work project.. Usually, a new contractor is engaged to complete the work. The Notice of Cessation brings a conclusion to the previous contract. See W.F. Hayward Co. v. Transamerica Ins. Co., 16 Cal. App. 4th 1101 (Cal. Ct. App. 1993) for the effect of a work cessation. A recorded notice is preferred as it would protect the suppliers of labor and material by actually giving notice of the cessation.

Under the proposed statute, the recording of a Notice of Completion has no effect on the time to bring claims. Therefore, recording a notice of completion on a public work is discretionary and accomplishes nothing. If this is the case, why is it in the statute at all? It will only create confusion as many public entities record notices of completion long after the work is actually finished.

CHAPTER 4 STOP PAYMENT NOTICE

ARTICLE 1 GENERAL PROVISIONS

Sections 44110- 44180 are consistent with current law for the filing of a stop payment notice with the public entity and other related stop payment issues relating to withholding of funds and time deadlines. This article also provides for the filing of a release of stop payment bond, discussed below. There is one disconnect in this statutory scheme. Section 44140 "Time for giving notice" which should be "Time for filing stop payment notice" refers to the time period of 30 days based upon the recordation of a Notice of Completion. However, as discussed above, the recording of a Notice of Completion is not an event of completion under §42210. One of these statutes must be amended to conform. The recommendation above that a subsection (c) be added to §42210 might do this.

Section 44180 provides for the filing of a release bond on a stop payment claim. This is simply a restatement of existing law. The statute is still discretionary on the part of the public agency to accept a release bond. Some public agencies do not. This should be mandatory. The bonds are issued by admitted surety insurers and the money withheld belongs to the direct contractor, not the public agency, so why the discretion?

ARTICLE 2 SUMMARY PROCEEDING FOR RELEASE OF FUNDS

Sections 44210- 44280 are restatements of current law except that the comments indicate that the court hearing the proceeding sits without a jury. If that is the case, then §44270 (b) needs to be re-written to take out the word "If" at the beginning of the subsection.

CHAPTER 5 PAYMENT BOND

Sections 45010 - 45090. These sections are a restatement of existing law. The commission has requested comment on §45020 which is titled "Consequences of failure to give bond". The introductory phrase is "If a payment bond is not given and approved as required by statute." This section is acceptable to sureties. However, sureties have experienced too many public works on which products other than the mandated surety bonds have been used to avoid obtaining the statutorily required bonds. Sureties wish the commission to consider an additional subsection to eliminate this growing practice.

ISSUES ON WHICH THE COMMISSION REQUESTED COMMENT WHICH ARE OF INTEREST TO SURETIES

1. ATTORNEYS' FEES ON ENFORCEMENT OF MECHANIC'S LIENS

The original intention of the mechanic's lien provision in the state constitution was to provide that the property owner would not be unjustly enriched at the expense of laborers and material suppliers. The mechanic's lien remedy is equitable, not contractual. Under the so called "American Rule" attorneys' fees are borne by the party engaging the attorney unless a contractual provision between the parties provides otherwise. The other exception is if an award of attorneys' fees is allowed by statute. Since, as between most lien claimants and the owner, there is no contractual relationship, there is currently no basis for an award of attorneys' fees to a successful lien claimant nor should there be in light of the underlying purpose of the mechanic's lien. Direct contractors and suppliers may have a right to attorneys' fees against the owner, if the contract between them so provides. However, any attorneys' fee award is not on the lien but on the contract. In addition because there is a contractual relationship, any judgment against the owner is personal, i.e., it can be enforced against any property of the owner. This is not true of a mechanic's lien taken to judgment. It is not a personal judgment, but a judgment "*in*

rem" and can only be enforced against the property. Attorneys' fees have nothing to do with labor and material provided to the project. They do not increase the value of the land or provide the owner with an unjust enrichment which is the underlying constitutional basis of the lien.

California Constitution Article XIV § 3. Mechanics' liens

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.

A statute providing for the recovery of attorneys' fees in an action on a mechanic's lien could be unconstitutional as the constitution limits the lien to the value of the labor and material furnished. An award of attorneys' fees in an "*in rem*" action could only be enforced against the land because it is not a personal judgment. This is the reason that attorneys' fees are not currently included in the statutory scheme. Indeed, this very concept of attorneys' fees was discussed in *Abbett Electric Corp. v. California Fed. Savings & Loan Assn.*, 230 Cal. App. 3d 355, 358 (Cal. Ct. App. 1991) wherein the court concluded: **Attorney's fees are not available to a prevailing litigant absent a contractual agreement or statutory authorization, and no statute provides for**

attorney's fees in mechanic's lien foreclosures. (Wilson's Heating & Air Conditioning v. Wells Fargo Bank (1988) 202 Cal.App.3d 1326, 1329-1330 [249 Cal.Rptr. 553].) "Although the statutory scheme [for mechanic's liens] originally provided for the recovery [*4] of attorney's fees by the successful lienholder, this provision of the statute was declared unconstitutional (Builders' Supply Depot v. O'Connor (1907) 150 Cal. 265, 268 [88 P. 982]) and no similar provision has been subsequently enacted . . . . It is thus black letter law that except for any cause of action on a contract between the lien claimant and the owner of the improved property which provides for fees, a lienholder has no entitlement to them from the owner . . .**

2. FIVE DAY NOTICE AFTER COMMENCEMENT OF STOP PAYMENT NOTICE PROCEEDING

The obvious purpose of the five day notice is to prevent the lender, owner or public entity on which the stop notice was served from disbursing the funds on the basis that the stop notice enforcement period has expired. See Civil Code §3210 ". . .No money or bond shall be withheld by reason of any such notice longer than the expiration of such 90-day period unless proceedings be commenced in a proper court within that time by the claimant to enforce his claim, and if such proceedings have not been commenced such notice shall cease to be effective and the moneys or bonds withheld shall be paid or delivered to the contractor or other person to whom they are due." Thus, the claimant has no one to blame if the funds are disbursed because the claimant failed to give the five day notice. To make the notice mandatory would turn the policy upside down. It would defeat an otherwise potentially valid claim. The purpose of the statute is to protect the claimant not to defeat the claim. The service of the summons and complaint itself might not due this as a summons and complaint would probably be required to be served on a representative of the lender or public entity which is not the same representative who is required to receive the stop payment notice.

3. REQUIREMENT THAT OWNER PROVIDE COPY OF BOND TO EACH POTENTIAL CLAIMANT

This might be a good procedure if the surety received the benefit of the shorter statute of limitations of six months regardless of whether the bond was recorded. It is of no advantage if the bond must be recorded as the proposal is to extend the six-month statute of limitations day for day for each day that a copy of the recorded bond is not provided to a potential claimant who has provided a preliminary notice. In the real world, few if any owners ever record payment bonds. This is especially true, because to take advantage of the shortened period of time, the bond must be recorded prior to the commencement of work. I doubt that most owners would even have the bond prior to commencement.

4. THIRTY DAYS VS. SIXTY DAYS CESSATION OF WORK AS COMPLETION

I do not see any valid reason to have a different period of cessation on a public work (30 days) as opposed to a private work (60 days) which constitutes completion.

5. NOTICE OF CESSATION ON PRIVATE AND PUBLIC WORKS

The commission has eliminated the provision for a recorded notice of cessation on private and public works. This is unfortunate. Upon a contractor's default in performance on a bonded public or private project, I often have the owner record a Notice of Cessation to start the lien period. However, note that some public entities will not do this because the current law is not clear that the Notice of Cessation applies to

public works. This situation can be corrected by adding "or cessation" in §§42220 and 42230 wherever the word "completion" appears and adding a subsection (c) to §42210 making the recordation of a Notice of Completion or Cessation completion of a public work. Subsection (b) containing the 30-day period should be extended to 60 days. As indicated, Notices of Cessation are used by sureties to commence the time period for filing stop payment claims and bond claims when there is a performance default on a public work project. Usually, a new contractor is engaged to complete the work. The Notice of Cessation brings a conclusion to the previous contract. See W.F. Hayward Co. v. Transamerica Ins. Co., 16 Cal. App. 4th 1101 (Cal. Ct. App. 1993) for the effect of a work cessation. A recorded notice is preferred as it would protect the suppliers of labor and material by actually giving notice of the cessation. The same is true on private works.

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Thursday, September 28, 2006

Via Express Mail, Saturday Delivery

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, California 94303-4739

Comments, *Revisions of California Mechanics Lien Law*

Dear Gentlepersons:

I write with comments about the proposed revisions to the California Mechanics Lien Law that is the subject of the Commission's Tentative Recommendation, #H-821 issued in June 2006.

I have read through the report and comment from the perspective of a lawyer who principally represents subcontractors involved in California commercial, industrial and multi-unit residential projects and all types of contractors and owners in Bay Area consumer/owner-builder residential projects for some years.

On the whole, I applaud the work of the Commission. It is well thought out and seeks to resolve the diffracted nature of California's Mechanic's Lien Law – without the wholesale adoption of a new system of enforcement.

That said, there remain issues that limit the efficacy of the remedies provided.

These issues are grounded in the legal matrix stated by Justice Croskey in ***Solit v. Tokai Bank*** (1999) 68 Cal.App.4th 1435 [81 Cal.Rptr.2d 243]. In *Solit*, Justice Croskey explains the distinction between the concept of *"Inchoate Lien Rights"* and the existence of a *"specific Lien,"* under the mechanics lien law and its constitutional precedents.

It is this "liberally protected," constitutional, *"Inchoate Lien Right* that guides my comments today about the proposed revisions to the current law.

First some specific responses to the Commissions invitation to comment:

Mail - - - expect it to take a week. Be surprised when it takes only three days.

Most major contracts now call for correspondence by facsimile. That said, many are now moving to internet transmittal of PDF forms. Many of the newer, major projects now provide for such correspondence as agreed means of communication.

Fax machines are widely used <u>between contractors</u> in residential construction, but communication with the owner, at all levels, remains via mail or personal delivery.

Acceptance by Public Entity

This provision is beneficial to the contractors who perform street utility work on projects, and as noted, owners who want repairs by the contractors. It has been used by dilitory contractors to

extend the time to file their lien claims. What is really necessary is a means to notify those contractors who have issued Preliminary 20 Notices ["pre-liens"] to the Owner of their lien rights, that the work is complete. That provides the opportunity to protect their rights.

Separate Contracts on a Single Job

This is a not a problem where the "Single Job" is a specifically defined "Work of Improvement," in a contract (a large portion of interior fit-up in an industrial building, for example, or a separate lot in a subdivision). But it creates havoc in circumstances where the separate contracts are for work in the same integrated work of improvement that is *not subject to reduction to possession* because the other trades have to finish their respective portions of the work as a whole. It is that element that ought to control.

Contract Change

I am involved in enforcing and defending delay claims and claims for contract revisions that usually have revised the contract sum by the 5% or more. I agree that notice is rarely given and even if it is, it does not seem to have any self-actuating legal effect.

Some lenders do put a provision in the construction loan documentation that failure to provide such a notice gives them rights to cut off loan advances until compliance with the terms of the construction loan, new fees for Lenders' consent and the like. But that is not a function of the Mechanics Lien Law, it is a protective provision placed in the law for the perceived purposes of the benefitted class – Lenders.

Erratum: Footnote 84 the citation to *Marsh* appears to be incorrect. The § referred to in the current edition is §4.13 et seq.

Attorneys Fees, at Page 35.

I think this would be a restriction on claimant's inchoate lien rights. Yes, where there is a bad lien. But even though it may be beneficial to claimants, it will also serve as a risk management stop on the decision to seek enforcement. Usually the Owner [large projects] and the Lender have a lot more bucks to burn than the contractor. Perhaps a restriction to residential property so the owner has a shot if he beats an unscrupulous contractor?

Expedited Release

My trouble here is the issue found in ***Solit, infra.*** In the effort to provide the title companies a way to rid the property of unwanted and unenforceable claims, the statute ought to recognize it is dealing with the specific lien. It is not stated that the remedy is only to the specific claim of lien.

Stop Notices – Private Work

Whatever the process, it should be a replication or "mirror image" of the Lien Notice provisions. Special notices due to the "augmented" nature of Stop Notices, in general, are traps for the unwary. As a practical matter, most small contractors do not venture into this area. The

consequences of error are just too overwhelming from a cost, time and consequences of mistake risk analysis. Large material suppliers, major trade contractors on commercial, industrial, or multi-unit construction have the staffs and legal help to make these kinds of claims – and even some of them fail at the process. Public work should stand on its own, as the Commission proposes.

Notice of Cessation

This is lodged in the Public Works area, that I am not going to comment on – other than to say the division of the Public Works provisions belong in the Public Contracts Act. As to the change of the time for cessation on private work – it should stay at 60 days. Any shorter time puts contractors at risk of owners that would use it as a ruse to cut off the inchoate rights promised by the State Constitution.

Additional Errata

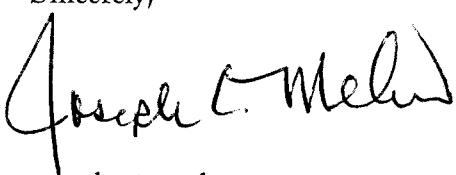
Footnote 117 refers to Miller & Starr Vol 10. That should be Vol. 12.

Notice to Lenders

A pet peeve. The consequences of the failure to Notice unknown [or purposely undisclosed] Lenders falls squarely on the contractors. Not on the Lenders. Not on the Owners, or even on the Prime Contractors. It falls on the "least-able-to-get-the-information-crowd," the subcontractors. Information that if they can't get it from project records, denigrate their lien rights by making the information necessary to their respective Pre-Lien Notices their absolute responsibility. Do or Die! Each of the statutes [existing and proposed] that provide for notice to the contractors about the Lenders has an escape clause that makes the contractors the class of persons who must search the record [or pay for the privilege of having some title company do so] for the information the Owner and the Lender have failed to provide. That is not fair. Make it a requirement, but make it the obligation of the Owner, the Lender and the Prime Contractor ["Direct" in this context is meaningless as they are usually in the burdened class] to provide the sub-contractors with the appropriate information, or notice to the Lender should be waived.

Thanks for listening, I wish you success in your venture – so long as my small and medium sized contractors don't get burned in the process.

Sincerely,



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FILE NO.: 0001.002

September 30, 2006

VIA ELECTRONIC-MAIL AND U.S. MAIL

California Law Revision Commission
4000 Middlefield Road, Room D-1
Palo Alto, California 94303-1335

Re: Comments on the Tentative Recommendation of the California Mechanics Lien Law and Associated Construction Remedies

Dear Committee Members:

Gibbs, Giden, Locher & Turner LLP ("GGLT") is pleased to submit comments on the California Law Revisions Commission's ("Commission") tentative conclusions regarding revisions to the California mechanics lien law and associated construction remedies.

We have attached a detailed memorandum which addresses the changes to the following areas of the mechanics lien law: (1) Notification; (2) Commencement and Completion; (3) Waiver and Release; (4) Miscellaneous Matters; (5) Preliminary Notice; (6) Mechanics Lien; (7) Invalid or Unenforceable Claim of Lien; (8) Stop Payment Notice; (9) Payment Bond; (10) Other Remedies; (11) Public Works Contract General Provisions; (12) Preliminary Notice for Public Works Contracts; (13) Stop Payment Notice for Public Works Contracts; and (14) Payment Bond for Public Works Contracts.

Additionally, we wished to highlight some of our comments:

1. The numbered sections chosen by the Commission (Civ. Code § § 7000-7848) are identical to the numbered sections of the existing Public Contracts Code and Business and Professions Code that are used in conjunction with the mechanics lien law and related construction remedies. We propose a new numbering scheme that does not overlap with existing sections to eliminate ambiguity amongst those who frequently utilize those Code sections.

2. Combine California Civil Code § § 7104 and 7110 to expand the manner in which notice may be given to include providing an "electronic record" if the person has agreed to receive the record by electronic means. It may also be helpful to require Owners to include electronic-mail addresses on all building permits.

3. California Civil Code § 7102(a)(6)(iii) is confusing and creates an ambiguity regarding the "statement or estimate of the claimant's demand, after deducting all just credits and offsets" between what is required in a preliminary notice and an actual lien or claim, which requires a more specific amount. We believe that Section 7102(a)(6)(iii) needs to be clarified to be consistent with Commission's goals.

4. Create a single Preliminary Notice statute for both public and private works of improvement.

5. California Civil Code § 7003 as written is confusing inasmuch as it is difficult to determine whether or not commencement occurs when materials are delivered to the site, or when materials are consumed in the work of improvement. Our revised section would read: "Material or supplies *intended to be* used, consumed, or incorporated in the work of improvement, are delivered to the site.

6. The Commission sought comment on whether or not California Civil Code § 7150(b) should remain a part of the statute. It is GGLT's opinion, with the Commission's goals of simplifying and clarifying the statutory scheme, that this section should be eliminated because the provisions of Section 7150(a) adequately define completion and provide a single statue to define completion.

7. The Commission also sought comment on whether or not California Civil Code § 7154 should remain a part of the statute and it is GGLT's position that this section does effectively serve the purpose of narrowing an owner's liability and allowing a contractor or subcontractor to receive its retention.

8. GGLT believes that California Civil Code § 7460's requirement that a claimant must record a notice of pendency of the action ("lis pendens") within 100 days after recordation of the claim of lien should be eliminated. Instead, we believe that the law should remain as it is: a claimant *may* record a lis pendens, should it desire to protect its lien priority.

9. The Commission sought comment concerning whether attorneys fees should be awarded to the prevailing party in an action to enforce a lien claim. GGLT recognizes that including an attorneys fees provision may lead to the earlier resolution of mechanics lien disputes while also serving as a disincentive for

claimants pursuing invalid claims and for owners fighting valid claims. Should the COMMISSION decide to include such a provision, it may be prudent to carve out an exception for single family homeowners, to protect the homeowner, and to establish a limit for the lien amount.

10. GGLT also proposes to either eliminate California Civil Code § 7550(c) altogether, or extend the time period by which a claimant shall give notice of commencement of the action from five days to at least ten days such that the stop payment notice is not invalidated, which insulates the lender.

11. GGLT believes that California Civil Code § 7004(b) should except out any escrow account set up under § § 7700-7730, et. seq.

12. GGLT proposes to change the language in California Civil Code § 7488(c) from: "The prevailing party is entitled to a reasonable attorney's fee" to *Attorney's fees shall be awarded to the prevailing party.*

13. California Civil Code § 7612(b) should reference § 7104 to prevent "secret" liens.

14. The language in Public Contract Code § 45090(a) should be changed from: "....to the direct contractor or one of the direct contractor's subcontractor" to *the direct contractor or subcontractors*. Former Civil Code § 3267 was unclear, and the recommended Section 45090(a) remains unclear.

15. GGLT proposes to change the title in California Civil Code § 7832 from "Stop work notice" to either *Work Cessation Notice* or *Suspension of Work Notice* to avoid ambiguity.

16. GGLT proposes to include the direct contractor's subcontractor in the list of entities that will not be liable should the direct contractor properly give a stop work notice in California Civil Code § 7838(a).

17. California Civil Code § 7844 should contain a detailed procedure by which an "expedited proceeding" can be obtained and indicate whether or not it specifically supersedes a binding arbitration proceeding.

18. Public Contract Code § 44150's language should be changed from a "public entity's reasonable cost of litigation" to 125% of the claim such that it is consistent with the amount if an entity bonded around the stop payment notice. Additionally, it may be prudent to identify the mechanism by which funds may be released.

19. The public entity's "discretion" should be eliminated from Public Contract Code § 44180 to require the public entity to allow a direct contractor to provide a release bond, should the direct contractor disagree with a claim stated in a stop payment notice.

We appreciate the opportunity to provide GGLT's comments and look forward to your ultimate revisions of the mechanics lien law and associated construction remedies. As we stated in the attached Memorandum, we stand ready to assist the Commission in this highly important task and we look forward to a further opportunity to review the proposed legislation before it is forwarded to the Legislature for its consideration. In the interim, should you desire any further comment or discussion on any of our comments, please do not hesitate to contact me.

Very truly yours,

John F. Heuer, Jr.
of GIBBS, GIDEN, LOCHER & TURNER LLP

Enclosure
cc: Kenneth C. Gibbs, Esq.

GIBBS, GIDEN, LOCHER & TURNER LLP

TO: California Law Revision Commission

FROM: John F. Heuer, Jr., Esq.; Glenn E. Turner, Esq., James D. Lipschultz, Esq., Richard J. Wittbrodt, Esq., Barbara R. Gadbois, Esq., Michael I. Wayne, Esq., Michael A. Scherago, Esq., Tomas A. Kuehn, Esq., Brendan P. Penney, Esq., Christopher E. Ng, Esq., Joanna M. Curtis, Esq., Victor F. Luke, Esq., Steven J. Massetti, Esq., Lynn A. Mastandrea, Esq.

DATE: September 30, 2006

MATTER: California Law Revision Commission
Tentative Recommendation – Mechanics Lien Law (June 2006)

SUBJECT: Comments of Gibbs, Giden, Locher & Turner LLP to Commission's Tentative Recommendations

CC: Kenneth C. Gibbs, Esq.
William D. Locher, Esq.

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1. Introduction

a. About Gibbs Giden Locher & Turner LLP

Founded in 1978, Gibbs, Giden, Locher & Turner LLP provides, among other things, full legal service to all levels of participants in the construction industry from public and private owners, architects, engineers, construction managers, prime contractors, subcontractors and material suppliers. Recently, Gibbs, Giden, Locher & Turner LLP was recognized by Chambers USA as the "top construction law firm headquartered in Southern California." The firm is a recognized and established leader in the construction industry.

b. General Comments and Recommendations

We applaud the California Law Revision Commission ("Commission") and all those who have participated in drafting the proposed comprehensive revision of the California Mechanics lien law. The goal of simplifying the existing statutes, while making substantive changes where consensus is that change is desirable, is noble indeed. Based on our review of the proposed statutory scheme and the conforming revisions that are contemplated, we believe that the Commission has achieved a good part of its goal. However, we also believe that there remain issues with the current mechanics lien law that are perpetuated by the proposed changes. Further, we believe that there are ambiguities or potential ambiguities that exist in the newly proposed scheme which should be clarified. Lastly, we believe that there are substantive changes that have been made, whether intentionally or unintentionally, that, in our opinion, are changes that are either undesirable or lack the consensus of those that occupy the industry.

Accordingly, and most respectfully, it is our recommendation that the Commission consider our comments that follow, together with the many other comments we expect will be, or have already been, received and, thereafter, issue further tentative recommendations for additional comment after additional drafting has been performed. Given the importance of the statutory schemes applicable to mechanics liens, stop payment notices, payment bond claims, etc., and the underlying Constitutional authority for mechanics lien rights, we believe that any substantial revisions to these schemes such as the revisions proposed by the Commission, should limit as best as is possible further ambiguity and confusion.

c. Organization of Comments and Recommendations

The organization of this Memorandum is patterned largely after the organization reflected in the Commission's Tentative Recommendation of June 2006. To the extent there are general comments about the proposed revisions, we've included those comments. Otherwise, the specific comments that follow reflect both complimentary and, at times, critical assessments of specific provisions of the newly proposed statutes.

2. Comments and Recommendations

a. Notification

i. General Comments.

The proposed recommendations of the Commission with respect to Notice are generally in line with the Commission's stated purpose of simplifying and clarifying the statutory scheme in this area; however, there are areas of potential confusion and ambiguity that should be addressed before further action is taken to enact changes to the lien law.

ii. Specific Comments and Recommendations

(1) Potential confusion and ambiguity resulting from uniform requirements for notice.

(a) Absence of cross-referencing

The Commission has recommended that all notices under the proposed revisions to the lien law be uniform in the information that is contained within those notices. (See, Proposed Civil Code §7100; et seq.) The purpose of this change, according to the Commission, is to eliminate slight variances in the contents required by different types of notice under the present lien law.

In general, the standard contents include: (1) the name and address of the owner and reputed owner; (2) the name and address of the direct contractor; (3) the name and address of the direct construction lender; (4) a description of the site sufficient for identification; (5) the name, address and relationship to the parties of the person giving the notice; and (6) where the person giving the notice is a claimant, the notice must include a description of the labor, materials, etc. provided, an identification of who the labor, materials, etc. were provided to, and a statement of the demand.

The proposed set of standard contents is broad enough to include the information which is required under the various notices prescribed under the present lien law. Using a standard set of contents should eliminate confusion regarding which notices must contain what information. Clearly, a uniform set of standard contents should simplify, at a minimum for laymen, the preparation of notices under the lien law.

However, we believe that the Commission should consider referencing the generalized notice provision(s) that are to apply to specific sections. For example, individual statutes requiring notice should be cross-referenced to the generalized notice provision that is to apply to the contents and giving of notice of that specific statute.

The proposed law also includes a provision that the notice is not invalidated by a variance from the foregoing requirements as long as the notice is "substantially inform the person given notice of the information required by this section." (Proposed Section 7102) This is, in our view, a "gray area" in this aspect of the proposed notice requirements and will certainly create doubt and give rise to litigation. Because many of the notices are regularly prepared by persons in the construction industry, as opposed to counsel, it makes sense to give some leeway to persons who make the effort to comply and whose failure to do so does not prejudice the person to whom the notice is sent. Further, this provision seems to be in line with the spirit of the lien law which is, in our view, to provide strong protections to those with claims on construction projects.

(2) Clarification of manner in which service may be given (see Proposed Civil Code § 7104)

The Commission attempts to standardize and create uniformity in the manner of notice (Proposed Sections 7104 and 7108). Specifically, the proposed revisions set forth the manner of notice to be employed in various situations. If a statute requires notice by mail, the proposed law requires first class registered, certified, or Express Mail or some other form of overnight delivery. The inclusion of various forms of overnight delivery is described by the Commission as an innovation and the Commission particularly seeks comment in this regard. Specifically, the Commission queries whether the words "overnight delivery" should be replaced with the words, "express service carrier."

Manner of notice clearly varies from notice to notice under the present law. The Commission's desire to simplify this aspect of notice is in line with the overall goal of simplifying and clarifying the law. This proposed change makes sense and should be supported.

In addition, because of the development, and overall reliability, of Express Mail and other forms of overnight mail, the inclusion of this type of notice is a positive step. Because this form of mailing can be very expensive, it seems unlikely, in our view, that it will make a large impact, however, it should be permitted.

As to the use of the term "overnight delivery" versus "express service carrier," I tend to favor the latter. The use of the term "overnight delivery" is somewhat ambiguous where "express service carrier" seems to more clearly define the type of service which is contemplated by the Commission.

This part of the new law also includes a standard provision to apply when notice by "posting" is required under the law (Proposed Section 7112). The new law requires that the notice be posted at a conspicuous location at the site as well as at the main office at the site, if one exists. This law does not create a dramatic change and should be supported.

(3) Electronic notice (see, Proposed Civil Code § 7110)

The proposed new law provides that electronic notice may be used where the party to be notified has agreed to receive the notice by electronic means (Proposed Section 7110). As with the provision allowing for overnight delivery, this provision seems in line with keeping up with a changing and modernizing world. Electronic mail is the preferred (and most convenient) manner of communication and may simplify and lessen the cost of certain methods of notice. While, as attorneys, it would be difficult for us to advise a client to consent to receiving this form of notice, it should be available to those who prefer this method. To give effect to this provision and to make it a real alternative, we recommend that the Commission consider requiring e-mail addresses be provided by the owner, direct contractor and lender – whether as a part of the prime contract, on the face of the building permit or both.

(4) Proof of notice (see, Proposed Civil Code §§ 7108 and 7116)

The proposed law attempts to create uniformity in the law regarding the types of proof sufficient to prove notice (Proposed Sections 7108 and 7116). Most notable under the proposed new law, proof of mailing can be shown by a return receipt, delivery confirmation, signature confirmation, or *other proof of delivery or attempted delivery provided by the U. S. Postal Service*, as well as by a tracking record from an express delivery carrier. This is a significant and, in our view, positive change. Under the present law, some sections require the actual "green card" as proof of delivery by mail. This is often very difficult or impossible to obtain for many in the construction industry. Because the spirit of this law is to protect the claimants, this expansion and standardizing of the proof requirements is a welcome change.

Because of volume or other considerations, many potential claimants use services to send preliminary notices and other notices under the lien law. Due to the length of some projects, many notices are sent several months before any alleged claim arises. Due to the expense of

obtaining, filing and maintaining the "green cards" many are not retrieved by the claimants from the post office. Later, when a claim arises, the card is not available. The Postal Service does maintain, however, a log which indicates the items which were delivered or attempted to be delivered by certified, return-receipt mail. In our experience, these records have coincided with the information supplied by claimants. Because there is a high level of accuracy and reliability, these ledgers and similar records of the Postal Service should be sufficient to prove service in the manner prescribed by law.

The Commission has specifically sought comment regarding the mail delivery by the Postal Service. Our experience has been generally positive and is set forth in the preceding paragraph. Again, the Commission also seeks input as to whether the term "overnight delivery" should be replaced by "express service carrier" in this section. For the reasons set forth above, we believe that it should.

(5) Addresses for service

The new law seeks to standardize the addresses to which notice is to be given. Under the new law, notice is to be sent to the recipient's residence or place of business or at any of the following addresses: (1) if to an owner, to the address shown on the construction contract, the building permit or construction trust deed; (2) if to a lender, to the address shown on the loan documents or the construction trust deed; (3) if to a "direct" contractor, to the address shown on the contract, the building permit or that shown in the records of the CSLB; (4) if to a claimant, to the address shown on the contract, the preliminary notice (or other form of notice given by the claimant) or on the records of the CSLB; and (5) if to a principal or surety on a bond, at the address provided on the bond for such notices.

The foregoing change is consistent with the stated goals of the Commission. It clearly and concisely identifies which addresses are acceptable and, in effect, will reflect and/or establish the level of diligence required of claimants and others in obtaining appropriate addresses for notice. It should also protect those receiving notice in that the addresses described in the new law should result in actual notice being affected.

(6) When notice is complete.

The new law attempts to standardize the notion of when notice is complete. This section does not reflect a dramatic departure from the present law but does include a provision regarding deposit with an express carrier. The proposed law is generally consistent with the new law with the addition of the language regarding the express carrier. The law is consistent with the goal of the Commission to simplify and clarify the lien law and should be supported.

b. Commencement and Completion

i. Specific Comments and Recommendations

(1) Definition of "Commencement"

As written, the definition of this term is confused which we believe will be the subject of great debate and interpretation in the courts if left unchanged. As the Commission knows, the material issue that is addressed by commencement is the issue of notice and priority of title to the real property. As inchoate or secret liens, mechanics liens relate back to the date that work on the project commences. Hence, determining when commencement occurs is a very important matter because it potentially pits the lien claimant against lenders and other encumbrancers of the real property.

With this concept in mind, a review of the proposed § 7003 does nothing to identify the date that the parties whose interest it is in determining notice and priority (i.e., lenders and encumbrancers.) For example, section (a) states that the work of improvement is deemed commenced on the date that materials or supplies "that are used, consumed or incorporated in the work of improvement are delivered to the site." This language requires a retrospective review of what materials were delivered, when they were delivered and a determination of whether those materials were actually used on the project. This is not necessary for a variety of reasons.

First, if the concern is notice, and the practice of just about every responsible lender is to make an inspection of a site immediately prior to the recordation of a deed of trust, the existence of any materials on site (whether or not they are used or consumed on the project thereafter), is enough for that lender to refrain from record its deed. We presume that any such responsible lender would not record a deed in such a circumstance, notwithstanding the provisions of this proposed statute.

Second, the case law on commencement is fairly well developed, as this issue has arisen many times previously. Therefore, there appears no real reason to attempt to codify the case law; however, if the Commission is determined to make such a codification, we believe the statute should be modified. A suggested modification would be to trigger commencement on the date that material or supplies that are "intended for use, consumption or incorporation into the work of improvement are delivered to the site" or the date that "actual visible work altering the nature or condition of the site is commenced." Both of these events result in visible alterations to the site that should permit any lender or encumbrancer to understand that a subsequent recordation of an interest against the property may be subject to a mechanics lien.

(2) Completion (Private Works)

(a) Acceptance by Owner

Existing law defines completion as that time when the work of improvement is accepted by the owner. The proposed law eliminates this definition because it is not used and because the recording of a Notice of Completion is preferable, which triggers the statutory period for a claimant to record a lien. Because there is room for ambiguity by allowing completion to be defined by that time wherein the work of improvement is accepted by the owner, the proposed law is consistent with the Commission's goal of simplifying and clarifying the law.

(b) Acceptance by Public Entity

The current law is that if a work of improvement is subject to acceptance by any public entity, completion is deemed to be the date of acceptance by the public entity, as opposed to the procedures outline in § 7150. The proposed change would eliminate this provision entirely. The Commission indicates that the apparent purpose of this provision is to hold the lien period open so that, in a dedication situation, the owner can require the contractor to make changes demanded by the public entity as a condition to acceptance. Eliminating this provision would be consistent with the Committee's goals of simplifying and clarifying the statutory scheme, because there is already a statute in place to identify the period when a work of improvement is deemed completed. The law is cleaner when there is only one statute to read to determine when/if a project is complete. Having additional rules for private projects that could be dedicated to the public is just confusing, therefore, we recommend that the provision be eliminated.

(3) Completion

(a) Consolidation of the Notice of Completion and Notice of Cessation

The proposed law creates California Civil Code § 7150, which combines former § 3092 (notice of cessation) and § 3093 (notice of completion). This change is consistent with the Commission's goals because it streamlines statutory completion under one section.

However, we believe that subsection (b) of § 7150 should be eliminated as the issue of completion of public projects has been relocated to the Public Contract Code. Although the frequency of hybrid projects (private projects that are subsequently transferred to public entities) has increased, we don't believe that a public entity's acceptance of the project should be the determining factor for purposes of completion. Moreover, given that a party cannot record a mechanics lien against a public project (and therefore, can't foreclose such a lien), requiring public entity acceptance of a hybrid project would infer that the public entity has taken possession of the project and, as such, precluding liens against the project. We think that triggering completion of hybrid projects on the events described in § 7150(a), is consistent with

parties' lien rights and appropriate. Accordingly, we again recommend that subsection (b) be eliminated.

(b) Notice of Completion

The proposed change moves this section from Civil Code § 3093 to Civil Code § 7152. The new statute (California Civil Code § 7152) also extends the time by which an owner can file a Notice of Completion upon actual completion from 10 days to 15 days. This change only extends the number of days from 10 days to 15 days wherein an owner must file a notice of completion. We're not certain of the reason for the Commission's expansion of the recordation period; however, we don't believe that such an expansion would be stiffly opposed by the industry.

(4) Notice of Recordation

The proposed change requires an owner to provide a potential lien claimant with a copy of the notice of completion. As stated, the owner's obligation to give notice extends to the direct contractor and to any claimant that has previously given preliminary notice (California Civil Code § 7156). The proposed California Civil Code § 7156 identifies the persons/entities to whom an owner must provide notice of its recording of a notice of completion as the direct contractor and a claimant that has previously provided a preliminary notice. An owner is not required to provide notice to a person who occupies the property as a personal residence, if the dwelling contains four or fewer residential units; a person who has a security interest in the property; or a person who obtains a security interest in the property. This change is consistent with the Commission's goal of simplifying and clarifying the existing law because it eliminates any ambiguity on a contractor's part in identifying the claim to which the notice relates. However, as we have noted previously, the statute should contain a cross-reference to the statute that describes the contents and manner of service of notice.

(5) Notice by County Recorder

The proposed change eliminates the County Record's obligation to give notice to potential claimants. The proposed change is consistent with the Commission's goals because it eliminates a provision that is rarely followed.

(6) Separate Contracts on a Single Job

The proposed California Civil Code § 7154 (former § 3117) allows the recording of separate notices of completion as to individual contracts as to portions of the work of improvement. We believe that the provisions of the current § 3117 should survive fully and be adopted fully in § 7154. This provision benefits the owner by narrowing liability as to the particular portion of the project while, at the same time, permitting lien claimants to be fully paid and receive retention without waiting for the end of a multi-phased project. The possibility of a lien foreclosure during the time that a multi-phased project is on-going is a risk but a

circumstance that hardly, if ever, occurs because the contractor that is typically involved in the dispute is still on the project which gives the owner leverage (continued payments) which facilitates resolution of the claim. Accordingly, we recommend that the provisions of § 3117 be adopted in full without change.

c. Waiver and Release

i. Specific Comments

(1) Use of terms "Claim Or Lien"

Throughout the proposed revisions, the words "claim," "rights" and "lien" are sometimes used together, as if to differentiate among them, and other times only the word "claim" is used. For example, proposed sections 7162 and 7164 discuss the release of a "claim or lien." Likewise, section 7170 employs the language "lien and other rights." The use of the term "lien" in conjunction with the terms "claim" and/or "rights" seems redundant and confusing. Indeed, a "claim" would appear to include a claim of lien, a stop payment notice, or a payment bond claim. (See proposed Civil Code § 7002 ("'Claimant' means a person that has or exercises a right under this part to record a claim of lien, file a stop payment notice, or assert a claim against a payment bond.").)

It is suggested that all statutory references to "claim or lien" or "lien and other rights" or substantially similar phrases be changed simply to refer consistently to "claim." In conjunction with this recommendation, it is also suggested that an additional section of the Civil Code, at § 7001, be added as follows:

"§ 7001. Claim

"7001. 'Claim' means a claim of lien, a stop payment notice, and/or a claim against a payment bond as and to the extent provided for in this Part and in Article 3 of Part ___ of the Public Contract Code (beginning with section 42310)."

(2) Conditional Waiver And Release On Progress Payment

(a) Potential ambiguity of "Notice" portion of the proposed form release language.

Under the "NOTICE" portion of the Conditional Waiver and Release on Progress Payment text, it is purported that the document serves to waive "the claimant's lien and other rights." The term "lien" is specifically addressed, yet the other job rights are combined under the general "other rights" phrase. In addition, the term "other rights" is ambiguous, as the term "other rights" could be interpreted to include contract rights, which of course are not intended to be released, as is provided under the "exceptions" section.

It is recommended that this provision be clarified. One suggestion is that the phrase "the claimant's lien and other rights" be changed to "certain of the claimant's claims."

Further, under the "NOTICE" section, the release states "a person should not rely on this document unless satisfied that the claimant has received payment." A conditional waiver and release is intended to be relied upon in order to induce payment. Contrary to this purpose, the language would appear to limit the ability of a releasee to rely upon the document until payment already has been made. This, too, should be clarified. To do so, the following language could be added after the word "document": "as evidence of claimant's waiver and release."

(b) Resolving "through date" confusion.

Under the heading entitled "Conditional Waiver and Release", the proposed language provides that the release is effective with respect to the claimant's work "provided to the customer on this job through the Through Date of this document."

Some of our attorneys have advised of substantial confusion existing in the construction community with respect to whether certain work was "provided" by the "through date" of a release. For example, disputes arise with respect to whether material was shipped to, delivered to, or invoiced on, the project before the "through date." While case law has resolved this issue, substantial confusion still exists in the industry.

In an attempt to resolve this confusion the phrase "labor, service, equipment, and material provided to the customer" could be changed to "labor and service provided, and equipment and material provided or delivered to the project."

(3) Unconditional Waiver And Release On Progress Payment

The proposed language under the subheading "Unconditional Waiver and Release" provides for the claimant to indicate the "amount of payment." The inclusion of an acknowledgment of the amount of payment being received appears to be an appropriate change. However, the phrase "amount of payment" is ambiguous as it is unclear whether the "amount of payment" is intended to refer only to the most recently received progress payment that is the subject of the unconditional waiver and release, or if it is intended to reflect all payments received to date. It is suggested that the phrase "amount of payment" be changed to "amount of payment that is the subject of this release." It is further suggested that an additional line be included as follows: "total amount of payments received by claimant: $_____."

(4) Public Contract Code Differences

The conditional waiver and release on progress payment and conditional waiver and release on final payment language under the proposed Public Contract Code sections includes the use of the term "lien and other rights," as discussed above. Inasmuch as no lien rights exist on public projects, inclusion of this language is unnecessary and potentially confusing. In addition,

as stated above, the term "other rights" is vague. However, it is assumed that the Commission intends that the same forms be made appropriate for use on both private and public projects. Certainly, this uniformity is preferred. It is suggested that the change outlined in Section 2 above, specifically that "lien and other rights" or "claim or lien" be changed to simply "claim," and that "claim" be defined in new Section 7001 of the Civil Code and, where appropriate, in the Public Contract Code.

d. Miscellaneous Matters

i. Specific Comments.

(1) Ownership Issues

The proposed law includes a new definition of "owner" in § 7028. An owner is defined as (a) with respect to a work of improvement, the person that contracts for the work of improvement, (b) with respect to the property upon which a work of improvement is situated, a person that owns the fee or a lesser interest in the property, including an interest as lessee or vendee under a contract for purchase, or (c) a successor in interest to an owner as defined above. The proposed law also codifies the case law definition of reputed ownership in § 7037 as a person that a claimant reasonably and in good faith believes is an owner.

In addition, the proposed law addresses issues of co-ownership, clarifying in §7058 (a) that an owner may give notice or execute or file a document on behalf of a co-owner if the owner acts on the on the co-owner's behalf and includes in the notice or document the name and address of the co-owner upon whose behalf he is acting. § 7058 (b) states that it is not effective notice upon an owner of the fee to give notice to an owner of a leasehold or other interest in property that is less than a fee.

Generally, these proposed changes appear to be consistent with the Commission's goal of clarifying and simplifying the mechanic's lien laws. Ownership has been defined and clarified in an attempt to make certain other provisions, such as notice requirements, more understandable. However, there appears to be a conflict between the definition of an "owner" in § 7028 and the effect of notice given to a "co-owner," as defined in § 7058.

An owner of a work of improvement is defined as a person that contracts for the work of improvement, while an owner of property is defined as a person that owns the fee or a lesser interest in the property, including an interest as lessee or vendee under a contract for purchase. Therefore, in some cases, one person may own property in fee, while a second person may have a long term leasehold interest in the property, and a third person, who contracted for a work of improvement on the property, may have a lesser leasehold interest in the property. Pursuant to § 7028, all three persons would be classified as "owners." However, notice by the contractor upon the third person, unless he is a purported owner, as defined in § 7037, will not be effective as to the first owner. Therefore, it is incumbent upon the contractor to provide notice to the owner in fee. This is not overly burdensome and should not come as a surprise to contractors; however,

the proposed law is silent as whether notice upon the third person would be effective as to the second person, with the greater leasehold interest.

If the property were to become encumbered by a mechanic's lien, the interest of the second person in the property may be dramatically affected, especially in the case of a foreclosure action. Therefore, consideration should be given as to whether notice should also be required as any person holding a greater leasehold interest than the owner as defined in § 7028 (a), but less than interest in fee. If the second person were to have knowledge of the work of improvement, but not post and record a notice of nonresponsibility, that person's interest in the property would be subject to a lien. However, if the second person did not have actual knowledge of the work of improvement, that person could argue that notice upon the owner in fee and the owner of a lesser leasehold interest was not effective as to the second person's leasehold interest.

While the proposed law does clarify that notice to the owner of a leasehold interest will not bind an owner in fee, it is suggested that § 7058 be revised to indicate whether notice upon an owner of a lesser leasehold interest will bind the owner of a greater leasehold interest.

(2) Authority of Agent

§ 7060 states that an act that may be done by a person under this part may be done by his agent, to the extent that said act is within the scope of the agent's authority. These proposed changes appear to be consistent with the Commission's goal of clarifying and simplifying the mechanic's lien laws. This provision both certifies that an agent may perform acts required to be done by a person and clarifies that those acts which may be done are limited to the scope of the agency. As discussed above, co-owners have certain agency authority to act on behalf of their other co-owners. The proposed law provides that notice by or to, or action by, an agent binds the owner, provided that such action is within the scope of the agent's authority. Further, by addressing the limits of agency, the proposed law clarifies that a contractor's authority to act as an agent on behalf of the owner is limited, and does not include other acts, traditionally not within the scope of a contractor's authority, such as compromise of litigation. No changes or further modifications are recommended.

(3) Contract Change

The proposed law includes a new definitions of "Contract" and "Contract Price" in §§ 7006 and 7008, to include a contract change. This clarification also affects § 7430 (Amount of Lien.) That provision states that the lien is not limited in amount by the contract price for the work unless the owner in food faith files the contract with the county recorder and records a payment bond in an amount of at least 50 percent of the contract price. Importantly, the provision of former § 2123 (c) which required an owner to give notice to the original contractor and the lender of an increase of 5 percent or more was not included in the proposed law.

Generally, these proposed changes appear to be consistent with the Commission's goal of clarifying and simplifying the mechanic's lien laws. The proposed modifications are more consistent than the prior laws in that the terms "contract price" and "contract" are defined to include "contract changes" and the terms are used consistently throughout the statute.

Eliminating the requirement that an owner notify the original contractor and the construction lender of a change in the original contract that changes the contract amount by at least 5% is a good change and one that should have general consensus. We agree with the commentary in the Tentative Recommendations that this provision of the existing law is not typically observed in the industry.

The purpose of this provision in the existing law is unknown. It may have been included to guarantee that the original contractor was made aware of increases of the contract amount in order to ensure that the lien, when eventually recorded, was for an amount large enough to cover all outstanding monies claimed, including contract increases. Regardless, the requirement that the owner give notice to the contractor makes little sense (since the contractor is presumably aware of any increases in the contract amount), and is a practice that is rarely, if ever, followed. As such, the removal of this provision appears to be worthwhile.

e. Preliminary Notice

i. General Comments.

In accordance with its goal of simplifying these statutes, we wondered why the Commission hasn't harmonized the preliminary notices required for public and private projects. The use of one form by various parties in the industry, it seems, would simplify things.

ii. Specific Comments and Recommendations

(1) Contents of the Preliminary Notice - § 7204

This section sets forth some of the required language to be included in the preliminary notice including the "**NOTICE TO PROPERTY OWNER**" language. The new language is simplified but is still required to be in "bold face type". The proposed language also includes the requirement that the owner provide a notice of recording the "notice of completion" for the construction project to all persons who served a preliminary notice.

The contents of the preliminary notice are set forth in this section and new proposed § 7102. Under Section 7102 the "claimant" (which presumably means a party giving the preliminary notice) is obligated to list in the notice: "A statement or estimate of the claimant's demand after deducting all just credits and offsets." This appears to be more for a lien, stop notice or bond claim instead of the previous requirement that the preliminary notice set forth as "estimate" of the labor and/or materials to be provided and does not appear to satisfy the Court of Appeals holding in *Rental Equipment, Inc. v. McDaniel Builders, Inc.*, (2001) Cal App. 4th

445, where the Court of Appeal stated that the estimate contained in the preliminary notice must be derived by the claimant using a "rational process" instead of a guess.

The Commission's goal of simplifying and streamlining the statutes with "unifying language" is a revision that is much appreciated. However, nowhere in the preliminary notice for private work sections does it indicate that the potential claimant must provide the recipient of the preliminary notice with an "estimate" of the labor and/or materials it intends to provide to the construction project. § 7204 sets forth a portion of the information the preliminary notice must contain. The claimant must also refer to § 7102 for additional items to be set forth in the preliminary notice. In confusing language, § 7102(a)(6)(iii) states that the preliminary notice must contain the following information: "A statement or estimate of the **claimant's demand**, after deducting all just credits and offsets." (Emphasis added.) This language appears to be more suited for liens, stop notices, and payment bond claims and not instructive to the person serving the preliminary notice who, under current law, provides an "estimate" and not a "demand" for payment. Therefore, it is suggested that § 7102(a)(6)(iii) be amended to properly direct the person sending and receiving the preliminary notice that the amount set forth therein is not a "demand" for payment but an "estimate" of the potential claim so that the recipient may protect itself. Moreover, the Commission should give some consideration to the Court of Appeals holding in *Rental Equipment, Inc. v. McDaniel Builders, Inc.*, (2001) Cal.App.4th 445, by obligating the provider of the preliminary notice to use a "rational process" for the estimate.

Additionally, we believe that since the Commission has adopted the use of electronic means for purposes of giving notice, the statutes pertaining to preliminary notices should require the notifying party to identify an e-mail address to which notices may be given. Further, we believe that the generalized notice provision (§ 7104) should refer to § 7110 (electronic notice) as an approved method for giving of notice.

(2) Definitions.

(a) General comments regarding definitions.

The new lien law contains definitions beginning with Section 7002 and ends at Section 7046. It is suggested that the substantive sections following the definition sections be modified by capitalizing the first letter of each defined word used in each substantive section so that there is no confusion by the reader that a specific word has been defined by the legislature.

(b) Definition of "Construction Lender"

The new lien law continues the obligation of a construction lender to withhold funds pursuant to a valid preliminary notice/stop notice. A construction lender is defined in new Section 7004. New Section 7004(b) defines a construction lender as: "An escrow holder or other person holding funds provided by an owner...as a fund for payment of construction costs for all or part of a work of improvement." It is unclear whether the new law would subject the escrow holder who holds funds deposited by an owner for the benefit of the direct contractor under the

"construction security escrow account" (created under the current law as set forth in Civil Code section 3110.5 and moved to new sections 7700 et seq.) to a subcontractor/material supplier stop notice. It is believed that the escrow holder under the current law, as set forth in Civil Code section 3110.5(d), was not subject to a stop notice by a subcontractor or material supplier. In order to ensure that the escrow holder of the funds deposited under the "construction security escrow account" is not subject to a stop notice under the new law, it is suggested that new Section 7004 (b), be rewritten as follows:

> 7004(b). An escrow holder or other person holding funds provided by an owner, lender, or other person as a fund for payment of construction costs for all or part of a work of improvement, except an escrow holder in receipt of those funds deposited by the owner for the benefit of the direct contractor under a "construction security escrow account" as set forth in Section 7700, et seq.

By making this clarification, it will be clear that the new definition of a construction lender does not include the escrow holder of those funds specifically set out for the benefit of the direct contractor under the statutes set out in 7700 et seq..

f. Mechanics Lien

i. Specific Comments.

(1) Laborers Compensation Fund

The term "Laborers Compensation Fund" is a new term in the lien law that has apparently been created to eliminate confusion over multiple terms that are used inconsistently. We believe this is a good idea.

(2) Persons entitled to lien (§ 7400)

In this section which describes the parties that are entitled to lien rights, the Commission has included the term "builder." Such a term is not defined in the statutory scheme nor is it used in § 3110 which currently describes the parties entitled to such rights. We recommend that if the term "builder" is to be used, that it be specially defined.

(3) Terminology

It is our understanding that the phraseology used in the present scheme has been eliminated to some degree in order to simplify and clarify the statutes. If that is the case, we recommend that the phrase "claim of lien" as set forth in § 7470 be removed – as should all other references to that term.

(4) Use of Material in Structure

Under the new law, upon proof that a claimant's materials were delivered to a job site, there would be a presumption that the materials were actually used in the construction. (Section 7026(b)). We presume that this presumption is to be rebuttable and not conclusive; however, it is not affirmatively stated either way. We suggest that the Commission clarify its intent and, in doing so, consider Evidence Code §§ 600 et seq., with respect to the creation and impact of presumptions.

Otherwise, we believe that the intended revision is a great change for material suppliers, but not good for owners and general contractors. Materials are frequently delivered to a site and not used in construction. On other occasions, materials are delivered to the wrong site. Why should owners and general contractors have the burden of disproving the incorporation issue? Because lien claimants are able to create involuntary liens on a person's property based solely on an allegation of money owed, it would only seem fair that the claimant have the burden of proving that its materials were incorporated into the project.

(5) Notice of Claim of Lien

Under the new law, a lien claimant must notify the owner, in advance, that it intends to record a lien. This would be enforced by a prohibition on the County Recorder recording the lien, unless the lien is accompanied by a proof of serving the Notice (§ 7420). We believe that the proposed revision is a good idea which may lead to an early resolution of some disputes without a lien being recorded.

(6) Lien Release Bond

Under the new law, the amount of the Lien Release Bond has been reduced from 150% of the amount of the lien claim to 125% of the amount. This makes it consistent with the Stop Notice Release Bond (§ 7428), which makes sense.

(7) Time for Commencement of Enforcement Action

The time limit to file the lawsuit remains unchanged at 90 days, but the new law also requires that a Lis Pendens be recorded within 100 days after the lien is recorded. Otherwise the claim of lien expires and is unenforceable (§ 7460). Strangely, § 7464 says that a claimant "may" record a lis pendens, even though section 7460 essentially makes it mandatory.

On the surface, this proposed change seems like a good idea for the protection of owners. However, it may hurt the ability of a claimant to resolve his claim without extensive litigation, because a claimant often is negotiating with a subcontractor or general contractor and does not want to notify the owner or others that a lawsuit has been filed. This could also be a big trap for claimants and their attorneys. To record a Lis Pendens, you need to have a conformed copy of the complaint back from court so that you have a case number for the Lis Pendens. There are

several courts that often take a week or two to return complaints. If you wait too long, you could be committing malpractice. This will probably lead to complaints getting filed earlier and will lead to increased messenger charges to make sure you get a conformed copy back immediately. We recommend the elimination of the language requiring the recording of a Lis Pendens within 100 days of recordation of the lien. In the event that the Commission preserves this provision, we recommend a change to the language to state that the failure to record a Lis Pendens prior to the sale of the property to a bona fide purchaser would make the lien invalid as against a bona fide purchaser or any subsequent good faith encumbrancer without notice, but would not otherwise affect the validity of the lien.

(8) Liability of contractor for lien enforcement (§ 7476)

Contrary to the Commission's comment to this proposed new section, it is not a restatement of the current § 3153. Instead, it contains a substantive change from the current provision.

First, the section that is currently in force and effect references, in its title, the contractor's obligation to indemnify the owner from lien claims. The title of the new section eliminates this reference.

Next, subsection (a) of the proposed provision refers to an owner's right to withhold monies from the contractor in the amount that is "claimed in the action" rather than the amount "for which claim of lien is recorded" as stated in the current section. This is a significant difference as it could arguable permit the owner to withhold more than the lien amount from the contractor (i.e., if the action, which is undefined in the new scheme, includes another cause of action for which damages are sought exceeding the amount of the lien claim.) Using the term "action" in this provision, without further definition or clarification is likely cause conflict.

Lastly, the scope of the contractor's obligation to indemnify the owner should be limited to lien claims that are made by claimants other than the direct contractor (i.e., direct contractor shouldn't be held to indemnify the owner from the direct contractor's own lien claim). Further, the direct contractor's indemnity obligation should be limited to lien claims of subcontractors or suppliers for which the contractor has already been paid.

(9) Attorneys Fees

The Commission seeks public comment concerning whether attorney's fees should be allowed to the prevailing party in an action to enforce a lien claim. Attorney's fees are not currently allowed in lien actions, but they are allowed in actions to enforce Bonded Stop Notice claims and Public Works Payment Bond claims.

In our experience, the existence of an attorney's fee provision can lead to an earlier resolution of claims, including mechanic's lien disputes, because of the potential exposure that is presented by such a provision. However, the existence of a fee clause or statutory provision

entitling a party to the recovery of fees can also lead a party to continue to litigate claims. For example, in the situation where a party has already incurred significant fees and costs, that party may opt to continue to litigate a claim in the hope that those fees and costs will be recovered, notwithstanding the risk of paying the opponent's fees. Nevertheless, in balancing these respective positions, and giving consideration to the purpose of a lien (i.e., to compensate an improver of real property for the value of the improvements), we believe that the existence of an attorneys fee provision might result in earlier resolutions of claims. If the Commission intends to adopt an attorney fees provision, the Commission might consider protections for single-family homes or residential structures of 4 units or less. Alternatively, the Commission could consider a ceiling on claims to which the fee clause would apply (i.e., fee provision applies to claims in the principal sum of $50,000 or less). Most importantly, the Commission should exclude the direct contractor from the recovery of fees, unless the underlying contract permits their recovery, because the contract terms between owner and direct contractor should prevail (i.e., if they negotiated out a fee clause, the contractor shouldn't be able to get around that arms length transaction by virtue of a statutory fee provision.)

g. Invalid or Unenforceable Claim of Lien

i. Specific Comments.

(1) Owner's relief.

The Commission's proposed changes in connection with invalid or unenforceable claims of lien appear to have less to do with the Commission's desired overall goal of "simplifying and clarifying" the mechanic's law scheme and more to do with providing owners with relief in connection with invalid or unenforceable claims of lien. In this regard, we believe the Commission's proposed changes are welcome and will be effective. We find the Commission's proposed § 7494 particularly effective in that it provides owners facing unenforceable invalid liens relief without the necessity of bringing an action to clear a cloud on title caused by an invalid or unenforceable lien. However, we do believe that some minor changes with respect to the expedited procedure for obtaining a release of lien would make the scheme even more effective.

Under the current proposed scheme, an owner is required to make a demand that a lien be removed at least 10 days before filing the petition and a determination on the petition may not be made as far out as 75 days after the filing of the petition (§§ 7482 and 7486.) Therefore, it may take as long as 85 days for an owner to obtain a release of an invalid or unenforceable claim of lien. This length of time may make the expedited procedure irrelevant to owners seeking a release of claim before the expiration of the 90 day statutory period. For example, an owner who has paid off an amount owed or an owner faced with a fraudulently recorded claim of lien, may not find the expedited procedure of particular value because the owner may obtain a release order after 85 days, under the provisions of § 7494, unless a *lis pendens* or extension of credit is filed, the lien will be of no legal significance in any event.

Consequently, we recommend shortening the time periods provided in §§ 7482 and 7486. The demand time proposed in § 7482 could be shortened to five days and the maximum time for determination on a petition in § 7486 could be shortened to 60 days. We believe that any additional burden that these changes would place on the judicial system would be outweighed by effectively addressing the Commission's stated goal of providing expedited relief (prior to the expiration of the 90 day statutory period) to owners faced with unenforceable or invalid claims of lien.

The Commission might consider one additional change to its expedited procedure for obtaining a release order. Proposed § 7480 makes clear that no other action or claim for relief may be joined with a petition for a release order. However, it is unclear whether or not an owner may bring a petition if the claimant has already commenced an action to enforce the lien. Obviously, to allow both actions to proceed simultaneously, without being joined may result in inconsistent judgments. Consequently, we believe that § 7480(b) should be clarified to prohibit a commencement of a petition seeking a release order in the event that an enforcement action has already been commenced.

h. Stop Payment Notice.

i. Specific Comments.

(1) Terminology.

(a) Use of the term "Stop Payment Notice"

According to the Commission, the term "Stop Notice" is cryptic, and can be confused with the "Stop Work Order." The proposed law replaces the term "Stop Notice" with the more descriptive "Stop Payment Notice." In our opinion, this proposed change in terminology is appropriate.

(b) "Giving" a Stop Payment Notice.

The Commission states that existing law refers inconsistently to "giving" the Notice, "filing" the Notice, and "serving" the Notice. Since a "Stop Payment Notice" is not filed in the traditional sense of lodging it with the Court Clerk, nor served with the formalities of Court process, the proposed law seeks to standardize the terminology by referring to the "giving" of the "Stop Payment Notice." The proposed change is consistent with simplifying the scheme.

(2) Contents of Notice

(a) Amount of Claimant's Claim.

The existing law requires a claimant to include in the "Stop Payment Notice," the amount in value, as near as may be, of the work already provided, or materials already furnished.

According to the Commission, the meaning of the phrase "as near as may be" is obscure. The proposed law replaces the existing standard with the requirement that the Notice state the claimant's demand after deducting all just credits and offsets. That is the same standard used for a claim of lien, and according to the Commission will help achieve consistency in the statute. We believe that the proposed modification simplifies and clarifies the statutory scheme and, therefore, should be adopted.

(b) Claim for Contract Changes and Damages for Breach.

The existing law governing "Stop Notices" does not refer to contract changes. By contrast, the mechanic's lien law allows a claimant to include in the claim of lien an amount due for written modifications of the contract, or as a result of rescission, abandonment or breach of the contract. The proposed law adopts the same standard for both. The proposed modification is consistent with the goal of clarifying and simplifying the statutory scheme. There is no reason why the claim amounts allowable for a mechanic's lien and for a "Stop Payment Notice" should differ.

(3) Demand for Notice

Under existing law, an owner may demand that a claimant give the owner a stop notice. If the claimant fails to do so, the claimant forfeits the claimant's mechanic's lien rights. See, Civil Code § 3158. The proposed law makes clear that only an unbonded "Stop Payment Notice" may be required under this provision by demand of the owner. The proposed modification is consistent with the goals of the Commission and reasonable because requiring a bonded "Stop Payment Notice" would often create an undue hardship on the part of the claimant, which could easily be abused by owner in order to induce the forfeiting of the claimant's mechanic's lien rights.

(4) Release Bond for Funds Withheld Pursuant to Notice

(a) Who May Give Release Bond.

Existing law provides that "an owner, construction lender, direct contractor or subcontractor" that disputes the correctness or validity of a "Stop Payment Notice" may obtain release of funds withheld pursuant to the notice by giving the person withholding the funds a release bond (see, Civil Code § 3171.) According to the Commission, there is no apparent reason why a material supplier or other interested person ought not to be able to obtain release of funds by giving an appropriate bond. The proposed law purportedly simplifies the statute by eliminating the restriction on person authorized to give a release bond.

In our opinion, however, the proposed law does much more than simplify or clarify the statutory scheme. The proposed modification is a substantive revision which will greatly broaden the class of persons entitled to obtain the release of funds held by "Stop Payment

Notices" by obtaining a release bond. If the proposed modification is adopted, it is more likely that material suppliers and other interested persons will obtain release bonds in order to trigger the continued flow of construction funds on a project.

(b) Conditions for Giving Bond.

Under the existing statutory scheme, the release bond remedy is limited to circumstances where a person disputes the correctness or validity of a "Stop Payment Notice." The proposed law seeks to simplify the statute by allowing a release bond in any circumstances. If this is the Commission's intent, we don't have a specific objection nor do we believe there is a consensus within the industry that would object to this change.

(c) Sureties on Bond.

Under existing law, a mechanic's lien release bond requires an admitted surety, whereas the "Stop Payment Notice" release bond does not specifically require an admitted surety. Because the two bonds are similar in function, the proposed law requires an admitted surety for a "Stop Payment Notice" release bond. We believe this change is appropriate and consistent with the Commission's goal of simplifying and clarifying the statutory scheme.

(5) Duty to Withhold Funds

Existing law states that if the owner is given a "Stop Payment Notice," it is the duty of the owner to "[w]ithhold from the original contractor or from any person acting under his or her authority and to whom labor and materials, or both, have been furnished, or agreed to be furnished, sufficient money due or to become due to such contractor to answer such claim and any claim of lien that may be recorded therefor (see, Civil Code § 3161.)

According to the Commission, the statute is garbled. It is unclear whether the person from which funds are to be withheld must be acting under authority of the owner or of the original contractor, and whether labor or materials must have been furnished to the owner, the original contractor or the person acting under authority of one of them. The comparable provision of the public works "Stop Payment Notice" from which this statute evolved, states simply that the public entity must withhold from the direct contractor, or from any person acting under the direct contractor's authority, an amount sufficient to pay the claim stated in the notice. See, Civil Code § 3186. According to the Commission, that interpretation is sensible, and the proposed law adopts it. The proposed law also omits the requirement that funds be withheld to cover the amount claimed both in the "Stop Payment Notice" and "in any claim of lien that is recorded."

According to the Commission, the claim of lien reference is problematic since any amount withheld pursuant to a "Stop Payment Notice" reduces the claim of lien. The Law Revision Commission solicits comment on this issue. We believe that the proposed law is consistent with the goal of clarifying and simplifying the statutory scheme. There is no reason

why there should be a substantive difference between the public work and private work statutory schemes in this regard. Additionally, the Commission is correct to say that the claim of lien reference is confusing because the amount withheld pursuant to a "Stop Payment Notice" should not be increased based upon the existence of a mechanic's lien claim.

(6) Enforcement of Payment of Claim Stated in Notice

Existing law requires a "Stop Payment Notice" claimant, within five (5) days after commencement of an enforcement action, to notify persons that have been given the "Stop Payment Notice." The five (5) day notice appears to supplement, and not replace, normal service of process requirements. According to the Commission, the consequences of failure to give the five (5) day notice are unclear. The case of Sunlight Electric Supply Co. v. McKee, 226 Cal.App.2d 47 (1964), sets forth that the five (5) day notice requirement is directory rather than mandatory. The rationale of the Sunlight Electric opinion is that the "Stop Payment Notice" claim should be construed liberally in favor of a claimant, just as a mechanic's lien is construed liberally in the private work context. However, according to the Commission, in a private work the "Stop Payment Notice" augments, and is not exclusive of, the mechanic's lien remedy. For this reason, the Commission solicits comments on whether the five (5) day notice requirement should be mandatory in place of the existing directory provision.

In our opinion, the statute should not alter the directory nature of the existing law. Regardless of whether a "Stop Payment Notice" claimant also may have a mechanic's lien claim, the law should be construed liberally in favor of the claimant, as is consistent with the current private work context. As such, the opinion reached by the Sunlight Electric court makes sense.

Additionally, we believe that the Commission should extend the time within which to serve a Notice of Commencement such that it is consistent with the statutory provisions relating to a Lis Pendens.

i. Payment Bond

i. Specific Comments.

(1) Limitation of Owner's Liability

In private works of improvement, it is extremely uncommon for owners to record a payment bond or directly benefit from the cap. This is not to say we suggest the laws be scrapped, only that the stakes are low on a practical level. We dislike the term "conditioned" being retained in proposed Civ. Code § 7606(a). "Condition" holds connotations as a prerequisite. That section does not create a prerequisite. Perhaps it is better phrased as, "A payment bond shall by its terms inure to the benefit of all claimants so as to give a claimant a right of action to enforce the liability on the bond."

(2) Bond Underwriter Licensed by Department of Insurance

The revision contained in proposed Civ. Code § 7604 is overdue and welcome.

(3) Limitation on Part

The revision is actually much more controversial than the comments indicate. Proposed Civ. Code § 7608(a) appears to try to utilize the new term "direct contractor" but otherwise maintain the wording of current Civ. Code § 3267. Neither the current statute nor the proposed one, however, takes into consideration the functional law in this area: Union Asphalt, Inc. v. Planet Ins. Co. (1994) 27 Cal.Rptr.2d 371, 21 Cal.App.4th 1762. Union Asphalt clearly allows third-tier subcontractors to be claimants on a payment bond, and therefore arguably contradicts the plain meaning of proposed Civ. Code § 7608. This section should either be reconciled with Union Asphalt or express intent to overturn it, lest the Legislature's purpose be misinterpreted.

(4) Notice prerequisite to enforcement

In many places throughout the proposed legislation, everyday and commonly used lower-case words are given esoteric definitions. Proposed Civ. Code § 7612(b) is a prime example with the use of the word "notice." We understand that "notice" is purportedly a term of art now and whose definition is contained in proposed Civ. Code § § 7100 et seq. Some reference to that section should be included so as to not create too much confusion. The notice requirement contained in current Civ. Code § 3242 could never be mistaken because the reader is directed to a precise instruction of what must be done. The proposed section should be no less clear.

j. Other Remedies

i. Specific Comments and Recommendations.

(1) Stop Work Notice (Civil Code § § 7830 to 7847, former Civil Code § 3260.2)

(a) Terminology

The substance of former § 3260.2(a), setting forth the notice to owner and project posting requirements, is broken out into new §§ 7830, 7832, 7834, 7836 and 7840. The new term "stop work notice" is defined and used in lieu of "stop work order" since it is not a court order, but rather, must be given and proved in the same manner as other notices under the mechanics lien law. The new sections remove the language that limits the remedy to private works, as redundant because the new sections fall under "Part 6 – Private Work of Improvement". The new sections eliminate language requiring the contractor to "serve" the notice on the owner and subcontractors and that the notice is "posted at a conspicuous location on the job site and at the main office of the job site". Instead, the new sections provide that the contractor may "give" notice to the owner and "post notice".

The definition of "stop work notice" still has the potential for confusion with "stop payment notice", "stop notice", etc., particularly since the stop work remedy applies only to a private work. We recommend that a more distinct term, such as "Work Suspension Notice" be used. If the term "stop work notice" is utilized, we think it is prudent to maintain the language that limits the stop work remedy to private works; as a "stop payment notice" is available on public works and similar terminology could cause confusion as to which types of projects are subject to the stop work remedy.

(b) Notice

It is not clear how the direct contractor is required to "give" notice to the owner, how the owner must "give" notice to the construction lender and how notice must be "posted" from reading these statutes. Since contractors and some legal practitioners may look only to the immediately surrounding statutory sections or may not be familiar with the entirety of Part 6, we recommend, as already set forth above, that the new statutes make clear cross reference to other pertinent provisions of Part 6 that notice must be given, or posted as provided in §§ 7104, 7108, 7110 and 7112.

(c) Preserving limitations to subcontractor or supplier liability

The text of § 3260.2(c) provides:

> "Notwithstanding any other provision, the original contractor or his or her surety, or subcontractor or his or her surety, shall not be liable for any delays or damages that the owner or contractor of a subcontractor may suffer as a result of the original contractor serving the owner with a 10-day stop work order, and subsequently stopping work for nonpayment if all of the posting and notice requirements described in subdivision (a) are met. An original contractor's or original subcontractor's liability to a subcontractor or material supplier resulting from the cessation of work under this section shall be limited to ..." (Emphasis added).

The proposed legislation eliminates text of the original statute in **bold** above that address subcontractor liability on the grounds that the provisions are "apparently an artifact of the legislative process" and to make clear that only a direct contractor can give the stop work notice.

While it is appropriate to make clear that only the direct contractor can give a stop work notice, we do not recommend that the limitation of subcontractor liability be removed. If a subcontractor, of any tier, took the prudent but optional step of giving its lower tier subcontractors and material suppliers a copy of the prime contractor's written notice (in addition to the direct contractor's jobsite posting) and, despite that notice, the lower tier subcontractors and suppliers continued working on the site and ultimately were not paid for the subsequent work (since, for example the owner eventually terminated the prime contractor after receiving

the stop work notice), the prime contractor could insulate itself from liability for mechanics liens and other claims arising from the lower tiers' work, but the subcontractor, despite its best efforts could not. Since the subcontractors cannot control the actions of the direct contractor, it seems equitable to limit a subcontractors' liability.

(d) Judicial determination

The text of § 3260(d) as proposed is not changed, which permits the direct contractor or its surety to seek a judicial determination of the amount due in an "expedited proceeding" if payment is not made within 10 days after a stop work notice is given.

Since suspension of work can have a significant, if not disastrous, impact on a project, we believe that the owner, who will likely suffer loss of income/use, increased interest on the construction loan and other consequential damages, should have the right to seek an "expedited resolution" as well as the direct contractor and its surety.

Our experience has been that judges are not familiar with the statute and rarely grant an "expedited" review. Notwithstanding this, we believe it is important that the resolution of a dispute that halts construction must be resolved on an expedited basis and that this provision remain in some form.

It is not clear why the resolution of the dispute must be by "judicial" determination. If the parties have agreed to a third party neutral, disputes review panel or arbitration of claims, why must the court make this determination? This provision illustrates why the right to stop work or suspend work on a private project, as well as other dispute resolution procedures, may best be left to the parties to freely negotiate.

(2) Security for Large Project (§§ 7700 to 7730, former Civil Code Section 3110.5)

The proposed changes in the law are not substantive, however, the Commission has solicited comments on § 7726, which requires the escrow account to be "located in this state". The Commission suggests that this term be dropped as meaningless given that local bank checks may be written from assets located elsewhere.

Presumably the requirement for the escrow account to be located in the State of California is to take advantage of California's escrow laws and protections and to ensure that the direct contractor seeking release of escrowed funds does not have to travel to an out of state bank to obtain release of funds or, in the event of a dispute, file suit out of state to secure release of the *res.* We do not recommend deleting the requirement that the account be located in California. Rather, we suggest that it be maintained as the default provision in the absence of mutual agreement to use an escrow account in a different location.

In addition, we recommend that the term "escrow account" be excluded from the definition of "construction lender" in new § 7004 so that security funds under this section are not subject to stop payment notice claims of subcontractors and material suppliers. We believe this limitation is consistent with the original underlying purpose of the stop work notice legislation.

k. Public Works Contracts – General Provisions

i. Specific Comments and Recommendations.

(1) Definitions

Although the name of the newly proposed Part to the Public Contract Code is "Public Works Contract Remedies" we do not believe the Commission is proposing legislation that governs all remedies that may be pursued on public works of improvement (i.e., enforcement of contractual rights, rights and obligations provided in other Parts of the Public Contract Code, etc.) We presume the Commission seeks to enumerate the rights, remedies and procedures related thereto governing statutory rights (i.e., stop payment notice and payment bond claims.) As discussed more fully in the following portion of this Memorandum, we believe that the new statutory scheme pertaining to public works o improvement should clearly and unambiguously state that the new provisions are intended to relate only to the aforementioned statutory rights. We believe this can, and should, be done by specifically defining the term "claim" to refer to stop payment notice and/or payment bond claims and using that term consistently throughout the new statutes.

(2) Notification

(a) Uniformity of notice requirements.

Despite the Commission's stated goal of simplifying the statutory scheme and, in this vein, its attempt to make uniform the notice provisions of statutory remedies applicable to private works, it does not appear as such an attempt has been made for public works. We believe that the notice provisions applicable to public works statutory remedies are equally susceptible to harmonization and that they should be made uniform.

(b) Electronic notice.

The Commission made provisions for electronic notice in the private works provisions and we believe such provisions, at least to some degree, should be incorporated in the public works scheme. There are occasions where notice, that is to be given, could be given by e-mail so as to more expeditiously accomplish statutory goals. For example, under § 44170, the public entity is to give notice to each claimant that has given a stop payment notice of the time within which that notice must be enforced. Electronic notice could be utilized in this instance, as in other similar instances, to expedite notice being given to claimants.

(c) Notice to disbursing officer.

The Commission's proposed change focusing all notices to the public entity by delivery to the disbursing officer of the public entity is a welcome change. To effectuate this change, however, we recommend that all public contracts be required to contain the name and address of the disbursing officer for purposes of ensuring notice is delivered to the right person and the correct address.

Further, the terms of § 44130(b), relating to the giving of stop payment notice to a public entity, should be harmonized with the requirements set forth in § 42070 which requires notice to a public entity to be given to the disbursing officer. We don't believe there is any reason for there to be any difference in treatment for these two provisions. If the disbursing officer is to receive preliminary notices, that same person should also receive stop payment notices. Permitting stop payment notices to be delivered to others, is not consistent with the goal of simplifying the process.

(3) Persons entitled to remedies - § 42030.

The Commission's proposed language of this section arguably, and very likely, eliminates whole groups of potential claimants with statutory rights under the present scheme. Specifically, second tier subcontractors and suppliers (those who subcontract with subcontractors or supply to subcontractors) and lower tiered parties, would be precluded from asserting stop payment or payment bond claims. Those same parties are presently able to assert such rights (see, §§ 3181 and 3226 incorporating § 3110.) Although the Commission's comment to this provision states that the provision "restates former Civil Code Section 3181" in actuality, that is not the case.

Nowhere in the new statute does it incorporate a similarly broad description of the "persons" that are entitled to assert rights under § 3110. Rather, section (1) of the statute seems to limit those rights to first tier subcontractors or suppliers ("a person that provides labor, service, equipment, or material for a public works contract pursuant to an agreement with a direct contractor.") Further, the reference in section (3) to a person described in § 4107.7 appears to be a mistake (Public Contract Code § 4107.7 relates to the impact of a contractor's failure to investigate hazardous material.)

If it is the Commission's intention in adopting § 42030 to restate the rights that are conferred to the same "persons" covered under § 3110 under the current statutory scheme, then the language of the proposed statute fails in a significant way to achieve this goal. On the other hand, if it is the Commission's intent to restrict the scope of potential parties who are entitled to assert stop payment or payment bond rights, then we believe that such an effort is not a desired result nor is it consistent with a general consensus of those who occupy the construction industry. As such, if latter is indeed the Commission's intent, we respectfully suggest that the proposed restriction be eliminated.

(4) Cessation as it determines "completion."

We believe that the elimination of the notice of cessation and the combination of the cessation and completion concepts is an appropriate change. We further believe that the Commission's suggestion about harmonizing the cessation period in the public works scheme (30 days) with its companion in the private works scheme (60 days), is appropriate and should be accomplished.

1. Public Contracts - Preliminary Notice

i. Specific Comments and Recommendations.

(1) Definition of "preliminary notice" (§ 41110)

The definition of "preliminary notice" as provided by this section states that a preliminary notice is a "prerequisite to use of the remedies provided in this part." That statement is incorrect as a preliminary notice is not a prerequisite to the maintenance of a payment bond claim (see, § 45060.) These provisions should be harmonized by including a statement in § 41110 expressly limiting it by § 45060.

(2) Contents of Preliminary Notice

The proposed law attempts to conform the content of the public work preliminary notice to be consistent with the private work preliminary notice. Existing law has different requirements for preliminary notices for private works and public works as set forth in *Civil Code* Section 3097 and 3098, respectively. This welcome modification to existing law should make it easy for claimants on both private works and public works to use one single form, which is already typical in the construction industry.

(a) Substantial Accuracy

The new statute, § 43030, provides that a preliminary notice on a public work shall give various required project information with "substantial accuracy". Without a doubt, the use of the terms "substantial accuracy" is sure to be the focal point of many disputes that will arise in the future.

In contract, §§ 7102 and 7204 (which governs preliminary notices for private works of improvement), does not contain any qualifying language that the information contained in the preliminary notice be stated with "substantial accuracy." California courts have strictly construed the requirements of a preliminary notice. The fact that the proposed law contains this qualifying language may spur an enormous amount of litigation to determine when a preliminary notice on a public work of improvement is substantially accurate. It also may create an unintended divergence between the strict compliance require for a private works preliminary notice versus a less stringent standard on a public work of improvement. Therefore, in order to

further conform the private works and public works statutes concerning preliminary notices, we recommend removing the "substantial accuracy" limitation of § 43030.

(b) Estimate of Total Cost

Current California law requires that a claimant provide a description of the work or materials furnished **and an estimate of the total cost** on private works of improvement. In accordance with a 2001 appellate decision, this estimate must be a derived figure, arrived at by rational analysis. [Rental Equipment, Inc. v. McDaniel Builders, Inc. (2001) 91 Cal.App. 4th 455]. § 43030 is silent as to an estimate of the total cost. We believe it is appropriate require claimants to give an estimate of the total cost of labor or material to be provided on the project so that the prime contractor may protect itself which is the purpose of a preliminary notice. As such, we suggest adding this requirement to the statute.

(3) Disciplinary Action for Failure to Give Preliminary Notice

Current law provides that a subcontractor fails to give a preliminary notice that it shall be subject to disciplinary licensing action if the contract amount exceeds $400. We welcome an update to this statute which no longer subjects a subcontractor to this penalty because the penalty of forfeiting its statutory rights is likely a sufficient penalty to the subcontractor (except inasmuch as the new statute purports to protect laborers compensation funds by preserving the penalty for this limited situation). We would suggest adding a monetary floor to § 43060, however, perhaps at least the sum of $2,000.00.

(4) Additional Suggestions for Modifications to the Proposed Law

(a) § 43040 – Giving preliminary notice

§ 43040(a) permits the claimant on a public work of improvement give its preliminary notice by "mail or personal delivery." While § 42080 clarifies the term "mailed notice" to be delivery by certified mail, registered mail or overnight delivery, there may be confusion by separately defining "mailed notice". Claimants that use the common definition of "mailed" may believe it is appropriate to use first-class mail to deliver a preliminary notice.

Permitting delivery of the preliminary notice by methods ensuring overnight delivery such as Express Mail, Priority FedEx, Overnight UPS, Overnight DHL and other overnight services are welcomed changes. However, § 43040(a), should specifically incorporate the language of § 42080 by either reciting the precise text found therein or by at least providing a reference to § 42080.

Moreover, the phrase "conducts business" in § 43040(b) may be troubling in that it is fairly broad and could encompass many more locations that is otherwise contemplated by the statute. Contractors conduct business at banks, material supplier shops, and many other

locations. We believe that allowing a claimant to serve a notice wherever a contractor maintains and office or at the contractor's residence should be sufficient.

m. Public contracts - stop payment notice

i. Specific Comments and Recommendations.

(1) Duty to Withhold Funds (§ 44150, former 3186).

This section requires the public entity to withhold from the direct contractor, sufficient funds to pay the claim stated in the stop payment notice and to "provide for the public entity's reasonable cost of any litigation pursuant to the stop payment notice". There is no consensus on what a public entity's "reasonable cost of litigation" should be and most public entities routinely withhold 125% of the claim stated in the stop payment notice, consistent with the release bond requirements in § 44180. We suggest that changing the amount to be withheld to "125% of the claim stated in the stop payment notice "would simplify and provide more certainty for public entities' withholding duties.

(2) Notice to Claimants (§ 44170, former 3185)

We suggest that this statute cross reference § 42210, to define "completion" for purposes of timing for the notice. We also suggest that the Commission consider whether the definition of completion in existing Public Contract Code § 7107, relating to disbursement of retention proceeds, should be revised to be consistent with § 42210.

(3) Release Bond (§ 44180, former 3196)

(a) Conditions for Giving Bond.

New § 7510, for private work, eliminated the requirement that a release bond be posted only where the principal **disputed** the correctness of validity of the stop payment notice. It is not clear why this restriction still remains for public works and we suggest that the conditions for posting release bond be the same for private and public work stop payment notice claims.

(b) Public Entity's Discretion.

It is not clear why a public entity has the discretion to refuse to allow posting of a release bond by a financially solvent California admitted surety insurer. There is no similar requirement for private work release bonds and we suggest the requirements for release bonds should be similar for public and private works.

n. Public contracts – payment bonds.

i. Specific Comments and Recommendations.

(1) Payment bond requirement

There is a bit of a contradiction between proposed § 45010(a)(1) and proposed Govt. Code § 14975. One creates a requirement prior to commencement, while the other creates a requirement prior to payment. There is nothing of obvious use to come from this tension.

(2) Construction of bond (§ 45040)

The statement at subsection (c) regarding the "sole" conditions of recovery on the bond is incorrect as it fails to reference notice pursuant to either § 43010 or § 45010 is also a condition.

(3) Statute of limitations

If the Legislature wishes to have a longer statute of limitations for public works than for private works, so be it. However, there is no reason to refer readers to other sections in order to calculate the statute of limitations. § 45050 uses one unit of measurement—the month—then directs the reader to add that with another section which uses a different unit of measurement—a day. Leaving the statute like this would be an obvious missed opportunity to fulfill the goal of simplification and clarification. This statute could simply end, "within 210 days after recordation of a notice of completion or, if a notice of completion is not recorded, within 270 days after completion."

(4) Limitation on chapter

Just as with proposed Civ. Code § 7608(a), proposed Pub. Cont. Code § 45090(a) does not appear to recognize the court decision of Union Asphalt, Inc. v. Planet Ins. Co. (1994) 27 Cal.Rptr.2d 371, 21 Cal.App.4th 1762. Third-tier subcontractors currently have a bond claimant's right in California, and this proposed section may contradict that fact with its plain meaning. The statute needs to be reconciled with Union Asphalt.

3. Conclusion

As we stated at the outset of this Memorandum, we believe that the Commission has made great progress in achieving its goal of simplifying, clarifying and making desired substantive changes to the mechanics lien law. The Commission should be congratulated. We also believe that there is more work to be done to eradicate existing ambiguities, clarify intended changes and make further modifications to those portions of law where consensus for such changes exists in the industry. We stand ready to assist the Commission in this highly important task and we look forward to a further opportunity to review the proposed legislation before it is forwarded to the Legislature for its consideration.