Study H-821 December 15, 2010

First Supplement to Memorandum 2010-53

Mechanics Lien Law: Clean-Up Legislation
(Draft Tentative Recommendation)

The Commission has just received a letter from the Building Industry and Credit Association (hereafter, "BICA"), commenting on two provisions of Senate Bill 189 (Lowenthal), the bill that implemented the Commission's recommendation to reorganize and recodify the existing mechanics lien statute. The letter is attached as an Exhibit.

The letter contains two separate comments. BICA first asserts, with an offered explanation, that a cited provision of SB 189 is "contrary to established law and may lead to unnecessary and costly litigation." Exhibit p. 1. Second, BICA suggests an improvement to another provision of SB 189 that BICA believes would clarify an inadvertent omission by the drafters of the existing mechanics lien statute. Exhibit p. 4.

Although there has not been sufficient time to do an appropriate legal analysis of either matter prior to the Commission's meeting of December 15, 2010, the staff will be prepared to orally discuss with the Commission options as to how to address these matters.

Respectfully submitted,

Steve Cohen
Staff Counsel

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December 14, 2010

VIA EMAIL AND U.S. MAIL

Steve Cohen, Staff Counsel
California Law Revision Commission
4000 Middlefield Road, Room D-2
Palo Alto, CA 94303-4739

Re: SB 189 - Comments Regarding New *Civil Code* Section 8422

Dear Mr. Cohen:

The offices of the undersigned are General Counsel to the Building Industry and Credit Association ("BICA"). The undersigned has practiced exclusively in the field of construction law for the past 30 years, and our firm has a statewide reputation in the construction industry. We represent all segments of the construction industry and do not favor any particular class of participants in the construction industry.

We are writing to express our concern about newly enacted *Civil Code* Section 8422, which does not take effect until July 1, 2012. For the reasons explained below, we suggest remedial legislation to correct deficiencies which we believe are contrary to established law and may lead to unnecessary and costly litigation.

Section 8422(b) provides:

> "Erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, or the work provided, invalidates the claim of lien if the court determines either of the following:
>
> (1) The claim of lien was made with intent to slander title or defraud." (emphasis added).

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It has long been the law of this state that the recording of a mechanic's lien is privileged and cannot be the basis of an action against the mechanic's lien claimant for slander of title. The case of *Frank Pisano & Associates v. Taggart* (1972) 29 Cal.App.3d 1 is directly on point. That case involved a cross-complaint by a property owner, who sued the mechanic's lien claimant for "wrongful disparagement of title", which is an acronym for slander of title. The Court of Appeal, interpreting *Civil Code* Section 47, ruled that the recording of a mechanic's lien was privileged and that a wrongful disparagement of title claim could not be pursued as a matter of law. The following excerpts from the *Frank Pisano* case provide the well-reasoned support for the Court's conclusion:

> "The tort of wrongful disparagement of title has been defined as follows:
>
> > 'One who, without a privilege to do so, publishes matter which is untrue and disparaging to another's property in land, chattels or intangible things under such circumstances as would lead a reasonable man to foresee that the conduct of a third person as purchaser or lessee thereof might be determined thereby is liable for pecuniary loss resulting to the other from the impairment of vendibility thus caused.' (Gudger v. Manton, 21 Cal.2d 537, 541 [134 P.2d 217], quoting Rest., Torts, § 624 [overruled in part on other grounds, Albertson v. Raboff, 46 Cal.2d 375, 381 (295 P.2d 405)].
>
> Plaintiffs contend that the judgment denying the Hymans any award was proper for the recordation of the claim of lien was privileged under Civil Code section 47, subdivision 2. This section provides that a publication made 'In any (1) legislative or (2) judicial proceeding, or (3) in any other official proceeding authorized by law...' is privileged.
>
> The import of section 47, subdivision 2 of the Civil Code was considered by our Supreme Court in the case of Albertson v. Raboff, 46 Cal.2d 375 [295 P.2d 405]. The court held that the filing of a notice of lis pendens was privileged within the meaning of section 47, subdivision 2. (At p. 381.) In reaching its decision, the court made the following statement respecting the scope of the privilege afforded by section 47, subdivision 2: 'It is our opinion that the privilege applies to any publication, such as the recordation of a notice of lis pendens, that is required (e.g., Code Civ. Proc., § 749) or permitted (e.g., Code Civ. Proc., § 409) by

> law in the course of a judicial proceeding to achieve the objects of the litigation, even though the publication is made outside the courtroom and no function of the court or its officers is invoked. [Citation.] Thus, it is not limited to the pleadings, the oral or written evidence, to publications in open court or in briefs or affidavits. [**29 Cal.App.3d 25**] If the publication has a reasonable relation to the action and is permitted by law, the absolute privilege attaches. [Citations.]' (At pp. 380-381.)
>
> [20] Applying this reasoning to the instant case, it must be concluded that the filing of a claim of mechanic's lien in conjunction with a judicial proceeding to enforce it is privileged within the meaning of Civil Code section 47, subdivision 2. The recording of the claim of lien is clearly authorized by law (see former § 1193.1) and it is related to an action to foreclose. (See former § 1198.1.)
>
> We conclude, therefore, that the absolute privilege attached in the present case. The filing of a mechanic's lien was permitted by law and it had a reasonable relation to an action to foreclose the lien. Any deficiencies in the lien procedure were a matter of defense to the action and did not militate against the privilege."

In our opinion, the new language in *Civil Code* Section 8422 is in conflict with *Civil Code* Section 47, as interpreted and applied to mechanic's liens in the *Frank Pisano* case. Whereas, *Civil Code* Section 47 subdivision 2 (as interpreted by the Court of Appeal) provides that the recording of a mechanic's lien is privileged, the new language of *Civil Code* Section 8422(b) suggests that it is not and arguably re-introduces a slander of title claim which has been precluded by *Civil Code* Section 47 and the *Frank Pisano* case.

We, of course, agree that a project owner can and should receive protection from mechanic's liens that are willfully overstated. Newly-enacted *Civil Code* Section 8504 (which is a restatement and clarification of existing *Civil Code* Section 3118) provides such protection, and states:

> "A claimant that willfully gives a false stop payment notice or that willfully includes in the notice a demand to withhold for work that has not been provided forfeits all right to participate in the distribution of the funds withheld and all right to a lien under Chapter 4 (commencing with Section 8400)." (emphasis added).

We respectfully submit that this is a much clearer standard than the new "slander of title" standard set forth in new Section 8422, and newly-enacted *Civil Code* Section 8504 does not conflict with existing law.

We also suggest that a second modification to Section 8422 should receive consideration. Section 8422(b) provides:

> "Erroneous information contained in a claim of lien relating to the claimant's demand, credits and offsets deducted, or the work provided, invalidates the claim of lien if the court determines either of the following:
>
> (1) ....
>
> (2) An innocent third party, without notice, actual or constructive, became the bona fide owner of the property after recordation of the claim of lien, and the claim of lien was so deficient that it did not put the party on further inquiry in any manner." (emphasis added).

We suggest that the highlighted language above be modified to state "bona fide owner or encumbrancer".

As a whole, the statutory scheme for mechanic's liens provide an innocent third party lender ("encumbrancer") the same protection as an innocent third party owner who had no notice of a claim of lien because of deficiencies in the lien. Further, we do not believe that the drafters of this legislation intended to provide protection only for bona fide owners but not "encumbrancers" (lenders).[1] However, because the term "encumbrancers" is used elsewhere in

[1] For example, new *Civil Code* Section 8461, enacted by SB 189, states:

> "After commencement of an action to enforce a lien, the plaintiff shall record in the office of the County Recorder of the county, or of the several counties in which the property is situated, a notice of the pendency of the action, as provided in Title 4.5 (commencing with Section 405) of Part 2 of the *Code of Civil Procedure*, on or before 20 days after the commencement of the action. Only from the time of recording that notice shall **a purchaser or encumbrancer** of the property affected thereby be deemed to have constructive notice of the pendency of the action, and in that event

(footnote continued)

SB 189, a court could conclude that the absence of the word "encumbrancers" in this subsection of Section 8422 was intentional and meant to deny protection to lenders. Accordingly, consistent with the other statutes within SB 189, innocent "encumbrancers" should receive the same statutory protection as "owners" or "purchasers".

Parenthetically, we note that the language in question here was taken by the drafters verbatim from existing *Civil Code* Section 3261. However, since one of the stated purposes of SB 189 is to clarify existing law, we suggest that this clarification be made.

Senate Bill 189 was enacted with a delayed operative date of July 1, 2012. The delayed operative date affords an opportunity to accomplish statutory clean-up before the new statutory scheme takes effect. We believe that the foregoing proposed changes to new *Civil Code* Section 8422 will provide clarification and eliminate conflicts with existing law.

Please contact the undersigned should you have questions.

Very truly yours,

Dale A. Ortmann /sks

Dale A. Ortmann

DAO:sks
cc: Eddie Bernacchi, Politico Group (via email)
Andrea Parisi, BICA (via email)

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only of its pendency against parties designated by their real names."

Similarly, newly enacted *Civil Code* Sections 8316 and 8460, and Section 1203.61 of the *Code of Civil Procedure*, distinguish between a "purchaser" and "encumbrancer" and provide the same protections to both.