Study H-859 April 4, 2016

Memorandum 2016-14

Common Interest Developments: Mechanics Liens and Common Area

The Commission[1] has done extensive work on two different aspects of real property law, common interest developments and mechanics liens. In the course of that prior work, the Commission noted a number of questions that could arise when a mechanics lien right is asserted against property in a common interest development.

This memorandum discusses those issues. It begins by providing general background on the relevant law. Next, it discusses specific problems that could arise. The memorandum concludes by discussing some possible solutions to those problems.

The staff would like to express its appreciation to a number of common interest development attorneys who were informally consulted about their experience with mechanics liens: Adrian Adams, Sandra Bonato, Jasmine Hale, Wayne Louvier, Kelly G. Richardson, and Curtis C. Sproul. The staff is particularly grateful to Allison Andersen, who contributed a significant amount of time providing background on the subject.

BACKGROUND

Common Interest Developments

A common interest development ("CID") is a real property development characterized by (1) separate ownership of a lot or unit (or a right of exclusive occupancy of a unit) that is coupled with an interest in common property, (2) covenants, conditions, and restrictions that limit use of both the common area and separate ownership interests, and (3) management of common property and

1. Any California Law Revision Commission document referred to in this memorandum can be obtained from the Commission. Recent materials can be downloaded from the Commission's website (www.clrc.ca.gov). Other materials can be obtained by contacting the Commission's staff, through the website or otherwise.

The Commission welcomes written comments at any time during its study process. Any comments received will be a part of the public record and may be considered at a public meeting. However, comments that are received less than five business days prior to a Commission meeting may be presented without staff analysis.

enforcement of restrictions by an owners' association. CIDs include condominiums, community apartment projects, stock cooperatives, and planned unit developments.[2]

Residential and mixed-use Common Interest Developments ("CIDs") are governed by the Davis-Stirling Common Interest Development Act ("Davis-Stirling Act").[3] Wholly commercial and industrial CIDs are subject to a separate statute, which includes many, but not all, of the provisions of the Davis-Stirling Act.[4] The issues discussed in this study appear to apply equally to both residential and non-residential CIDs. Therefore, to simplify discussion, this memorandum only refers to the law governing residential CIDs. *It should be understood that the issues discussed in the memorandum may also apply to commercial and industrial CIDs.*

All CIDs have some element of separate ownership of part of the development (a "separate interest") coupled with an interest in "common area." Common area is a *necessary* element of a CID. The Davis-Stirling Act does not apply to real property developments that "do[] not contain common area."[5]

The "common area" is all of the property in the development that is not included in the separate interests.[6] The precise nature of the separate interests and common area, and the manner in which they are owned, is what distinguishes the four different types of CIDs:

- A "condominium project" is a real property development made up of condominiums.[7] Each owner holds a separate interest in a "unit" (which is a three-dimensional volume of space that need not be physically connected to land).[8] A unit owner also holds an undivided interest in the common area.[9] In a condominium project, the common area typically includes the shared structural elements of a building, such as the foundation, interior and exterior walls, hallways, and plumbing and electrical systems.
- A "planned development" is defined in the negative, as "a real property development other than a community apartment project, a condominium project, or a stock cooperative."[10] The separate

2. Civ. Code §§ 4000-6150.2.
3. Civ. Code § 4100.
4. Civil Code §§ 6500–6876.
5. Civ. Code § 4201.
6. Civ. Code § 4095(a).
7. Civ. Code § 4125(a).
8. Civ. Code §§ 4125(b), 4185(a)(2).
9. Civ. Code § 4125(b).
10. Civ. Code § 4175(a).

interest in a planned development is a "separately owned lot, parcel, area, or space."[11] The common area is typically the area around the separate interests, which may consist of roads, landscaping, and other amenities. The common area is owned by either the managing association or by the separate interest owners in undivided interests.[12]

- A "stock cooperative" is a real property development in which a corporation is formed to hold title to the entire development.[13] An owner is a shareholder of the corporation, whose separate interest consists of a "right of exclusive occupancy" of a portion of the property.[14] As in a condominium project, the common area in a stock cooperative may include structural elements of a shared building.
- A "community apartment project" is a real property development in which each owner holds an undivided interest in the development as a whole, coupled with an exclusive right to occupy an apartment.[15] The exclusive right of occupation is the separate interest.[16] Again, the common area may include structural elements of a shared building.

As a further complication, some parts of the common area may be designated as "exclusive use common area" ("EUCA"). These areas are part of the common area, but are designated for exclusive use by one or more of the separate interest holders whose individual interest is appurtenant to the EUCA.[17] Examples of EUCA include parking spaces, balconies, or patios. While EUCA is owned as common area, the responsibility for maintenance and repair of EUCA may be assigned to the associated separate interest owner.[18]

Mechanics Liens

A mechanics lien is a special type of creditor's remedy. In California, it is established in the state Constitution.[19] It provides for a lien on property for those

11. Civ. Code § 4185(a)(3).
12. Civ. Code § 4175(b). There is a somewhat exotic form of planned development in which the "common area" consists solely of reciprocal easements. See Civ. Code §§ 4095(b), 4175(b).
13. Civ. Code § 4190.
14. Civ. Code § 4185(a)(4).
15. Civ. Code § 4105.
16. Civ. Code § 4185(a)(1).
17. Civ. Code § 4145.
18. Civ. Code § 4775(a).
19. Cal. Const. Art XIV, § 3 ("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.").

who have "bestowed labor or furnished material" on a work of improvement of real property.[20]

Procedures to implement the exercise of the lien right are provided in the Civil Code.[21] Because the right to a mechanics lien is a constitutional one, courts generally construe any ambiguities in favor of the claimants.[22]

In the event of nonpayment for the material or services covered by the mechanics lien right, and if the procedural steps discussed below are properly followed, a mechanics lien claimant obtains a security interest in real property that can be enforced through foreclosure.[23]

A mechanics lien is available to a person who "provides work authorized for a work of improvement."[24] The lien "attaches to the work of improvement and to the real property on which the work of improvement is situated, including as much space about the work of improvement as is required for the convenient use and occupation of the work of improvement."[25]

A claimant may only enforce a lien if they have first given preliminary notice to "the owner or reputed owner," the direct contractor, and the lender.[26] A claimant with a "direct contractual relationship with an owner or reputed owner," is not required to give notice to the owner, only the lender.[27] This preliminary notice must be given within twenty days after the claimant has "first furnished work on the work of improvement."[28] Delayed preliminary notice does not totally bar a lien claim, but it does prohibit the lien from covering work performed more than twenty days before serving notice.[29]

To be enforceable, a lien must be recorded within a specified time of "completion" of the work of improvement. The meaning of "completion" varies depending on whether or not the lien claimant is a direct contractor.[30]

---

20. *Id*.
21. Civ. Code §§ 8400-8494.
22. See, e.g., E.G. McGillicuddy Constr. Co. v. Knoll Recreation Ass'n, 31 Cal. App. 3d 891, 897-8 (1973) (noting that doubts should be resolved in favor of the claimant due to "the policy to construe the mechanic's lien law with a view to effect its objects and to promote justice").
23. See Civ. Code § 8460.
24. Civ. Code § 8400.
25. Civ. Code § 8440.
26. Civ. Code § 8200(a); *see* Civ. Code § 8410 (requiring preliminary notice for mechanics liens in accordance with the requirements in §§ 8200 to 8216).
27. Civ. Code § 8200(e)(2).
28. Civ. Code § 8204(a).
29. Civ. Code § 8204(a).
30. Civ. Code § 8412. A "direct contractor" is in privity with the owner. Civ. Code § 8018. Claimants other than direct contractors (i.e. subcontractors as defined in Civ. Code § 8046) must

In general, once a claim of lien is recorded, the claimant then has ninety days to file a civil action to enforce the lien.[31] If the claimant fails to commence action to foreclose within ninety days after recording, the claim expires.[32] Once an action is filed, the claimant must record a lis pendens.[33] An enforcement action may result in the sale of the property to satisfy the amount claimed in the lien.[34]

A person who has perfected a claim of lien also has another remedy, besides enforcement of the lien and foreclosure. The person may give a "stop payment notice" to the construction lender or the owner of the property.[35]

> A stop payment notice … is a written demand by a claimant on the owner, construction lender, builder's control, or other custodian of the construction funds to withhold the sums claimed by the claimant from the sums due the direct contractor or owner. When the stop payment notice is served, it constitutes an equitable garnishment or equitable assignment of the construction loan funds which gives the claimant a lien on the funds being held for the payment of the construction costs.…
>
> Stop payment notices differ from mechanics liens in that they attach to the owner's funds or the construction loan proceeds from a lender rather than the real property being improved. By recording a mechanics lien, the claimant obtains a lien upon the owner's land; by serving a stop payment notice, a priority claim is obtained upon money.[36]

The advantage of a stop payment notice is that it is a claim against money, which can be enforced in the same manner as a money judgment. This is an important alternative remedy when the proceeds of a foreclosure sale of the improved property would not be sufficient to satisfy both the senior lien holders (who have payment priority) *and* the mechanics lien. In such a situation, foreclosure to enforce the mechanics lien would be pointless. By contrast, the stop payment notice provides a way to be paid from currently held funds, without regard to any senior liens on the improved property.[37]

---

record their liens after the claimant's work is finished but before the deadline imposed on direct contractors. Civ. Code § 8414.

31. Civ. Code § 8460(a).
32. Civ. Code § 8460(a).
33. Civ. Code § 8461.
34. Civ. Code § 8466.
35. Civ. Code §§ 8500-8560.
36. Miller & Starr, California Real Estate, *Mechanics Liens, Stop Payment Notices, and Surety Bonds* § 32:68, at 246 (4th ed. 2015).
37. *Id.* at 245.

GENERAL CONCERN

In evaluating the effectiveness of the mechanics lien law as applied to property in a CID, the goals of this study are twofold. First, the mechanics lien statute should provide a meaningful remedy for lienholders that ensures that their state constitutional right is upheld. Second, the statutes should create clear obligations for CID property owners and avoid unduly burdensome or ambiguous requirements.

As discussed below, many elements of mechanics lien law involve action that affects or is taken by the owner of the improved property. This poses no problem when property is owned by a single person or jointly by spouses (as is usually the case for a single detached residential dwelling). But determining the "owner" of improved property becomes more difficult in CIDs, because of the shared ownership structure that is inherent in that form of property ownership. The mechanics lien statute does not define "owner, " but case law indicates that anyone with "some" interest in the property could be considered an owner, "whether as fee owner, life tenant, remainderman, lessee, or whatever."[38]

Suppose that a paving contractor does work on a common area parking lot in a CID. Who is the "owner" of the improved property? In a community apartment project, condominium project, and some planned developments, the common area will be owned by all of the separate interest owners, in undivided interests. In stock cooperatives and some planned developments, the common area is owned by the managing association. Even where the common area is owned by the association, all of the owners arguably have a "some" ownership interest in the common area (as an incident of separate interest ownership).

The problem of determining the "owner" of improved property may be further complicated if work is done on exclusive use common area. Recall that EUCA is generally *owned* as common area, but specific separate interest owners have exclusive use rights and may have special obligations for maintenance and repair.

Even if a lien claimant can determine who the owners are, the shared ownership common to CIDs could create operational problems and unexpected results.

38. Benson Elec. Co. v. Hale Bros. Associates, Inc., 246 Cal. App. 2d 686, 690 (1966).

These complications have not been clearly addressed by the mechanics lien statutes. They are discussed in more detail below.

SPECIFIC CONCERNS

This part of the memorandum discusses how the general concern discussed above — the consequences of shared ownership of property in a CID — plays out in different parts of the mechanics lien procedure.

Authorization of Work

Claimants have a valid mechanics lien right only for work that is "authorized" by the owner.[39] How would this requirement operate when work is done on common area property in a CID? Must every separate interest owner expressly authorize the work? Some very large CIDs have thousands of separate interests.

This question is partially answered in the Davis-Stirling Act, which provides that labor performed on the common areas in a condominium project is deemed to be performed "with the express consent of each condominium owner."[40] This means that a claimant for work on the common area of a condominium project can rely on the authorization of whoever contracted for the work — the individual authorization of every unit owner is not necessary.

However, there is no similar rule for those who improve common area property in other types of CIDs. This seems problematic. Suppose that a contractor does work on the common area in a CID consisting of 500 units. If it is a condominium project, the authorization of the owners is presumed by law. If it is a planned development, the contractor cannot be sure that all owners have authorized the work. What then? Obtain the written consent of all 500 separate interest owners?

The rules on authorization of work may also be a poor fit for work done to improve exclusive use common area. In that situation all those who share ownership of the common area may be "owners," but it may be that only one of those owners has the duty to maintain and repair the property. If a separate interest owner authorizes work on EUCA, which is somehow attached to the separate interest, a contractor may reasonably (and erroneously) assume that the

39. Civ. Code § 8404. Interestingly, Section 8404 does not make mention of a "reputed" owner like other areas of mechanics lien law.

40. Civ. Code § 4615.

work is being done on separate interest property (with the owner being the person who contracted for the work).

Preliminary Notice

To perfect a mechanics lien claim, the claimant must give preliminary notice to "the owner or reputed owner," the direct contractor, and the "lender or reputed lender."[41] Preliminary notice is a "necessary prerequisite" to a lien claim.[42] A failure to give preliminary notice invalidates a claimant's lien rights.

As discussed above, the shared ownership of property within CIDs may make it difficult to know who is the owner of improved property in a CID. For example, if the managing agent of an association in a very large planned development authorizes work to repair the entrance gate, the contractor might reasonably assume that the association is the owner and that preliminary notice need only be given to the association's agent. That may not be technically correct. If the common area is owned jointly by the separate interest owners, in undivided interests, then the contractor arguably needs to give notice to every separate interest owner individually. That invites error and could be absurdly burdensome in a very large CID.

One partial solution to these kinds of problems stems from the fact that the mechanics lien statute permits giving preliminary notice to a "reputed" owner. The term "reputed owner" is not defined in statute, but courts have held that a person may properly be considered the "reputed" owner for the purpose of providing notice of a mechanics lien claim if they are "a person or entity reasonably and in good faith believed to be the owner by those involved with the work of improvement including the general contractor and those furnishing labor, service, equipment or material to be used in the work of improvement."[43] That would avoid some problems, but would not be a complete solution (e.g., where a lien claimant has actual knowledge that the improved property is owned by all separate interest owners, as tenants in common).

41. Civ. Code § 8200(a); *see* Civ. Code § 8410 (requiring preliminary notice for mechanics liens in accordance with the requirements in §§ 8200 to 8216).
42. Civ. Code § 8200(c).
43. Brown Co. v. Appellate Dept., 148 Cal. App. 3d 891, 900 (1983).

Property Identification

Some of the attorneys we consulted expressed concern about liens being recorded without an adequately precise description of the improved property.[44] This could have the effect of clouding title of parts of a CID that were not included within the work of improvement. For example, a condominium development has two residential buildings and each is defined in the governing documents as a distinct and separate common area. Work is performed on only one of the two buildings. Nonetheless, a lien is recorded against the "common area" of the CID, without differentiating between the two buildings. Such a lien would burden more property than is necessary.

"Separate Residential Unit"

Existing Civil Code Section 8448 provides that a condominium project that consists of multiple residential units within a single building may be considered a single residential unit. This is a useful clarifying rule because important elements of the mechanics lien procedure depend on whether work is done on a single residential unit or multiple residential units.[45] Significantly, this provision allows for a single completion date for all residential units in a building, which makes it easier for a developer to clear the entire building as "lien-free" in the subdivision approval process.

There is no parallel provision for other types of CIDs. That omission seems problematic, because other types of CIDs *can* consist of multiple residential units within a single building (e.g., a stock cooperative).

Recordation of Lien Claim

To perfect a lien claim, the claimant must also record the claim against the property with the county recorder.[46] Once enforcement proceedings have commenced, the claimant must also record a lis pendens.[47]

This should be fairly straightforward when work is done on a single separate interest. But the situation is much more complicated when work is done on common area, for two reasons.

---

44. See, e.g., email from Allison Andersen, Andersen Law (Dec. 6, 2015) (on file).
45. See Civ. Code §§ 8448(b)(1) (determination of completion date), (2) (allocation of materials between works of improvement)
46. Civ. Code §§ 8412, 8214.
47. Civ. Code § 8461.

First, because every separate interest includes an incidental ownership interest in the common area, it is not certain whether it would be sufficient to record only against the common area property or whether the lien claim should also be recorded against the title of every individual separate interest. The latter would impose a significant procedural cost on a lien claimant. It would also have a broad effect burdening the title of numerous separate properties for work that does not directly affect their separate interests.

Second, the staff has learned that title for the common area is not always recorded separately from the title for the individual separate interests in a CID. In response to an inquiry from the staff, a representative of the California Land Title Association explained that the practice varies with the type of CID:

> In a condominium, each owner owns a unit and an undivided interest in the common area. There is no separate title record for the common area. In a planned unit development, the common area is usually a separate lot or lots owned by the homeowner's association. In that case, there would be a separate title record for the common area.[48]

Furthermore, it seems likely that a single title record will be recorded for the entire development, including both common area and all separate interests, in a stock cooperative or community apartment project. In those types of CIDs, the entire development is owned by the association or by the separate interest owners as tenants in common, respectively. This further complicates the question of where to record a claim of lien. If a claim of lien is recorded against the development as a whole, then every owner's title will be burdened.

"Blanket Liens"

Because of the confusion surrounding recordation against property in a CID, it is the practice of at least some contractors to record against the entire development, under the existing procedure for what are commonly called "blanket liens."[49] Civil Code Section 8446 authorizes the use of blanket liens:

> 8446. A claimant may record one claim of lien on two or more works of improvement, subject to the following conditions:
> (a) The works of improvement have or are reputed to have the same owner, or the work was contracted for by the same person for

48. See email from Anthony Helton, Legislative Coordinator, California Land Trust Association (Mar. 17, 2016) (on file).
49. See email from Allison Andersen, Andersen Law (Dec. 6, 2015) (on file).

> the works of improvement whether or not they have the same owner.
>
> (b) The claimant in the claim of lien designates the amount due for each work of improvement. If the claimant contracted for a lump sum payment for work provided for the works of improvement and the contract does not segregate the amount due for each work of improvement separately, the claimant may estimate an equitable distribution of the amount due for each work of improvement based on the proportionate amount of work provided for each. If the claimant does not designate the amount due for each work of improvement, the lien is subordinate to other liens.
>
> (c) If there is a single structure on real property of different owners, the claimant need not segregate the proportion of work provided for the portion of the structure situated on real property of each owner. In the lien enforcement action the court may, if it determines it equitable to do so, designate an equitable distribution of the lien among the real property of the owners.
>
> (d) The lien does not extend beyond the amount designated as against other creditors having liens, by judgment, mortgage, or otherwise, on either the works of improvement or the real property on which the works of improvement are situated.

This has the practical effect of burdening title for all separate interests as well as the common area, even when work was done only on the common area. As a result, the separate interest owners may run into difficulties when selling or refinancing their separate interest. To clear the lien (as to their separate interests), owners would need to determine and pay a proportional share of the amount of the claim.[50]

Moreover, it is not entirely clear that the use of a blanket lien is proper when work is done on common area within a CID. Section 8446 authorizes a blanket lien "on two or more works of improvement," when those works of improvement have a common owner (or reputed owner) or when a single person contracts for the work.[51] It seems incorrect to consider a single project affecting the common area to comprise "two or more works of improvement."

At a minimum, the use of a blanket lien is confusing and may unduly burden separate interest title.

50. See Civ. Code § 4615(c).
51. Civ. Code § 8446(a).

Service of Lien Claim

In order to enforce a mechanics lien claim, the claimant must serve a copy of the claim on the owner or reputed owner.[52] Service of process must be made by mail to the owner or reputed owner's residence, place of business, or to the address listed on the building permit.[53] However, the statute provides that "if the owner or reputed owner cannot be served by this method," then service by mail to the construction lender or original contractor is sufficient.[54] In the case of common area with unclear ownership, this provision might serve to protect claimants by allowing them to serve the lender instead.[55]

Failure to serve the claim as specified causes the claim to be "unenforceable as a matter of law."[56] Early case law established that a claim that does not name the owner is still valid "if the names are not known."[57] Recent cases continue to hold that a claim may be enforceable against an owner not named in or served with the original claim so long as the original claim was filed in good faith.[58]

These statutory provisions for naming and serving the owner or reputed owner may be flexible enough to protect claimants where it is unclear who owns improved property in a CID. However, it is not clear that this will always be sufficient to protect a claimant who, in good faith, erroneously serves fewer than all of the owners.

Giving Stop Payment Notice to Owner

A stop payment notice to an owner must be given to the "owner or the owner's architect, if any."[59] If a work of improvement involves an architect, then the stop payment notice can be given to the architect, avoiding any questions about who is the "owner." But if there is no architect, then the same sort of

52. Civ. Code § 8416(c).
53. Civ. Code § 8416(c)(1).
54. Civ. Code § 8416(c)(2).
55. However, this option is only available if the claimant "cannot" serve the owner/reputed owner. This provision likely would not apply if, for example, the claimant was merely inconvenienced by the common area having multiple owners. It would only seem to protect claimants who legitimately could not identify the owner/reputed owner of the property.
56. Civ. Code § 8416(e).
57. Allen v. Wilson, 178 Cal. 674, 678 (1918) (citations omitted).
58. Frank Pisano & Associates v. Taggart, 29 Cal. App. 3d 1, 19 (1972) ("[I]t is sufficient to give only the name of the reputed owner. When an individual does so in good faith, he does not lose his lien if he subsequently determines that some other individual is the actual owner."); see also Wood v. Wrede, 46 Cal. 637, 637-8 (1873) (rejecting mechanics lien claim when claimant knew who the owner was but failed to correctly list the owner in the claim).
59. Civ. Code § 8506(a).

difficulties that were discussed earlier would exist in determining who is the "owner" for the purpose of giving notice.

Sale of Property to Satisfy Judgment

The remedy guaranteed to claimants under mechanics lien law is a foreclosure right on the property for which they have provided labor or materials.[60] However, it is unclear whether this is a meaningful remedy when the lien is for the improvement of common area property in a CID.

As a practical matter, how would a foreclosure sale work when the property to be sold is common area in a CID? In some cases, such property will have little or no value. For example, if a lien is enforced for work to replace a water main under a landscaped common area in a planned development, who would purchase the landscaped area? More problematically, if the common area consists of the structural elements of a building (e.g., the walls, floors, and ceilings of a condominium project), what would it mean to sell that common area property separate from the units that the building contains? Who would purchase such property? The staff suspects that foreclosure would often be a meaningless remedy for common area property in a CID.

The opposite problem could arise in a CID where the entire development is owned by a corporation or by the members as tenants in common (i.e., a stock cooperative or community apartment project, respectively). In that situation, foreclosure would arguably result in the sale of the entire development, including both common area and the separate interests. What would be the effect if someone were to purchase the entire development?

Thus, depending on the type of CID and the work performed, mechanics lien claimants may have a meaningless remedy (forced sale of physically inseverable or valueless property) or they may have a disproportionately powerful remedy (forced sale of the entire development).

It may be that a mechanics lien claim against a CID would never proceed to the stage of foreclosure. The mere recordation of the lien and the threat of enforcement would create enough leverage that the claimant would be paid. But if the CID lacks the funds to pay the claim, or refuses to do so, the lien claimant may be left without meaningful recourse. The CID attorneys consulted by staff generally suggested that lien claims are paid fairly quickly once the separate

60. See Cal. Const. Art. XIV, § 3; Civ. Code § 8460.

interest titles have been burdened by a recorded claim of lien. That kind of leverage may be increased by use of blanket liens, recorded against the title of all of the separate interest properties.

While the leverage that results from a recorded lien against title and the threat of foreclosure may be sufficient to "work things out" in many cases, that may not be sufficient to ensure that all legitimate lien claimants will get paid. Given the constitutional origin of the mechanics lien right, it would be a problem for the remedy to be toothless in some circumstances.

POSSIBLE SOLUTIONS

The issues discussed in this memorandum are technical and may not have easy solutions. It may also be that everyone involved in the intersection between mechanics lien law and CIDs are "muddling through" and achieving acceptable results despite a lack of clarity in the law. **For those reasons, the staff believes it would be useful to have public comment on the issues discussed in this memorandum before the Commission puts too much effort into developing statutory reform proposals.**

Nonetheless, the staff believes it would be helpful to briefly describe a few alternative reforms, to give some idea of the possibilities and to prompt discussion.

Association as "Owner" of Common Area

Many of the difficulties involved in determining the owner of improved property within a CID could be avoided by adding a provision that, regardless of the specific ownership structure of the CID, the association is deemed to be the sole owner of the common area for the purposes of mechanics lien procedures. All CIDs are managed by an association.[61] The association is generally responsible for repair and maintenance of the common area in CIDs.[62]

This approach would address all of the following issues when work is done on common area in a CID:

- The association, acting alone, may authorize the work.
- Giving preliminary notice to the association, as the owner, is sufficient.

61. Civ. Code §§ 4800, 4080.
62. Civ. Code § 4775(a).

- Giving a stop payment notice to the association, as the owner, is sufficient.
- Serving a claim of lien on the association, as the owner, is sufficient.

For those reasons, it may make sense to designate the association as the agent for purposes of mechanics lien procedures.

If that change were made, it might make sense to require that the association notify its membership when it is served with a lien claim.

Separate Interest Owner as "Owner" of Appurtenant EUCA

While exclusive use common area is part of the common area, it is dedicated for the exclusive use of a particular separate interest owner. EUCA will often be physically associated with a particular separate interest in a way that gives an impression that it is part of the separate interest. Typically, a separate interest owner will have the duty to maintain and repair associated EUCA. If a separate interest owner contracts for such work, it is reasonable for those who contribute labor or materials to the work of improvement to assume that the separate interest owner is also the "owner" of the EUCA.

For those reasons, it might make sense to revise the law to provide that a separate interest owner who contracts for a work of improvement for EUCA is deemed to be the "owner" of that EUCA for purposes of mechanics lien processes.

This may already be what is happening with respect to provisions that authorize notice to or service on a "reputed owner."

Require More Specific Identification of Improved Property

As discussed above, a mechanics lien might be framed using a broad and imprecise property description, resulting in recordation against property in a CID that was not part of the work of improvement. The law could be revised to require a more precise property description in documents perfecting and enforcing a claim of lien.

The staff is concerned that such a change could unduly impair lien claimant's rights. Many CIDs have very complicated property descriptions, which can only be understood by closely examining recorded title records (perhaps with advice of counsel). Many lien claimants are non-lawyers and have claims too small to justify hiring counsel. If the lien claim process is too strict, it could cause

claimants to lose their rights over good faith technical errors. **The staff invites public comment on whether a better balance could be struck on this issue.**

Generalize Definition of "Separate Residential Unit"

As discussed above, Civil Code Section 8448 defines "separate residential unit" as including a residential structure that contains multiple residential units. This provides useful clarity, but it only applies to condominiums. The staff sees no obvious policy reason for that limitation. It seems that the same rule could usefully be extended to all types of CIDs.

Clarify Recordation Requirement

When a work of improvement is limited to common area, it would seem to make sense to require that a claim of lien be recorded against the title to that common area, rather than against every separate interest's title or against title to the development as a whole.

However, that may not be possible in all cases. The input we received from the California Land Title Association suggests that some CIDs do not record title to the common area separately from the title to the individual separate interests. To the extent that this is true, there may be no alternative to recording against every separate interest. That strikes the staff as unduly burdensome, both procedurally and with regard to the cloud that would be cast over every owner's title.

The staff is unsure how to address this issue. Suggestions from the experts in the area and interested members of the public would be greatly appreciated.

Alternative to Foreclosure

As discussed above, while a recorded lien and the threat of foreclosure may produce sufficient leverage to secure payment of a lien claim, that may not always be the case. For the practical reasons discussed above, foreclosure and sale of common area property would probably not be realistic in many situations. This could significantly undercut the efficacy of the mechanics lien as a remedy. Possible reforms to address that problem are discussed below.

Inability of CID to Voluntarily Pay Claim

The efficacy of a mechanics lien claim is a particular concern if a CID does not have sufficient funds set aside for payment of the claim, in which case it may not have the *ability* to pay. In general, an association is under an obligation to levy

regular and special assessments "sufficient to perform its obligations under the governing documents and [the Davis-Stirling Act]."[63] That includes a statutory responsibility to repair, replace, and maintain the common area.[64] This would seem to establish a legal duty to raise assessments in order to obtain the funds required to pay a valid lien claim.

However, the Davis-Stirling Act restricts an association's ability to raise assessments, requiring approval by a vote of the CID's membership in certain circumstances.[65] That restriction may prevent a CID from raising the funds necessary to pay a mechanics lien claim.

There is an exception to the statute that restricts assessment increases. It does not apply in certain specified emergency situations.[66] One of those emergencies involves an assessment increase to pay "[a]n extraordinary expense required by an order of a court."[67] It is not clear that an order enforcing a mechanics lien claim would fall within that existing emergency exception.

One reform possibility would be to amend the emergency exception provision to make it applicable where an increase is required to pay a mechanics lien claim that has been found valid in an enforcement proceeding. This would make it easier for an association to levy assessments to meet its obligation to pay a valid lien claim. **The staff invites public comment on the merits of that approach.**

Stop Payment Notice as Alternative to Foreclosure

Another possibility involves the "stop payment notice" remedy discussed earlier. A claimant who has perfected a claim of lien can choose to serve a stop payment notice on the construction lender (if there is one) or on the owner of the improved property (i.e., the owner of the improved common area in a CID).[68] This puts a hold on the use of construction funds, to the extent of the amount claimed, reserving those funds for payment of the claim.[69] A claimant may then bring an action to enforce the claim against the construction funds.[70] If the

63. Civ. Code § 5600(a).
64. Civ. Code § 4775(a).
65. Civ. Code § 5605(b).
66. Civ. Code § 5610.
67. Civ. Code § 5610(a).
68. Service on the "owner" raises the same issues about determining the owner of common area that are discussed above.
69. Civ. Code §§ 8522, 8536.
70. Civ. Code § 8550.

defendant in that action does not pay, the judgment in favor of the claimant may be enforced under the general law on the enforcement of a money judgment.[71] This could include enforcing the judgment against the association's current funds and accounts receivable (most importantly, future assessment revenue).

Existing law seems to contemplate that a mechanics lien claimant might enforce a claim against an association's funds. The Davis-Stirling Act expressly shields some part of an association's regular assessment revenue from judgment creditors:

> Regular assessments imposed or collected to perform the obligations of an association under the governing documents or this act shall be exempt from execution by a judgment creditor of the association only to the extent necessary for the association to perform essential services, such as paying for utilities and insurance. In determining the appropriateness of an exemption, a court shall ensure that only essential services are protected under this subdivision.[72]

Importantly, that exemption does not apply to "any lien for labor or materials supplied to the common area."[73] That is helpful for present purposes, because it makes clear that existing law contemplates enforcement of a mechanics lien claim against an association's regular assessment revenue stream, even giving it priority over the association's need to pay for "essential services."

Clarify Provision Authorizing Enforcement of Lien Claim Against General Assessment Funds

The wording of the provision discussed above is not as clear as it could be, because it is not clear that a mechanics lien can be directly enforced against association funds. A mechanics lien attaches to the improved real property, not the owner's funds. A stop payment notice *does* attach to the owner's funds, but the language of the exception discussed above does not clearly encompass the enforcement of a stop payment notice (which is not exactly a "lien").

It might be helpful to revise the provision shielding regular assessment revenue against judgment enforcement, *to expressly state that the existing mechanics lien exception also applies to the enforcement of a stop payment notice*. **The staff invites public comment on that possibility.**

---

71. *California Mechanics Liens and Related Construction Remedies* § 3.98, at 250 (Cal. Cont. Ed. Bar, 4th ed. 2014).
72. Civ. Code § 5620(a).
73. Civ. Code § 5620(b).

Clarify Funds Subject to Stop Payment Notice

Another potential problem with reliance on the stop payment notice as a remedy is that it only affects funds that have been set aside for the payment of construction costs. If the notice is served on an owner, and the owner has not clearly segregated funds for payment of the project costs, it may not be clear which funds the stop payment notice can be enforced against.

That uncertainty could be addressed by expressly providing that a stop payment notice for the improvement of common area in a CID can be enforced against any funds or revenue of the CID, without regard for whether they have been expressly designated for payment of construction costs. **The staff invites public comment on that possibility.**

Direct Contractor Unable to Give Stop Payment Notice

One last complication regarding the stop payment remedy is that a direct contractor is not allowed to serve a stop payment notice on the owner of the improved property.[74] This makes sense, because the stop payment notice remedy is predicated on the notion that downstream lien claimants are making claims to money that would otherwise have been paid to the direct contractor. That approach doesn't make sense when it is the direct contractor who is making the claim.

This does not leave the direct contractor entirely without an alternative to the mechanics lien. Because the direct contractor is in privity with the owner of the improved property, the direct contractor has the option of bringing an action to enforce the contract (an option that is not available to downstream claimants). That may be sufficient.

Conclusion

With the reforms discussed above, it would be easier for a claimant to enforce a claim directly against the association's funds and revenues (by means of a stop payment notice). The association could then apportion that cost to its members.

Clarify Application of Blanket Lien Procedure

As discussed earlier, some claimants record blanket liens when performing work on common area in a CID, which then burden every separate interest

74. Civ. Code § 8520(a).

owner. That can be problematic if a blanket lien is used in circumstances that the statute does not contemplate or allow.

It might be appropriate to expressly foreclose use of a blanket lien for work performed on common area in a CID. The negative effect this change would have on claimants would perhaps be offset if some of the other reforms in this memorandum are implemented (e.g., clarifying that association is the "owner" for purposes of work on common area, clarifying which property can be recorded against when performing work on common area, providing an alternative remedy that would allow a lien claim to be enforced directly against association funds and revenue). **The staff invites public comment on this possibility.**

If, instead, the blanket lien procedure should apply to common area in a CID, it would be helpful to clarify its use in that context. **Again, the staff invites comment on that approach.**

Make No Changes

One final possibility is that the Commission could leave the law as it stands today. The foreclosure remedy against common area may be theoretically toothless. In practice, however, claimants recording claims against common areas effectively burden the title of owners in a development and generally encourage prompt payment due to the threat of foreclosure. In addition, the use of blanket liens and the wiggle room found in the "reputed owner" concept may provide a way around some of the technical problems associated with common ownership.

NEXT STEPS

If the Commission decides that the problems described in this memorandum are serious enough to pursue further, the staff could draft implementing language for some or all of the possible reforms discussed above (or others) for consideration at a future meeting. This would sharpen the discussion and provide a stronger prompt for public input.

How would the Commission like to proceed?

Respectfully submitted,

Meredith Hankins
Law Student Extern

Brian Hebert
Executive Director