Study H-820

Report to Law Revision Commission Regarding Recommendations for Changes to the Mechanic's Lien Law [Part 2]

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California Law Revision Commission
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[Part 2]

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CONTENTS

1. Introduction

On November 16, 1999, Part 1 of the Mechanic's Lien Study was presented to the Commission pursuant to Memorandum 99-85. As noted in said Memorandum, pursuant to a request from the Assembly Judicial Committee, the Commission agreed to conduct a comprehensive review of the Mechanic's Lien law on a priority basis. The letter from the Assembly Judicial Committee is attached as an Exhibit to Memorandum 99-85.

Part 1 of this Report was submitted in November of 1999. Part 1 dealt with minor substantive and technical revisions. As noted in Memorandum 99-85, the Commission plans to consider Part 2, which will consider broader issues of reform along with other materials at the Commission's second meeting in February 2000.

As noted in Memorandum 99-85, issues have been presented in recent and pending bills. One bill mentioned in said Memorandum is AB 171 submitted by Margett.

Also before the Assembly Judiciary Committee was ACA 5 and AB 742 by Assemblyman Honda, which together would restrict Mechanic's Liens on single-family owner-occupied buildings and establish a Default Recovery Fund for payment of certain unsatisfied obligations of contractors.

As set forth in Memorandum 99-85, the Commission does not take positions on bills but speaks to the Legislature through its own recommendations and bills. However, the subject has been referred to the Commission by one of the policy committees that regularly sees bills concerning Mechanic's Liens and therefore, it is the judgment of the committee that the subject needs a comprehensive review. As noted in Memorandum 99-85, the Commission will not depart from its practice of not taking positions on pending bills, however, it will be necessary to consider the issues raised in the pending bills and the various alternatives to address any potential problems in the law.

In Part 1 of this Report, the issues raised by AB 171, ACA 5, and AB 742 were not addressed at the request of staff. At the hearing on November 30, 1999, the two primary issues of discussion by parties appearing at the hearing centered

around AB 171, ACA 5, and AB 742. It is the purpose of this Report to address those additional issues.

2. Proposal To Eliminate Lien Rights on Single-Family, Owner-Occupied Residences

ACA 5, together with AB 742, proposes that lien claimants shall not have the right to record a Mechanic's Lien on a work of improvement consisting of an single-family, owner-occupied residence where the owner has "paid the contractor in full."[1] The purpose of the legislation was to protect the private homeowner from having to "pay twice." There was substantial support and substantial opposition to that legislation.[2] The Contractor's State License Board (CSLB) who would be administering the trust fund that would substitute for the Mechanic's Lien where the owner had paid the contractor in full opposes the legislation.[3] The CSLB has, in turn, proposed their Home Improvement Protection Plan for the year 2000.[4]

The arguments in support of the proposed legislation are hereinafter set forth. First of all, it should be noted that the proponents of the legislation evidently feel that there is a need for the legislation. That is, on home improvement contracts involving the owner of a single-family residence which is owner-occupied often pay their contractors in full and still end up with Mechanic's Liens on their property. The first argument of the proponents of the legislation is that the Mechanic's Lien remedy is an ineffective substitute for privity of contract. The proponents contend that the homeowner assumes the risk associated with the prime contractor's failure to honor his or her contracts with subcontractors and material suppliers. They argue that since the owner has a contract with the contractor and has paid the contractor in full, the owner should not have to pay twice when the contractor, in turn, fails to pay its subcontractors or suppliers. The proponents of the legislation also contend that the existing laws are inadequate to protect homeowners against non-payment by original contractors and that there are defects in the Preliminary Notice. The proponents of the legislation contend that the warning contained in the Preliminary Notice (Civ. Code § 3097) is inadequate. They take the position that an owner reading said notice would assume that as long as the owner paid the original contractor, they would be fully protected. They further contend that on very small projects, the 20-Day Notice is received after the owner has paid the contractor in full. They further contend that the statutes which protect homeowners are inadequate. They contend that the sections of the Business and Professions Code imposing obligations on contractors to pay their subcontractors and suppliers are inadequate to protect the homeowner from the "rogue" original

1. For the text of ACA 5, see Exhibit pp. 1-2; for AB 742, see Exhibit pp. 3-5; for the Assembly Judiciary Committee consultant's analysis of ACA 5, see Exhibit pp. 6-17.

2. Support and opposition are listed at Exhibit pp. 15-17.

3. See Exhibit pp. 19-22.

4. See Exhibit pp. 23-62.

contractor who fails to abide by the law and fails to pay the subcontractors and suppliers. They further contend that payment bonds are inadequate to substitute as a source of payment for subcontractors. They contend that most contractors on home improvement contracts would be unable to obtain surety bonds guaranteeing payment to subcontractors and suppliers. They take the position that their legislation is narrowly drafted to protect a narrow class of homeowners, to-wit, owners of single-family owner-occupied homes who have paid their original contractors in full.

In essence, the proponents of this legislation contend that the Mechanic's Lien law, as it currently stands, does not provide adequate protection to the owner of a single-family owner-occupied dwelling where a work of improvement is constructed, they have paid their contractor in full and that contractor, in turn, fails to pay subcontractors and supplier. As a result of the foregoing, they perceive a necessity for the legislation in question.

As noted in Part 1 of this Report to the Commission, the Mechanic's Lien law has long been a part of California law. The first California statute relating to Mechanic's Liens was the Act of April 12, 1850.[5] The basic right to a Mechanic's Lien is guaranteed by the California Constitution of 1879 and has remained unchanged to this date.[6] The California Constitution provides that suppliers of labor, services, equipment and materials have a lien upon real property for which they have bestowed such labor, services, equipment and materials and that the Legislature shall provide for the "speedy and efficient" enforcement of that lien. No other creditor's remedy enjoins such "constitutionally enshrined status."[7]

There does not appear to be any substantial evidence that the problem which the legislation seeks to address is a prevailing problem in the construction industry. No evidence has been submitted that there are a substantial number of "homeowners" who have been the victims of the problem of "double payment." This problem has been asserted before the Legislature in the past, but the Legislature has never seen fit to alter the current protections that exist in the law that protect owners. In fact, there is no evidence that this is a substantial problem. As noted in Part 1 of this Report, the California Supreme Court in the *Connolly* case[8] recognized that the protective policy of the Mechanic's Lien law serves the needs of the construction industry. As pointed out by the California Supreme Court in the *Connolly* case, labor and material suppliers are in a particularly vulnerable position. Their credit risks are not as diffused as those of other creditors. They extend a bigger block of credit and they have more riding on one transaction and they have more people vitally dependent upon eventual payment. They have much more to lose in the event of a default. As a result, there must be some procedure

5. Roystone Co. v. Darling, 171 Cal. 526, 530 (1915).
6. *Id.* at 530-31.
7. Wm. R. Clarke Corp. v. Safeco Ins. Co., 15 Cal. 4th 882, 889 (1997).
8. Connolly Dev., Inc. v. Superior Court, 17 Cal. 3d 803 (1976).

for the interim protection of contractors, subcontractors, laborers, and material suppliers in that situation. Without such protection, the improvements could be completed, the loan funds disbursed and the land sold before the claimant can obtain an adjudication on the merits of his or her claim. As noted by the California Supreme Court, as to the interest of the owner whose property is subject to the Mechanic's Lien, the owner suffers only a minor deprivation by reason of the lien since the owner retains possession and use of the property and furthermore, the owners whose account is subject to a Stop Notice, suffers only the encumbrance of the very funds that he or she has previously allocated for the exclusive purpose of paying construction costs. Without recourse to prevent the owner from disposition of the property, the claimant would be left with only an unsecured and potentially uncollectible claim for compensation for the labor, service, equipment or material that has enhanced the value of the property itself. The Supreme Court in the *Connolly* case also acknowledges that the owner and lender can protect themselves against liens and Stop Notices by securing and recording a payment bond from the general contractor under Civil Code Sections 3161, 3162, and 3235. The Supreme Court noted that before recording the Mechanic's Lien or filing a Stop Notice, the claimant is required to serve a Preliminary Notice upon the owner, contractor and construction lender under Civil Code Section 3097. The Supreme Court noted that upon receipt of such notice from one not entitled to claim a lien, the owner or construction lender could immediately file a suit to enjoin the claimant from asserting his or her lien under Code of Civil Procedure Section 526. Further, the owner could, by the use of a temporary restraining order, if necessary, (under Civil Code Section 527, secure a hearing before the lien was, in fact, imposed. The Supreme Court noted that even after the lien has been recorded or a Stop Notice filed, the owner could seek a mandatory injunction ordering the claimant to release the lien. The Supreme Court noted that the owner need not wait until the claimant sues to enforce the lien by reason of the fact that the imposition of the lien and the owner's denial of its validity compromises a controversy sufficient to permit an immediate suit for declaratory relief under Code of Civil Procedure Section 1060. Such a declaratory relief action would have priority on the calendar of the trial court under Code of Civil Procedure Section 1062(a). By filing a action for injunctive or declaratory relief, the owner or lender could obtain a hearing either before imposition of the lien or within a reasonable period thereafter. The Supreme Court therefore concluded that the recordation of the Mechanic's Lien and the filing of the Stop Notice inflicts upon the owner only a minimal deprivation of property; the laborer or materialmen have an interest in the specific property subject to the lien since their work and materials have enhanced the value of the property; state policy strongly supports the preservation of laws which give the laborer and materialmen security for their claims; in measuring those values, the Supreme Court indicated that it did not deal in cold abstractions in that it took into account the social effect of the liens and the interest of the workers and materialmen that the liens are designed to protect and measured those liens against the loss, if any,

caused to the owner; the Supreme Court concluded that the balance tips in favor of the workers and materialmen and therefore concluded that the safeguards provided by the California law to protect property owners against unjustified liens are sufficient to comply with due process requirements and therefore the Supreme Court upheld the constitutionality of the Mechanic's Lien and Stop Notice laws.

The removal of the Mechanic's Lien remedy on home improvement contracts would adversely impact small subcontractors and material suppliers and their employees. The inability to enforce a Mechanic's Lien could result in bankruptcy of the subcontractor and the loss of wages to the employees who worked on the property. Another economic impact would be that contractors and subcontractors would have a much more difficult time in obtaining credit on single-family owner-occupied dwellings. Without the protection of the lien law, many subcontractors would refuse to bid on or work on those types of projects and contractors and subcontractors would find it difficult to find material suppliers that would extend credit to them on those types of projects. This, in turn, would reduce the number of contractors and subcontractors either able or willing to work on home improvements contracts and would drive up the cost of those projects to the homeowner. As a result, the very person that the proposed legislation seeks to protect would be adversely affected from an economic standpoint. Without the availability of the Mechanic's Lien law, material suppliers would most likely put contractors and subcontractors on a COD basis requiring contractors and subcontractors to pay for the materials either before or contemporaneously with delivery of the materials. The contractors and subcontractors on home improvement contracts typically do not have the financial wherewithal to finance both the labor and material costs up front before receiving payment from the owner. To eliminate the right to a Mechanic's Lien in this limited circumstance would adversely impact the construction industry from an economic standpoint, which is one of the primary industries in the state of California.

There are existing protections in the law that adequately protect owners against the so-called "double payment problem." The owner, at the beginning of the job, is going to receive Preliminary Notices from the subcontractors and material suppliers. The Preliminary Notice itself puts the owner on notice that if those parties are not paid, that Mechanic's Liens may be filed. Specifically, the Preliminary Notice required under Civil Code Section 3097 contains the following notice to owner:

> If bills are not paid in full for the labor, services, equipment, or materials furnished or to be furnished, a mechanic's lien leading to the loss, through court foreclosure proceedings, of all or part of your property being so improved may be placed against the property even though you have paid your contractor in full. You may wish to protect yourself against this consequence by (1) requiring your contractor to furnish a signed release by the person or firm giving you this notice before making payment to your contractor or (2) any other method or device that is appropriate under the circumstances.

(It should be noted that this notice was altered inadvertently by legislation that took effect on January 4, 2000. This error is currently being corrected by legislation.)

The Contractors License Law requires that the contractor furnish to the owner of a home improvement project a notice fully advising the owner of the Mechanic's Lien law. Specifically, Business and Professions Code Section 7018.5 requires a contractor entering into a contract with an owner, specified as a home improvement or swimming pool contract, to serve a notice to the owner.[9] That notice carefully advises the owner as to the primary provisions of the Mechanic's Lien law and specifically advises the owner that they may want to require the contractor to supply a payment or performance bond to fully protect the owner. The Contractors License Law has many other provisions that protect homeowners in that it is a ground for disciplinary action for the contractor to abandon a construction project (Bus. & Prof. Code § 7101); to divert or misapply funds (Section 7108); failure to pay subcontractors within ten days of being paid (Section 7108.5); require an unpaid laborer grant a release (Section 7110.1); material failure to complete the project for the price stated in the contract (Section 7113); material failure to comply with the license law (Section 7115); willful and fraudulent act injuring another (Section 7116); willful failure to prosecute work diligently (Section 7119); willful failure to pay money when due for material or services or false denial of liability to obtain a discount or delay (Section 7120). Contractors and subcontractors have knowledge of these provisions of the Business and Professions Code and operate with knowledge of these provisions, which provide them incentive to promptly construct the project and pay the subcontractors and suppliers.

The courts in California have recognized various ways in which an owner may protect his or her interests. Specifically, in the case of *Bentz Plumbing & Heating v. Favalaro*,[10] the court states:

> We do not mean to denigrate the legitimacy of the owner's interest in knowing whether and how much subcontractors and materialmen with potential lien claims on his property have been paid by the prime contractor. We observe, however, that there are several means of protecting their interests. The property owner may limit his lien liability to the measure of the prime contract price by recordation of the contract where a payment bond has been obtained by the prime contractor in an amount equal to 50 percent of the contract price. (Civ. Code, §§ 3132, 3235, 3236.) The owner may himself, by purchase and recordation of a payment bond in like amount, secure priority over mechanics' liens. (Civ. Code § 3139; Connolly Development, Inc. v. Superior Court, *supra*, 17 Cal.3d at p. 808.) Finally, defendants could have issued joint checks to pay for each subcontractor's work (i.e., checks made out to the prime contractor and the subcontractor or materialman as joint payees). Estoppel may be invoked against a subcontractor which endorses a joint check, on the ground that its inclusion as payee makes it clear that the maker

9. See notice at Exhibit p. 63.

10. Bentz Plumbing & Heating v. Favaloro, 128 Cal. App. 3d 145, 151 (1982).

> of the check intends thereby to discharge his obligation to the subcontractor. (Post Bros. Constr. Co. v. Yoder (1997) 20 Cal.3d 1, 5-6 [141 Cal. Rptr. 28, 569 P.2d 133]; Re-Bar Contractors, Inc. v. City of Los Angeles (1963) 219 Cal. App.2d 134, 136 [32 Cal.Rptr. 607]; see also Cal. Construction Contracts and Disputes (Cont.Ed.Bar 1976) §§ 3.55, pp. 123-126; *id.* (Cont.Ed.Bar Supp. 1981) pp. 15-16; Cal. Mechanics' Liens and Other Remedies (Cont.Ed.Bar 1972) § 6.19, p. 161; id., (Cont.Ed.Bar Supp. 1980) pp. 41-42 [importance of using joint checks due to unsettled interpretation of Civil Code § 3262]; Moss, Application of the Doctrine of Estoppel in Construction Industry Litigation (1974) 49 L.A. Bar Bull. 250, 254 [same].)

[Footnotes omitted.]

At noted above, the California Supreme Court in the *Connolly* case stated that the owner and lender can protect themselves against Stop Notices and Mechanic's Liens by securing and recording a payment bond from the original contractor.

The Mechanic's Lien law itself already has adequate provisions protecting owners. Specifically, under the Mechanic's Lien law, the owner may insulate its property from Mechanic's Liens and may insulate its construction loan funds from bonded Stop Notices by obtaining a payment bond. Specifically, under Civil Code Section 3235, if the owner obtains a payment bond equal to 50% of the contract price, from the contractor, and records it in the office of the County Recorder and files the prime contract, the court must restrict recovery under Mechanic's Lien claims to an amount equal to the amount found due from the owner to the original contractor. Thus, if the owner obtains such a payment bond from the contractor, where the owner has paid the contractor in full, the owner will have no liability under the Mechanic's Lien law. Civil Code Section 3236 provides that it is the intent and purpose of Civil Code Section 3235 to limit the owner's liability to the measure of its contract price with the contractor. Civil Code Section 3236 provides that it is appropriate for the owner to protect itself against the failure of the original contractor to make full payment for all work done and materials furnished by exacting such a bond from the contractor. This, of course, was the Legislature's way of balancing the interests of the owner and the interests of the contractor and the unpaid subcontractors, laborers, and material suppliers. It, in effect, provides that the owner will never have to pay twice if the owner obtains a payment bond from the original contractor. The California Supreme Court long ago analyzed the rights of the owner versus the rights of the contractor, subcontractors, laborers, and material suppliers. Specifically, in the case of *Roystone v. Darling*, the court analyzed the Mechanic's Lien law and the method pursuant to which the Legislature addressed the rights or the owner versus the rights of the lien claimants. Civil Code Sections 3235 and 3236 were the Legislature's way of balancing the interests of the lien claimants versus the interests of the owner. Said sections provide that the owner can protect itself against the failure of the original contractor to make full payment for all work done and materials furnished by exacting a payment bond from the original contractor. This balancing of the interests of the owner (to limit the owner's liability for liens to its contract price so that the owner will not

have to pay twice) against the interests of the claimants to be paid where they have improved the owner's property by the simple expedient of bonding the job for 50% of the contract price was extensively analyzed in the landmark case of *Roystone*. Although a very old case, it is still good law and clearly spells out the reason and effect of the bonding provisions. The Supreme Court noted the following: Prior to the adoption of the Constitution of 1879, the lien was a creature of statutes; numerous decisions of the Supreme Court declared that liens were limited by the contract price between the owner and the contractor and could not, in the aggregate, exceed the contract price; the Constitution of 1879 guaranteed the Mechanic's Lien remedy and directed the Legislature to provide for its speedy and efficient enforcement; the statute of 1880 contained a direct declaration that the lien shall not be affected by the fact that no money is due on the contract; in the case of *Latson v. Nelson*,[11] the court considered the power of the Legislature to disregard the contract of the owner and give liens to laborers and materialmen for an amount in excess of the money due from the owner to the contractor and declared that the Constitution was not intended to impair the right of contract and therefore, provisions of the Code granting third parties' lien rights in disregard of and exceeding the obligations of the owner was an invalid restriction of the liability of contract; the Legislature in 1885, recognizing the decision in *Latson v. Nelson*, sought to regulate the mode of making and executing contracts regulating the timing and amounts of progress and final payments; that law remained in effect until the 1911 revisions of the lien law; the cases had held that if there was a contract, that contract limited the amount of liens; the statutes from 1885 to 1911 did not work well; the Act of 1911 was designed to remove the objections to the former law; the revisions of 1911 allow the owner total freedom of contract with the contractor; the 1911 revisions allow the owner to file the contract and record a payment bond for 50% of the contract price and thereby limit its liability for liens to its contract price with the contractor; the 1911 Act provides that the liens shall be direct liens and shall not, in the case of claimants other than the contractor, be limited by the contract price between the owner and contractor (it should be noted that the foregoing is the same principle applicable to the current lien law); the purpose of the 1911 Act was to reverse the policy of the prior act and to now make liens direct against the owner's property and independent of any account of indebtedness between the owner and contractor; the Legislature made the liens direct liens and not limited by the contract price between the owner and the contractor and the intent of the statute was to limit the owner's liability to the contract price where the owner has filed the contract and recorded the payment bond (it should be noted that is still the law in Civil Code Section 3235); where the bond had not been obtained, the contract price is immaterial to the lien (except as to the contractor); where the bond has been obtained and recorded, the contract price controls and the account of the indebtedness from the owner to the contractor is

11. 2 Cal. Unrep. 199, 11 Pac. Coast L.J. 589 (case not officially reported).

decisive on the amount of the lien; in view of the fact that the Constitution grants lien rights and that the Legislature shall provide for the speedy and efficient enforcement of those lien rights, these bonding provisions of the statute which give the owner a "reasonable and practical" mode to improve his or her property through a contractor at a fixed price without further liability is a legitimate exercise of the Constitutional mandate; the 1911 revisions do not deprive the owner of the right to contract to improve his or her property and at the same time exempt his liability for liens by providing reasonable security for the Constitutional right of lien (that is, the payment bond) is "not an unreasonable burden"; the bond required by the Act of 1911 is provided for the express purpose of enabling the owner to escape liability for his or her building in any sum in excess of the contract price; the concurring opinion of Justice Henshaw stated that it was wholly beyond the power of the Legislature to destroy or even impair the constitutionally guaranteed lien right. The foregoing analysis and statements by the Supreme Court in 1915 are as valid today as they were in 1915. The Legislature has balanced the interests of the owner and the lien claimants. The owner can limit its liability for liens and Stop Notices to its contract price if it files the contract and obtains from the contractor a payment bond for 50% of the contract price and records the same. AB 742 adds the additional administrative scheme which is unnecessary and burdensome to the owner, contractor, and lien claimants. The owner is well protected under the existing provisions of the Mechanic's Lien law.

In addition, the Mechanic's Lien law provides for indemnity to the owner for the defaults of the original contractor in failing to make payment to subcontractors, laborers, and suppliers. Specifically, Civil Code Section 3153 provides that where a claim of lien is recorded for labor, services, equipment, or materials furnished to any contractor, that contractor shall defend any action brought thereon at his own expense and during the pendency of such action, the owner may withhold from the original contractor the amount of money for which the claim of lien is recorded. In the event a judgment is entered in the action against the owner foreclosing the lien, the owner is entitled to deduct from any amount due the original contractor the amount of such judgment. If the amount of the judgment exceeds the amount due from the owner to the original contractor, or if the owner has settled with the original contractor in full, the owner is entitled to recover from the original contractor or the sureties on any payment bond any amount of such judgment costs in excess of the contract price for which the original contractor was originally the party liable. In other words, the owner is indemnified by the Mechanic's Lien law for the default of the original contractor in failing to pay subcontractors, laborers, and suppliers.

In light of all the foregoing, it is clear that there is adequate protection that already exists in the myriad of statutes governing the construction industry in the State of California. The proposed statute is unnecessary and would have a substantial adverse economic impact on the construction industry and small homeowners.

It would also eliminate the lien rights of laborers who had participated in building the home.

There are other ways in which the owner could be protected against the "alleged double payment" problem on single-family owner-occupied works of improvement. There are numerous alternatives that could accomplish the purpose which the proposed statute seeks to accomplish. In addition to the bonding of the project, which the owner can currently do under the Mechanic's Lien law, another alternative would be to make the furnishing of a payment and a performance bond mandatory in the case of a single-family owner-occupied dwelling that is the primary residence of the owner. The Mechanic's Lien law could be amended to set forth appropriate provisions requiring bonding in those limited circumstances. The cost of the bonding, of course, is passed on to the owner and it would increase the cost of the project to the owner, but it would provide the owner with ultimate protection from a defaulting original contractor. It would completely serve to protect the owner from the failure of the original contractor to pay subcontractors, laborers, and suppliers. It would likewise protect the owner from failure to complete by the original contractor. The primary objection to any such statute would be claims by contractors that they would be unable to obtain such bonds because they are not "bondable." Those, of course, are the very contractors that shouldn't be in the home improvement business to begin with. If such a provision were enacted, the marketplace would react and surety companies would be willing to write such bonds and would find ways in the underwriting process to protect their interests. Specifically, sureties would take a more active participation in the projects that they bond for small contractors to insure that the money flows down from the contractor to the subcontractors, laborers, and suppliers. This would increase the cost of the bonds and thus the cost to the owner, but would provide the owner with much greater protection from defaulting original contractors. The cost of the bond would be much less than having to litigate and pay Mechanic's Liens.

The costs associated with the proposed statute in terms of the amount it would cost a typical homeowner for attorney's fees generated from the new legal issues raised by the proposed amendment *outweigh* the costs associated with a simple modification to the Mechanic's Lien law requiring that such projects be undertaken only with payment and performance bonds in place. Thus, by this modification to the Mechanic's Lien law, the legislature could more effectively address the double payment problem than by a more drastic amendment to the Mechanic's Lien law. As noted above, the Contractor's State License Board is opposed to AB 742. The CSLB is currently considering alternatives called the Home Improvement Plan for the year 2000 (HIPP 2000).[12] It is recommended that Items 1, 2, 4, 5, 6, 7, and 8 set forth on page 24 of the Exhibit be adopted and particularly the new mini performance bond (new Business and Professions Code Section

12. The alternatives are listed in Exhibit p. 24, and discussed in the pages following.

7071.55, as proposed by the Association of California Surety Companies) be adopted if a full performance and payment bond requirement be deemed too drastic. The mini bond proposal would double the dollar amount available to homeowners in bond protection.[13] This would protect owners of most home improvement projects. This proposal is vastly superior to the drastic and expensive procedures set forth in AB 742.

In light of the foregoing, it is recommended that rather than substantially amending the entire concept of the Mechanic's Lien law, that if a change is perceived to be necessary, that it be in the form of a mandatory bonding provision on private works of improvement where the improvement is an improvement to an single-family, owner-occupied residence requiring mandatory bonding on such projects as has been recommended by the CSLB.

3. Proposal That an Owner Be Required To Notify by Registered or Certified Mail the Original Contractor and Any Claimant Who Has Provided a Preliminary 20-Day Notice That a Notice of Completion or Notice of Cessation Has Been Recorded Within 10 Days of the Recordation of Such a Notice of Completion or Notice of Cessation.

Assembly Bill 171 would require the owner of a public or private work of improvement to notify by registered or certified mail the original contractor and any claimant who has provided a Preliminary 20-Day Notice that a Notice of Completion or a Notice of Cessation has been recorded within ten days of the recordation of such a Notice of Completion or Notice of Cessation.[14] This is an additional statute that was commented upon at the hearing of November 30, 1999. Essentially, the proponents of said legislation contend that the owner of a private or public work of improvement should be required to notify the original contractor and any claimant who has provided a 20-Day Notice that a Notice of Completion or Notice of Cessation has been recorded. This legislation has been submitted on the basis that it is difficult for the claimants on public and private works of improvement to determine whether or not a Notice of Completion or a Notice of Cessation of labor has been recorded. As noted in Part 1 of this Report, the original contractor must record its lien or serve its Stop Notice on private works of improvement within sixty days of recordation of a Notice of Completion or Notice of Cessation, and the subcontractors and material suppliers must record their Mechanic's Liens or serve their bonded Stop Notices on private works of improvement within thirty days of the recordation of a Notice of Completion or Notice of Cessation of labor. The Notice of Completion or Notice of Cessation is, of course, recorded in the office of the County Recorder in the county in which the real property is located. Many original contractors, subcontractors and material suppliers are small companies who do not have the ability or expertise to monitor

13. See Exhibit p. 27.

14. For the text of AB 171, see Exhibit pp. 64-66.

the recordings in the County Recorder's office to determine that a Notice of Completion or a Notice of Cessation has been recorded. Thus, the proponents of this bill assert that when the owner has received a Preliminary Notice from a potential claimant, the owner has knowledge of the fact that it has, in fact, recorded a Notice of Completion or a Notice of Cessation and the owner therefore should, in turn, advise the potential claimants that such a Notice of Completion or Notice of Cessation has been recorded so that the claimants may know that their time for recording liens or service Stop Notices is currently running.

The arguments in opposition to this proposed legislation are that it imposes an unfair burden on owners (particularly individual homeowners) that should not be imposed. The opponents of this legislation argue that claimants should have the obligation to monitor the recordings in the County Recorder's office to determine when a Notice of Completion or Notice of Cessation has been recorded so that they will know that their period for filing claims is running.

Your consultant believes that AB 171 would be beneficial. The claimants, on the one hand are obligated to furnish the owner, contractor and construction lender with a Preliminary Notice by personal service, registered mail or certified mail and therefore the owner is on notice of who the potential claimants are on the project. The owner, in turn, records the Notice of Completion or Notice of Cessation of labor when the project is completed and only the owner knows that it has done so. The claimants' time for recording its Mechanic's Lien or serving its Stop Notice commences to run upon the recordation of the Notice of Completion or Notice of Cessation of labor. It is an extremely short period of thirty days. Requiring the owner to notify the claimants that their time for recording a lien or serving a Stop Notice is running does not seem to be an unreasonable burden upon the owner.