Memorandum 2001-71

Mechanic’s Liens: General Revision

As part of moving the general mechanic’s lien revision along, this memorandum discusses the points raised by Gordon Hunt in his first Report to the Commission and some other comment we have received recommending revisions. Changes approved by the Commission will be implemented in the general revision draft and the work will be completed for review at the meetings scheduled for November.

DRAFTING APPROACH

The staff has been working on a general revision draft and it was to be attached to this memorandum, but the draft is not finished and in view of the lateness of this memorandum, it is not productive to attempt to deal with 150 pages of working materials at the upcoming meeting.

At the June meeting the Commission approved preparation of a general revision draft “scaled to the time available for its completion” so that a bill can be introduced in 2002. At the May meeting, the Commission decided not to adopt the approach of starting with a clean slate and drafting a clear, simpler, and far shorter statute, as suggested by James Acret. The Commission did not believe that there was sufficient time to build a new statute, particularly in view of the lack of consensus among various commentators and the time it would take to work through all the issues presented by a completely new statute.

The existing statute, in this writer’s experience, is one of the “best” examples of confusing language, inconsistent wording, overlong sections, disorganization, and dense verbiage to come before the Commission in many years. The single worst example is Civil Code Section 3097 which “defines” the preliminary 20-day notice. This section first entered California law in 1959 as a one-page substantive provision, and has now more than quintupled into a multifaceted aggregation of provisions sometimes bordering on incomprehensibility. As a conditioning exercise for anyone involved in the process of mechanic’s lien law reform, the staff recommends reading Section 3097 in one sitting.
The confusing state of the law is in large part the result of many amendments accumulating over the decades, without thorough and systematic review and reorganization. Courts have been complaining about the “confused and confusing” mechanic’s lien statute at least since 1915. The recodifications in 1951 and 1969 did not clean up the law to a significant extent. The mechanic’s lien statute was amended 84 times between the 1872 codification and the 1969 move to the Code of Civil Procedure (41 bills were chaptered between the 1951 and 1969 recodifications). In the 30 years since the 1969 codification, 63 bills have been chaptered. The grand total is 148 chaptered bills addressing the mechanic’s lien statute since its first codification in 1872.

The staff approached the general revision by starting with the existing statute and trying to clean it up. Originally, it was hoped some meaningful cleanup could be done by amending sections, but as the work proceeded it became clear that almost all sections needed revision, many of them extensively. Using underscore and strikeout made it very difficult to read heavily revised sections, and some sections needed to be split up into a number of shorter sections and reorganized — a prime example being Section 3097 (preliminary notice). Since this drafting approach seemed not to be working well, the staff switched to the generally preferable law revision approach of repealing the old statute and enacting a new one. This makes the draft much more readable, because it eliminates all of the debris of underscoring and strikeout. On the other hand, it can be more difficult to track detailed language changes. Comments following each section will provide guidance as to the source of new provisions, the disposition of repealed sections, and the relation between the two.

One of the chief goals of the general revision draft is to remove substantive rules and detailed procedures from the definitions, in line with sound drafting principles, and put them where they belong. We have also tracked places where definitions are being used and are attempting to make sure that defined terms are used consistently. One definition does not appear to be used at all, in the defined sense. See Civ. Code § 3105 (“subdivision”).

**Hunt Recommendations**

In his first report to the Commission, Gordon Hunt included 15 numbered suggestions for revision of the mechanic’s lien statute. See Hunt, *Report to Law Revision Commission Regarding Recommendations for Changes to the Mechanic’s Lien*
Law — Part 1 (November 1999) (attached to Memorandum 99-85) [hereinafter Hunt Report]. The following discussion quotes heavily from this report, as indicated by sidelined, single-spaced text. Several matters are also discussed in staff notes in the attached draft. Some emphasis has been added to Mr. Hunt’s commentary by way of boldface type.

Prime Contractor [Hunt Report p. 4]

2. Definition of “Original Contractor” Under the Lien Law

Section 3095 defines an “original contractor” as any contractor who has a direct contractual relationship with the owner. The remainder of the sections relating to the Mechanic’s Lien law are inconsistent in terms of following the definition set forth in Section 3095.…

The term “contractor” is likewise used in Section 3098. In Section 3110, it is stated that for the purpose of the Mechanic’s Lien law, every “contractor” or other person having charge of a work of improvement or portion thereof shall be held to be the agent of the owner. In Section 3112, in referring to payment, there is a reference to “contractor.” In Section 3123(c), it is provided that the owner shall notify the “prime contractor” of any changes in the contract. In Section 3124, the statute refers to a claimant being employed by a “contractor.” There are other examples of these discrepancies throughout the statutes.

All sections dealing with the Mechanic’s Lien law should be consistent and the word “original contractor” should be substituted wherever the term “contractor” or “prime contractor” is used.

The Commission has tentatively decided to use “prime contractor” throughout the statute, instead of “original contractor” or the other possible candidate, “general contractor.” A survey of the California codes finds 42 sections using “prime contractor,” 21 sections using “general contractor,” and 49 sections using “original contractor,” the bulk of them, of course, in the mechanic’s lien statute (42). The staff’s general impression from reading commentaries on mechanic’s lien law is that “prime contractor” is the most common term, even when the mechanic’s lien statute is under discussion.

Elimination of Confusing Provision in Section 3097(b) [Hunt Report pp. 4-7]

3. Preliminary Notice: Delete Civil Code Section 3097(b)

One of the key provisions of the Mechanic’s Lien law is the requirement for Preliminary Notices on both public and private works of improvement. With regard to private works of improvement, Section 3097 requires a Preliminary Notice to the owner, original contractor, and construction lender. This notice is a condition precedent to the right of the claimant to record a Mechanic’s Lien, serve a Stop Notice, or bring an action on any payment bond.…
The purpose of these Preliminary Notice provisions is to provide notice to the owner of who the potential claimants are on the project so that appropriate steps can be taken during the progress of a job, to see to it that those persons are paid so that Mechanic’s Liens are not recorded, Stop Notices not filed, and actions on payment bonds are not brought. In the case of private works of improvement, the owner, of course, has direct knowledge of the persons with whom it has its contractual relationship, to-wit, the “original contractor.”

The lender, likewise, as a practical matter, will have knowledge of who the “original contractor” is. Construction lenders, as a matter of diligent administration of their construction loans, will require a copy of the contract between the owner and the “original contractor” and will have in their files a cost breakdown, usually provided by the “original contractor” for the various line items involved in the construction project as to the amount to be paid for various scopes of work, such as plumbing, electrical, roofing, masonry, drywall, and other such items.

As a result, neither the owner nor the construction lender needs a Preliminary Notice from the “original contractor.” Thus, Section 3097(a) provides that any person not having a direct contractual relationship with the owner must, as a condition precedent to its right to record a Mechanic’s Lien, serve a Stop Notice or bring an action on a payment bond, give a Preliminary Notice to the original contractor, construction lender, and owner. This provides the owner and the construction lender with knowledge of who the potential lien, Stop Notice, and bond claimants are on the project. This, in turn, enables the owner, lender, and original contractor the opportunity to obtain releases pursuant to Section 3262 as progress payments are processed during the progress of the job, to pay the potential claimants by joint check, or to pay the potential claimants directly so that Mechanic’s Liens, Stop Notices, and bond claims can be avoided.…

Section 3097(a) works well in the industry and should not be changed.

Subdivision (b) of Section 3097 has created confusion in the construction industry. Subdivision (b) provides that, except for “the contractor” or one performing actual labor for wages or an express trust fund, all persons who have a direct contract with the owner and who furnished labor, service, equipment, or material for which a lien or payment bond can otherwise be claimed under the Mechanic’s Lien law, or for which a Stop Notice can otherwise be given shall, as a necessary prerequisite to the validity of any claim of lien, claim on a payment bond, or of a Stop Notice (Notice to Withhold), cause to be given to the construction lender, if any, or the reputed construction lender, a written Preliminary Notice.

On the one hand, subdivision (a) of Section 3097 provides that persons not having a direct contractual relationship with the owner must provide a Preliminary Notice to the owner, contractor, and construction lender. Subdivision (b) provides that a person having a direct contractual relationship with the owner “except the contractor” must give a Preliminary Notice to the construction lender. The term “contractor” as noted above is not defined anywhere in the Mechanic’s Lien statute. The question is, who is the “contractor” that Section 3097(b) exempts from giving a Preliminary 20 Day
Notice? It is the belief of the author that this subdivision of Section 3097 was inserted to cover those situations where the owner was acting as an “owner/builder,” that is, where the owner was contracting directly with the trade subcontractors for the various phases of the work.

For example, an owner/builder would contract directly with a subcontractor to do the grading and excavation, then a follow-on subcontractor to do the foundation work, a follow-on subcontractor to do framing and so on through the project. Construction lenders may desire a Preliminary Notice from those “subcontractors” where there is no true “original contractor” in the picture. The statute, however, is ambiguous in that regard.

This author recommends that subdivision (b) be eliminated from Section 3097. Subdivision (a) is adequate and serves the purpose for which it was intended, that is, it places the owner, contractor, and construction lender on notice of all the potential lien, Stop Notice, and bond claimants on the job. Subdivision (b) is ambiguous and unnecessary. Certainly an “owner/builder” knows exactly who all of the trade subcontractors are that it is contracting with for the work of improvement. The owner/builder is therefore in the best position to advise the construction lender who those “subcontractors” are. Further, as a practical matter, during the administration of the project, a diligent construction lender will be demanding from the “owner/builder” copies of all the “subcontracts” that the owner has with the separate trade “subcontractors” and will be requiring waiver and release forms under Section 3262 in the processing of the monthly progress payments.

The staff concurs in Mr. Hunt’s recommendation and the provision is not continued in the draft statute.

Lien for Laborers’ Benefits [Hunt Report p. 8]

4. Requirements in Civil Code Section 3097 To Set Forth the Identity and Address of any Trust Fund in a Preliminary Notice Given by a Subcontractor Who Is Required Pursuant to a Collective Bargaining Agreement To Pay Supplemental Fringe Benefits Into an Express Trust Fund (Section 3097(b)(6)) Should Be Deleted

The courts in California have held that ERISA has occupied the field and therefore, trust fund claimants have no lien rights. It is recommended that the requirement for listing the identity and address of trust funds be deleted from Section 3097. That would likewise require deletion of subdivision (k) of Section 3097.

The staff does not recommend this change. The Legislature has addressed the preemption issue, although the solution has not yet been tested. See 1999 Cal. Stat. ch. 795; see also Sackman, Restoring Mechanic’s Lien, Stop Notice, and Bond Protections, L.A. Law., June 2000, at 19. Regardless of one’s assessment of whether
the 1999 legislation will survive preemption challenges, it would be premature to attempt to repeal this very recent enactment.

**Time to File Stop Notices** [Hunt Report pp. 8-10]

5. *Time To File Stop Notices Should Be Clarified*

The time limits for recording Mechanic’s Liens are set forth in Civil Code Sections 3115 and 3116. Section 3115 provides that each original contractor, in order to enforce a lien, must record a claim of lien after completing the contract and before the expiration of 90 days after completion of the work of improvement, if no Notice of Completion or Notice of Cessation has been recorded or within 60 days after recordation of a Notice of Completion or Notice of Cessation. Thus, as to original contractors, they may not record their liens until they have completed their contract and no later than 90 days after completion or 60 days after recordation of a Notice of Completion or Notice of Cessation. With regard to claimants other than an original contractor (to-wit, subcontractors and material suppliers), Section 3116 provides that they may record their liens after they have ceased furnishing labor, service, equipment, or materials and no later than 90 days after completion of the work if no Notice of Completion or Notice of Cessation has been recorded or within 30 days after the recordation of a Notice of Completion or Notice of Cessation. As a result of these two sections, if an original contractor records its lien before it has completed its contract, that lien would be premature. Likewise, if a subcontractor or material supplier were to record its lien before it had ceased furnishing labor, service, equipment, or materials, its lien would be premature.

With regard to “Stop Notices for Private Works of Improvement” in Chapter 3, Sections 3156-3176.5, the statute provides in Section 3158 that claimants other than the “original contractor” may give to the owner a Stop Notice. It further provides that any person who shall fail to serve such a Stop Notice, after a written demand therefor from the owner, shall forfeit his right to a Mechanic’s Lien. Section 3159 provides that claimants may, prior to the expiration of the period of time within which his or her claim of lien must be recorded under Chapter 2, serve upon the construction lender a Stop Notice or bonded Stop Notice.

Section 3103 defines a Stop Notice and provides what it must contain, including a statement in subdivision (c) that the Stop Notice must contain the amount in value as near as may be of that already done or furnished and the whole agreed to be done or furnished. This statement is necessary by reason of the last sentence in Section 3158, which provides that “Any person who shall fail to serve such a Stop Notice after a written demand therefor from the owner shall forfeit his right to a Mechanic’s Lien.” The purpose of that last sentence in Section 3158 is to enable the owner to determine, during the progress of the job, what subcontractors or material suppliers have outstanding claims and if, in fact, a demand is made by the owner upon a subcontractor or material supplier to file a Stop Notice, when they are in the middle of the job, they would set
forth in the Stop Notice, under Section 3103, the amount in value of that they had already done and the whole agreed to be done or furnished.

Some practitioners have concluded, by virtue of the foregoing, that an unpaid claimant may, at any time during the progress of the job, serve a Stop Notice on the owner or a bonded Stop Notice on the construction lender, even though that claimant is still furnishing labor, service, equipment, or material to the jobsite. As a practical matter, that practice is being conducted in the construction industry and creating havoc on construction projects. Once the Stop Notice or bonded Stop Notice is filed, the owner and/or construction lender will withhold progress payments. The foregoing procedure is inconsistent with the provisions of Sections 3115 and 3116. It is therefore recommended that Sections 3115 and 3116 be amended to make them applicable to both Mechanic’s Liens and Stop Notices or bonded Stop Notices. As amended, Section 3115 would read as follows:

Each original contractor, in order to enforce a lien or bonded stop notice, must record his or her claim of lien or serve his or her bonded stop notice upon the construction lender after he or she completes his or her contract and before the expiration of….

The wording set forth above is to make Section 3115 the guiding statute as to both the recordation of the lien or the service of a bonded Stop Notice on a construction lender. The reason that it only references a bonded Stop Notice filed with the construction lender is that original contractors may file bonded Stop Notices under Section 3159, but only persons other than original contractors may serve Stop Notices on an owner pursuant to Section 3158.

Section 3116 would be amended to read as follows:

Each claimant other than an original contractor, in order to enforce a mechanic’s lien, or to serve a stop notice upon an owner or a bonded stop notice upon a construction lender, must record his or her claim of lien or serve upon the owner a stop notice or serve upon the construction lender a bonded stop notice after he or she has ceased furnishing labor, services, equipment, or materials….

The foregoing amendments would make it clear that the time limits for recording Mechanic’s Liens and serving Stop Notices are identical. The only time that a claimant would have the obligation or the right to serve a Stop Notice upon the owner before the claimant finished its work or before it ceased furnishing labor and material on the project would be in that limited circumstance where the owner would, pursuant to Section 3158, demand that the claimant serve a Stop Notice upon it.

The staff recommends implementation of the substance of this suggestion. Because of the proposed restructuring of the mechanic’s lien statute in the draft, the language will vary. The staff has doubts, however, about the operation of the demand provision in Section 3158. We wonder if it would be better to repeal the demand rule. If its purpose is to enable the owner to determine what is owing at various stages of the project, it would seem to be a cumbersome way to
accomplish that goal, since it involves invoking a creditor’s remedy with other consequences.

Attorney’s Fees in Action on Stop Notice [Hunt Report pp. 10]

6. Civil Code Section 3176 Should Be Amended To Clarify an Ambiguity

Civil Code Section 3176 allows courts to award attorney’s fees and costs to the prevailing party in any action against an owner or construction lender to enforce payment of a claim stated “in a bonded stop notice.” This section is ambiguous by reason of the fact that a Stop Notice served upon an owner need not be bonded.

... The only requirement for bonding is with regard to a Stop Notice served upon a construction lender on a private work of improvement. Specifically, under Section 3162, withholding by the construction lender on a private work of improvement, is optional unless the Stop Notice is bonded, in which event withholding is mandatory.

As a result of the foregoing, there is no provision for a “bonded stop notice” to be served on a private owner. Accordingly, Section 3176 should be amended by amending the first paragraph to read as follows:

In any action against an owner on an unbonded stop notice or against a construction lender to enforce a payment of a claim stated in a bonded stop notice, the prevailing party shall be entitled to collect from the party held liable by the court for payment of the claim, reasonable attorney’s fees in addition to other costs and in addition to any liability for damages.

This will make Section 3176 compatible with the requirements for Stop Notices served upon an owner and bonded Stop Notices served upon a construction lender.

The staff has doubts about this proposal. The staff does not necessarily agree that the section is ambiguous. It provides for attorney’s fees where there is a bonded stop notice, regardless of whether a bonded stop notice is “required.” But even as to lenders, the stop notice is not required to be bonded, unless the claimant wants to invoke the feature of Sections 3159 and 3162 requiring the lender to withhold (except that withholding is still not required if a payment bond has been previously recorded under Section 3235). Whether a stop notice is required to be bonded to achieve a particular result is a separate issue from the conditions for attorney fee liability.

From the standpoint of the claimant, service of a bonded stop notice is required to have a right to attorney’s fees. Read literally, the statutory correspondence is between bonding and attorney’s fees, not between attorney’s fees and whether the recipient of the stop notice is required to withhold pursuant to the notice (whether bonded or not). The staff does not claim to understand the
full implications of either theory at this point, and so is unable to recommend revising the statute to extend liability for attorney’s fees. Further research will need to be done.

Claims Includable in Stop Notices [Hunt Report pp. 10-11]

7. Civil Code Section 3123 Should Be Amended To Expressly Cover Stop Notices in Addition to “Liens”

Civil Code Section 3123 sets forth the amount of the “lien.” Section 3123(b) was amended to allow claimants to include in their “lien” amounts due for written modifications of the contract or as a result of the rescission, abandonment, or breach of the contract. This section does not set forth that Stop Notices may likewise include those sums.

Section 3123(b) was recently interpreted in Basic Modular Facilities, Inc. v. Ehsanipour [83 Cal. Rptr. 2d 462 (1999)] to expressly hold that a lien claimant could include, in its Mechanic’s Lien, damages for breach of contract. No court has yet addressed whether or not a Stop Notice can include damages for breach of contract and the other items specified in Section 3123(b). Most practitioners believe that the Stop Notice is co-extensive with the Mechanic’s Lien and whatever amounts are includable in a Mechanic’s Lien would likewise be includable in a Stop Notice or bonded Stop Notice.

In order to clear up any ambiguity in that respect, it is suggested that Section 3123 be amended to apply to both liens and Stop Notices by adding a reference to “stop notice and bond claims” after references to “lien” or “liens” in this section.

The staff recommends approval of the substance of this proposal. We can see no reason for inconsistency between the claims covered by one remedy versus another. Ideally, the statute should be simplified throughout by eliminating this type of inconsistency and the need for repetitive wording, which itself is an invitation to inconsistent revisions in future years.

Presumption Concerning Use of Materials [Hunt Report pp. 11-12]

8. The Mechanic’s Lien Law Should Be Amended To Provide That Proof of Delivery of Material Creates a Rebuttal Presumption of Use of the Material in the Work of Improvement

It is a simple matter for a contractor or subcontractor to testify directly as to the work, labor, service, or material that it provided in connection with the work of improvement. Material suppliers, however, sell their materials either to original contractors or subcontractors. Sometimes those materials are delivered directly to the jobsite and other times they are not. In some instances, the materials are delivered, first of all, to an original contractor’s or subcontractor’s
place of business for fabrication and later installation in the work of improvement.

A classic example of this procedure is the furnishing of steel materials by a steel supplier to a subcontractor who has contracted to fabricate and erect the structural steel on a project. In most instances, that steel will be delivered directly by the material supplier to the subcontractor’s place of business and will be fabricated at that place of business in accordance with the plans and specifications and then delivered to the jobsite for installation.

Where a material supplier delivers its material directly to the jobsite, once the material arrives at the jobsite, the material supplier loses control of the material and typically has no direct knowledge as to the installation of the material in the work of improvement. The courts have held that mere delivery to the jobsite is not sufficient. The claimant is obligated to prove not only that its materials were furnished for use in the work of improvement, but that, in fact, the materials were used in the work of improvement. [citations omitted]

A logical inference to be drawn upon proof of delivery of material to the jobsite is that, in fact, the material was used in the job, in absence of some evidence that it was removed from the job after delivery. Accordingly, it is recommended that a section be added to the Civil Code providing that proof of delivery to the jobsite creates a rebuttable presumption that the material was used in the job and the burden of proof then shifts to the owner to prove that it was not....

This would be a substantive revision, but the staff is not sure how significant it would be in practice. The staff is inclined to believe this is a sensible proposal, but we have not fully researched the issue. There may be preferable alternatives. For example, the Uniform Construction Lien Act (1987)

allows a lien if seller’s belief that the goods are to be used on a particular site is evidenced either by a notation on the sales contract, by a delivery order, or by actual delivery to the site.

However, except with respect to materials specially fabricated for the particular real estate and not salable in the ordinary course of the materialman’s business, a materialman gets no lien unless the materials are actually used in the making of the improvement. A lien is given to persons who supply materials such as gasoline, which are consumed in the course of the improvement ....

[UCLA Pref. Note at 3.] Section 204 of the uniform act provides, in part:

(b) The delivery of materials to the site of the improvement, whether or not by the claimant, creates a presumption that they were used in the course of construction or were incorporated into the improvement.
9. Attorney’s Fees in Mechanic’s Lien Foreclosure Proceedings

The treatment of attorney’s fees in the Mechanic’s Lien law is not consistent. As noted above, with regard to Stop Notices and Bonded Stop Notices on private works of improvement, the Code provides for attorney’s fees to the prevailing party in an action on a Bonded Stop Notice. There is no attorney’s fees provision in the statute with regard to Mechanics’ Liens. In fact, the courts have held that attorney’s fees are not recoverable pursuant to a Mechanics’ Lien [Abbett Elec. Corp. v. California Fed. Sav. & Loan Ass’n, 230 Cal. App. 3d 355 (1991)]. On public works of improvement, attorney’s fees are recoverable on the Payment Bond (Section 3250), but are not recoverable in an action to enforce a Stop Notice on public works [citations omitted]....

The question is more difficult with regard to private works of improvement. There appears to be no rational basis to allow attorney’s fees in an action on a Stop Notice on private works but not allow attorney’s fees in an action to foreclose a Mechanics’ Lien. The provision for attorney’s fees is important in that it quite often results in serious settlement negotiations between the parties and enhances the possibility of settlement where the parties know that the prevailing party will be entitled to recover attorney’s fees. A recent California Supreme Court case [Scott Co. of Cal. v. Blount, Inc., 20 Cal. 4th 1103, 979 P.2d 974, 86 Cal. Rptr. 2d 614 (1999)] highlights the importance of attorney’s fees and the interplay with the statutory offers of settlement that can be made under Code of Civil Procedure Section 998 coupled with the provisions of Civil Code Section 1717 allowing the prevailing party to recover attorney’s fees where attorney’s fees are provided for.

It is therefore recommended that the Mechanics’ Lien law be amended to provide for attorney’s fees to the prevailing party in an action to foreclose a Mechanics’ Lien. This could be accomplished by adding a subdivision (c) to Section 3144, as follows: “In any action to enforce a Mechanic’s Lien, the court may award the prevailing party reasonable attorney’s fees.” This section is based upon Arizona Revised Statutes, Section 33-998(B).

The staff does not recommend adding general liability for attorney’s fees to the mechanic’s lien statute in the course of this general revision. This would be a significant change and is likely to be controversial. The basis for the liability for attorney’s fees in enforcement relating to bonded stop notices is unclear to the staff, so we decline Mr. Hunt’s invitation to leap from that liability into a global liability for attorney’s fees in mechanic’s lien enforcement. If we desire consistency, the far less disruptive approach would be to delete the liability for attorney’s fees under certain bonded stop notices. If the Commission is interested in pursuing this issue, the staff suggests that it be made the focus of a separate study with a view toward introducing a separate bill.
10. Revisions to Civil Code Section 3262

For years, the construction industry operated on the assumption that lien waiver and release forms used during the processing of progress payments during the job would result in waiver of the claimant’s lien, Stop Notice, or bond rights once payment was in fact made. In the case of Bentz Plumbing & Heating v. Favaloro, [128 Cal. App. 3d 145 (1982),] Bentz Plumbing as a subcontractor submitted lien waivers to the original contractor totaling $14,500. Bentz Plumbing only received $6,750 from the original contractor and recorded a Mechanic’s Lien for $14,406.49. The owner had paid the original contractor in reliance upon the waivers that Bentz Plumbing had executed. The appellate court held that the waivers were null and void under Section 3262 as it existed at that point in time.

The industry was taken aback by virtue of that decision and sought to amend Section 3262. As a result, the Legislature got into the “form writing business.” The statute was amended in 1984 to provide for four waiver and release forms, to-wit, a conditional and unconditional waiver and release upon progress payment and a conditional and unconditional waiver and release upon final payment.

In 1992, the case of Halbert’s Lumber, Inc. v. Lucky Stores, Inc. [6 Cal. App. 4th 1233, 8 Cal. Rptr. 2d 298 (1992)] denied a material supplier its Mechanic’s Lien for material delivered to the job site, but not installed, where the material supplier signed a conditional waiver waiving all lien rights for material “furnished” through a date subsequent to the date of the delivery of the materials to the job site. The court held that the material supplier had therefore waived its lien rights.

In response to the Halbert’s Lumber case, the statute was amended again effective January 1, 1994. The new forms provide that any retention retained before or after the release date is not waived. They further provide that any “extras” furnished before the release date for which payment has not been received are not waived. Although the term “extras” is not defined in the statute, it is a term of common knowledge in the construction industry meaning labor, service, equipment, or material furnished beyond the scope of the work as called for in the original contract documents. The forms also do not release “extras” or “items” furnished after the release date. The forms also provide that rights based upon work performed and items furnished under a written change order which has been fully executed by the parties prior to the release date are released unless the claimant specifically reserves those rights in the release. The language that has created substantial ambiguity, and which has not been decided by the courts, is the language in Section 3262(d)(1) reading as follows:

This release of any mechanics’ lien stop notice or bond right shall not otherwise affect the contract rights, including rights between parties to the contract based upon a rescission, abandonment, or breach of the contract, or the right of the undersigned to recover compensation for furnished labor, services, equipment, or
material covered by this release if that furnished labor, services, equipment, or material was not compensated by the progress payment.

This language, if interpreted in accordance with its plain terms, seems to convert the conditional waiver and release upon progress payment to a mere receipt. In other words, the language states that if the claimant is not being paid for “furnished” (past tense), labor, services, equipment or material, then the claimant is not waiving its rights with regard to that “furnished” (past tense) labor, services, equipment, or material.

The statute has been subject to much criticism ... [quotations from several articles omitted]:

James Acret states the following [citation omitted]:

Compensation for work or material ‘not compensated by the progress payment’: this language is flagrantly ambiguous. At minimum, it means the claimant preserves all personal causes of action and releases only Mechanics Lien, Stop Notice, and bond rights. This would include the contract rights discussed above. Thus, the language seems duplicative unless it also (under a broader interpretation) preserves the claimant’s Mechanics Lien, Stop Notice, and bond rights for all work or materials ‘not compensated by the progress payment’. But such an interpretation seems absurd. It would nullify the effectiveness of the release in the only circumstances under which it could be of any practical value, since it is only ‘unpaid’ claimants who assert Mechanics Lien, Stop Notice, and payment bond rights to begin with.

The amendments to the unconditional release on progress payment track the amendments to the conditional release on progress payment, but one provision of the Unconditional Waiver and Release moves from the Byzantine to the Rococo: it is the notice that this release is enforceable against you if you sign it even if you have not been paid. Wait a minute! Didn’t we just read that this release does not cover claims that were not compensated by the progress payment?

The industry operates on the assumption that if the claimant is paid a certain amount through a given date, then all of its liens, Stop Notices, and Bond rights through that date are waived with the exceptions noted in the release form. Most people in the industry believe that they are giving full releases when in fact they are not. It is clear that the forms in Section 3262 need to be revised or the statute itself revised. In light of the fact that these waiver and release forms have become common practice in their usage in the construction industry, it is recommended that the forms be revised.

In an earlier letter to the Commission, James Stiepan of the Irvine Company termed the entire lien release process regarding progress payments to be “little more than a meaningless exercise.” (See First Supplement to Memorandum 99-85, Exhibit pp. 1-2.) He finds Gordon Hunt’s revisions a “step in the right direction,” but advocates some additional clarifications.

James Acret suggested revision of the release rules in his simplified mechanic’s lien draft. (See Memorandum 2001-41, Exhibit pp. 2-3.) His suggested rule reads:
A release of, or agreement not to enforce, mechanics lien, stop notice, or payment bond rights that is contained in the text of a construction contract or sales agreement is void. A release of mechanics lien, stop notice, or payment bond rights for assets that have not yet been furnished is void except to the extent that the assets have actually been paid for, and except that such a release is enforceable by a party who has reasonably relied upon such a release to its detriment without knowledge of nonpayment.

The staff agrees that the release rules and forms need to be revised, but we have not yet had time to formulate a proposed solution. It is the Commission’s historical view that enactment of statutory forms is unwise. Regardless of whether the rules are (unwisely) imbedded in mandatory form language or are (preferably) stated in substantive provisions, this area should be cleaned up.

Completion [Hunt Report p. 16-17]

11. Proposed Revision to Civil Code Section 3086

Civil Code Section 3086 defines “completion” and the equivalents of completion. Completion is defined in the case of any work of improvement other than a public work of improvement as the actual completion of the work of improvement. This of course is a question of fact in each case that needs no further amendment. Section 3086 also sets forth certain equivalents of completion …. The last paragraph of Section 3086 up to the semicolon should remain as is. The language reading as follows should be deleted:

...provided, however, that except as to contracts awarded under the State Contract Act, Chapter 3 (commencing with Section 14250), Part 5, Division 3, Title 2 of the Government Code, a cessation of labor on any public work for a continuous period of thirty (30) days shall be deemed a completion thereof.

The foregoing provision is unnecessary and a trap for the unwary. There is no legitimate reason for an exception for local public works contracts which have a cessation of labor for thirty days to start the time for filing Stop Notices or claims on the payment bond to run. On many public works projects there will be delays that exceed thirty days. Those are adequately covered in subdivisions (a), (b) and (c). In the case of W.F. Hayward Co. v. Transamerica Ins. Co., 16 Cal. App. 4th 1101 (1993), a subcontractor lost its bond rights when the original prime contractor was terminated on a County of Los Angeles job and labor ceased for more than 30 days. The time for filing claims should be as set forth in subdivisions (a), (b), and (c), and therefore it is recommended that the language quoted above be deleted.

The staff thinks that the suggested revision is acceptable. This also raises the issue of the desirability of removing provisions relating to public works from the mechanic’s lien statute. (This issue was discussed in Memorandum 2001-41,
The special rules in the Public Contract Code create a source of confusion and lead to inconsistencies between the two sets of statutes applicable to public works contracts.

In 1982, the Public Contract Code was created — 13 years after the mechanic’s lien statutes were moved to the Civil Code from the Code of Civil Procedure and other sources. The new code pulled sections together from a number of other codes, including the Education Code, Government Code, Streets and Highways Code, and Water Code.

Public Contract Code Section 100 reads, in part: “The Legislature finds and declares that placing all public contract law in one code will make that law clearer and easier to find.” Contractor and supplier remedies relating to public construction contracts go hand in hand with the provisions governing the contract terms and bidding process. Under the existing scheme, the stop notice procedure seems to be consolidated in the Civil Code, but there are many other bond provisions in the Public Contract Code and probably elsewhere. See, e.g., Pub. Cont. Code §§ 4100 et seq. (Subletting and Subcontracting Fair Practices Act), 7103 (most state entity works over $5,000; others under Civ. Code § 3247), 10100 et seq. (State Contract Act), 10700 et seq. (Cal. State Univ. Contract Law), 20100, 20104, etc. (Local Agency Public Construction Act).

From a law revision standpoint, it is obvious that provisions relating to bonding remedies in public works belong in the Public Contract Code. There are too many differences, special provisions, and exceptions to justify continuation of the public works provisions currently in the Civil Code mechanic’s lien statute.

**Discipline for Contractor’s Failure to Provide Information** [Hunt Report p. 17]

12. Make Failure of Contractor To Make Available Name and Address of Owner and Lender a Ground for Disciplinary Action

Subdivision (l) of Civil Code Section 3097 now provides that the “original contractor” “shall” make the name and address of the owner and lender as shown in their contract available to any person wanting to serve a Preliminary Notice. **Even though the statute uses the word “shall” (mandatory), there are no teeth in the statute.** As a practical matter, many times when potential claimants (subcontractors and material suppliers) contact the “original contractor” to obtain the name and address of the owner and lender as shown in the original contractor’s contract with the owner, the original contractor is uncooperative and either fails to furnish the information or furnishes inaccurate information. It is recommended that subdivision (l) be amended by adding the following language:
The failure or refusal of the original contractor, licensed under Chapter 9 (commencing with Section 7000) of Division 3 of the Business and Professions Code, to make this information available as required by this subdivision, constitutes grounds for disciplinary action by the Registrar of Contractors.

The staff has no recommendation on this suggestion. We are not in a position to assess whether it is useful to add this duty or whether making it a ground for discipline would be effective. We have heard allegations that enforcement of discipline under the Contractors’ State License Law in California is subpar — whether this is a fair or accurate assessment, we don’t know. But if the Contractors’ State License Board is not able to enforce existing rules, we doubt the utility of adding additional disciplinary matters to their agenda. A far better approach is to provide statutory consequences, particularly when they are logical, as proposed with regard to the double payment problem. Relying on punitive measures by a regulatory body is not likely to be as effective.

This raises the general question of what in the mechanic’s lien law should provide a ground for disciplinary action. Should the statute pick and choose or, leaving aside our concerns about the effectiveness of the penal approach, should there be a general provision making violation of any duty imposed on a licensee a ground for discipline?

Seeding Copies of Payment Bond [Hunt Report pp. 17-18]

13. Require Owner to Furnish Copy of any Payment Bond to any Claimant Who Serves a Preliminary Notice on the Owner

Often times an owner will acquire a payment bond on a private work of improvement and not record it. Additionally, it is difficult for the subcontractors and material suppliers to search the records of the County Recorder’s office to ascertain whether or not a payment bond has been recorded. Arizona’s Preliminary Notice section has such a provision. See Ariz. Rev. Stat. § 33-992.01. This procedure could be implemented by adding [language] to Section 3097 reading as follows:

Within ten (10) days of the receipt of a Preliminary Notice, pursuant to this section, if any payment bond has been obtained but not recorded or obtained and recorded in compliance with Section 3235, the owner and contractor must provide a copy of the payment bond, including the name and address of the surety and bonding agent providing the payment bond, to the person who has given the Preliminary Notice. In the event that the owner or contractor fails to provide the bond information within that ten-day period, the claimant shall retain lien rights and stop notice rights to the extent precluded or prejudiced from asserting a claim against the bond as a result of not timely receiving the bond information.

The language set forth is adopted from the Arizona Mechanic’s Lien law.
The staff does not support this recommendation. We are concerned about adding more technical duties and layers of paper-shuffling, and increasing the complexities of the statute and multiplying the interrelations of notices, bonds, releases, claims, etc. Would the proposed duty apply to all owners, including homeowners under home improvement contracts? Then there is an additional education issue, and notices explaining duties would have to be revised to achieve the idealistic goal of making the murky clear.

The staff is not convinced that the current reliance on the county recorder should be retained, much less expanded. At some point, it is not possible to fix a complicated scheme like the mechanic’s lien statute with more notices, filings, and recordings. When that realization takes hold, it becomes clear that the statutory scheme needs to be rethought from the ground up, with a different mechanism to make it work.

James Stiepan finds a number of problems with Mr. Hunt’s proposal. (See First Supplement to Memorandum 99-85, Exhibit p. 2.):

(i) The analysis and suggested language presume that an unrecorded bond may limit lien rights, despite the fact that Section 3235 et seq ... refers only to recorded bonds. Under the circumstances, the reference to unrecorded bonds is confusing at best.

(ii) The requirement that a copy of the bond must be provided within ten days after the Preliminary Notice is needlessly restrictive. It should not matter when the information is provided as long as the claimant is not prejudiced.

(iii) The reference to the “owner and contractor” should instead be to the “owner or contractor.”

(iv) The entire thrust of the provision that a copy of the bond “must” be furnished is inappropriate. Rather, the subdivision, if needed at all, should merely recite that if a copy of the bond is not provided in time to avoid prejudicing lien rights, then the claimant shall retain those lien rights.

Time to Sue on Stop Notice Release Bond [Hunt Report pp. 18]

14. Time To Sue on Stop Notice Release Bond Does Not Start To Run Until a Copy of the Release Bond Is Served on Claimant

The Mechanic’s Lien Release Bond Section (Section 3144.5) provides that the time to sue on the Mechanic’s Lien release bond does not start to run until a copy of the bond is served upon the claimant. There is no similar provision with regard to Stop Notices.
In one case, a court ruled that the statute of limitations on a Stop Notice release bond was three years and the claimant did not even know of its existence until after the three years from execution of the bond had expired. The claimant lost. [See Winick Corp. v. General Ins. Co., 187 Cal. App. 3d 142 (1986).]

The Stop Notice law should be consistent with the lien law....

The staff recommends this revision be made. The mechanic’s lien statute should be revised to make the rules governing lien, stop notice, and bond remedies consistent unless there is a clear and convincing reason for retaining the exceptions.

Notice of Preliminary Notice Mistakes [Hunt Report p. 19]

15. Requirement for Recipient of Preliminary Notice To Notify Claimant of Inaccuracies

Mistakes in Preliminary Notices are often made. A recipient of the Preliminary Notice is not required to notify the claimant of the error. In fact, the recipient will probably use the inaccuracy as a defense in the lien foreclosure action. The purpose of the Preliminary Notice is to provide accurate notice to the owner, contractor, and lender. If the claimant has made an error, it should be cleared up so that accurate notice is given to the correct owner, contractor, and lender.

This proposal seeks to overcome the above and require the recipient of the Preliminary Notice to notify the claimant of any inaccuracies. This proposal is patterned after Arizona law. [See Ariz. Rev. Stat. § 33-991.01(i).] This could be accomplished by adding the following language to Section 3097:

A. Within ten (10) days after receipt of a Preliminary Notice given pursuant to this section, the recipient shall notify the claimant of any inaccuracies in said Preliminary Notice. The failure of the recipient of the Notice to give the claimant notice of the inaccuracies does not excuse the claimant from giving a Preliminary Notice, but it does stop the recipient of the notice from raising as a defense any inaccuracy of such information in the Preliminary Notice, provided the claimant’s Preliminary Notice otherwise complies with the provisions of this section. If the claimant receives a notice of such inaccuracies, the claimant shall, within thirty (30) days of the receipt of any notice of inaccuracies, give an Amended Preliminary Notice in the manner provided by this section. Such Amended Preliminary Notice shall be considered as having been given at the same time as the original Preliminary Notice.

The foregoing language is patterned after the Arizona statute.

James Stiepan finds this proposal “troubling” and urges that it be “quickly jettisoned.” (See First Supplement to Memorandum 99-85, Exhibit p. 2.) He writes:
First, as a practical matter, my experience is that minor non-substantive errors that would not prejudice the recipient are not deemed by the courts to vitiate lien rights. Second, the proposed language imposes a sweeping burden on the recipient of the Preliminary Notice to perform a clinical analysis of that Notice within ten days, regardless of whether any inaccuracy should have been known to the claimant or could have been discovered with reasonable care.

The staff is not convinced that this proposal is desirable or fair. The law should not place additional burdens on the owner that do not provide commensurate benefits. Before the Commission would approve this type of proposal, there needs to be a convincing case made of the need for it and a justification for placing a burden on the debtor to assist enforcement efforts of creditors. If the Commission wishes to pursue this matter, the staff would research the background on the Arizona statute to find out what circumstances led to its enactment and to determine, if possible, how it works in practice.


16. Amendments Made to Civil Code Section 3097 in 1999 Should Be Repealed
   In 1999, Senate Bill 914 was enacted as Chapter 795.

   This is no longer an issue. The problem was addressed by urgency legislation in 2000. See 2000 Cal. Stat. ch. 13 (AB 576, Honda), operative April 17, 2000).

Other Completion Issues

James Stiepan has suggested that the mechanic’s lien statute should be revised to clarify the rules governing when a work of improvement is completed. (See First Supplement to Memorandum 99-85, Exhibit pp. 2-3.) He writes:

Because the lien periods are keyed to the date of completion of the project, as is the validity of a recorded Notice of Completion, it is essential that the date of completion be ascertainable with some confidence. Unfortunately, conflicting case law and ambiguous code provisions make that determination more of a crap shoot.

Without proposing specific language at this time, I believe that the Code should reflect the following principles:

   (i) The date of completion should be tied to the standard real estate concept of substantial completion, exclusive of minor punch
list items that do not materially adversely affect use or occupancy. This is consistent with the practice in most construction contracts to effect final payment [within] a specified time after such substantial completion. However, as a matter of fairness to the “mechanic” who is actually performing a portion of the remaining punch list work, the date of completion for that claimant would occur upon the later completion of the portion of the work for which that claimant is responsible.

(ii) The date of issuance of a certificate of occupancy, if applicable, may be used as a proxy for substantial completion. Perhaps this is what is intended by reference to “acceptance by any public entity” in Section 3086, although that is not sufficiently clear.

(iii) Rather than requiring that a Notice of Completion must be recorded within a narrow window of ten days, Civil Code Section 3093 should provide that the lien filing period would be extended on a day-for-day basis for any later (i.e., after ten days) recordation of the Notice.

Completion issues are also addressed in Senator Margett’s SB 938, which has passed the Senate by a 38-0 vote. SB 938 would require the owner, within 10 days after a notice of completion or cessation is filed, to give notice to subcontractors and suppliers who have given a preliminary notice. Failure to do so would negate the shortening of the lien-filing period normally resulting from such filings, meaning that the 90-day period would apply. The bill was pulled off calendar in the Assembly Judiciary Committee on June 19th, as noted in Memorandum 2001-53, pending receipt of the Commission’s recommendations for mechanic’s lien reform. (See particularly the Assembly Judiciary Committee Analysis of SB 938 attached to Memorandum 2001-53, at Exhibit pp. 2-6.)

The staff believes these issues must be studied, but staff resources have not yet been available to do the necessary analysis. At a minimum, the issues raised by SB 938 will need to be addressed so that the Commission can respond to the request from the Assembly Judiciary Committee. Since the Committee is holding off on mechanic’s lien bills that it considers within the scope of the Commission’s comprehensive review, the staff believes it will be necessary for the final stage of the mechanic’s lien project to include a review of any legislative proposals that have been stalled. The consequence of this unusual role for the Commission is that the substance of a bill may come to the Commission as a proposal for inclusion in the report to the Assembly Judiciary Committee and, perhaps, in
some form, as part of the Commission’s overall recommendation for revision of
the mechanic’s lien law.

Respectfully submitted,

Stan Ulrich
Assistant Executive Secretary