Study H-821 October 4, 2007

First Supplement to Memorandum 2007-45

Mechanics Lien Law: Public Work of Improvement
(Analysis of Comments on Tentative Recommendation)

This supplement concludes a discussion of comments on the public work part of the Commission's tentative recommendation on *Mechanics Lien Law* (June 2006). It discusses a proposed new payment bond remedy that would be applicable to a "hybrid" project (i.e., the private development of publicly owned land).

We have received a letter from the California State Council of Laborers Legislative Department and Construction Laborers Trust Funds for Southern California (collectively, the "Laborers Group") relating to this subject, which is attached as an Exhibit to this memorandum.

BACKGROUND

A public entity may partner with a private developer to improve property that is publicly owned, at least in part (hereafter, a "hybrid" project). Because a hybrid project is contracted for by a private developer rather than a public entity, it is governed by the private work provisions of the existing mechanics lien statute. See Civ. Code §§ 3100, 3247; *North Bay Construction, Inc. v. City of Petaluma*, 143 Cal. App. 4th 552, 49 Cal. Rptr. 3d 455 (2006), *Progress Glass Co. v. American Ins. Co.*, 100 Cal. App. 3d 720, 161 Cal. Rptr. 243 (1980).

At the August meeting, the Commission revised the proposed law to make clear that the proposed law continues that rule. CLRC Memorandum 2007-34, pp. 2-4; CLRC Minutes (August 2007), p. 3.

On a private work of improvement, providing a payment bond as security for contributors on the job is optional. Civ. Code § 3236, proposed Civ. Code § 7600.

By contrast, on most public work projects a payment bond is mandatory. Civ. Code § 3247, proposed Pub. Cont. Code § 45010. The rationale for the distinction is generally understood to be the unavailability of a mechanics lien claim on

publicly owned property, based on sovereign immunity principles. *North Bay Construction, Inc. v. City of Petaluma*, 143 Cal. App. 4th 552, 49 Cal. Rptr. 3d 455 (2006).) The mandatory payment bond serves as a substitute source of recovery for contributors on these projects.

Because a hybrid project is governed by the private work provisions, a payment bond on such a project is optional. Several commenters, including the Laborers Group, argue that the bond should be mandatory on such a project. Exhibit pp. 3-4; CLRC Memorandum 2007-34, pp. 2-6.

The commenters point out that, since a hybrid project improves publicly owned property, contributors to the project are barred from asserting a mechanics lien claim, just like contributors to a public work. Therefore, without the substitute mandatory payment bond remedy, a contributor to a hybrid project is left with inadequate security in the event of non-payment.

At the August meeting, the Commission directed the staff to draft a mandatory payment bond remedy for hybrid projects.

Issues involved in drafting the new remedy are discussed below.

SCOPE OF APPLICATION

In drafting the new payment bond remedy, the first step is to identify the scope of the remedy's application, i.e., which works of improvement would be subject to the new mandatory bond requirement.

Work of Improvement That Cannot be Liened

As a matter of policy, a payment bond should be required whenever a mechanics lien claim is not available. Unfortunately, under existing law it is not entirely clear when that situation exists.

Generally speaking, in the state of California a lien claim may not be recorded on property owned by a public entity. *Sunlight Elec. Supply Co. v. McKee*, 226 Cal. App. 2d 47, 37 Cal. Rptr. 782 (1964). However, this is a common law rule, and its boundaries have not been fully explored. *North Bay Construction, Inc. v. City of Petaluma*, 143 Cal. App. 4th 552, 49 Cal. Rptr. 3d 455 (2006). For example, although California has not done so, some other jurisdictions have recognized exceptions to this general principle, based on the *nature* of the public interest ownership (i.e., proprietary vs. governmental). See cases cited in *North Bay Construction, Inc.*, *supra*.

Moreover, in a hybrid project, both a public entity *and* a private entity have an ownership interest in the same property. Whether a lien may be recorded on the private entity's interest in the property, without disturbing the public entity's interest, remains an unresolved issue. There is nothing in the existing mechanics lien statute or case law that clearly answers the question.

Thus, a requirement that a payment bond must be provided for "projects on which a mechanics lien claim is unavailable" would be too uncertain to be workable.

Work of Improvement in Which a Public Entity Has Any Ownership

A clearer approach would be to require a payment bond on any work of improvement in which a public entity has any ownership interest at all. That standard would undoubtedly encompass all projects in which a lien might not be available.

However, that standard might be over-inclusive. It would mandate a payment bond on a project on which a court might ultimately determine that a lien claim *is* available.

Moreover, the concept of "public ownership interest" might be ambiguous in some cases. For example, Laborers Group points to what are known as "Build-Buy" projects, in which a private developer contracts to sell private property to a public entity after it is developed, thereby creating only a *future* (and possibly contingent) public ownership interest in the property. Exhibit p. 3. Would that be a "public ownership interest" in the work of improvement? Would a property tax lien be a public ownership interest? An easement?

Such a broadly defined standard of application could be a trap for the unwary. For example, a homeowner contracting for a small home improvement project on property with a public drainage easement in the backyard could be subject to the proposed mandatory payment bond requirement.

Compromise Approach

A third approach, which the staff recommends, would be to state expressly which type of public ownership interest would trigger application of the proposed bond remedy.

Because the proposed new remedy would constitute a significant substantive revision to existing law, the staff suggests a conservative approach. The bond should only be mandatory if the public ownership interest is obvious and is

likely to preclude the recording of a lien claim on the property. It is important that the rule be clear. Even if the statute does not cover *all* circumstances in which a lien might be precluded, it would still provide more protection for contributors than exists under current law.

With these principles in mind, the staff recommends that a bond be required if a public entity has: a fee simple ownership interest, presently held, either solely or jointly. Each of those criteria is discussed below.

Fee Simple Ownership Interest

Fee simple ownership of property is the largest interest that can exist in land, and is of potentially infinite duration. Miller & Starr, California Real Estate § 9.3 (3d ed. 2007).

A lien on property in which a public entity holds fee simple title would undoubtedly impair the public entity's ownership interest. If the lien were foreclosed and the property sold, the public entity's interest would be transferred to the buyer.

For that reason, the staff draft would require a payment bond when a public entity has a fee simple interest in property.

A reference to fee simple ownership also serves another purpose. It precludes lesser interests in property, such as a leasehold or easement. See *City of Manhattan Beach v. Superior Court*, 13 Cal. 4th 232, 914 P.2d 160, 52 Cal. Rptr. 2d 82 (1996); Miller & Starr, California Real Estate § 9.1 (3d ed. 2007).

It seems likely that a leasehold or easement held by a public entity would not preclude recording a mechanics lien against a private owner of the underlying estate. If the underlying estate were sold in foreclosure, the public entity's leasehold or easement would not be disturbed. The new owner would take subject to those interests. See Miller & Starr, California Real Estate § 11.94 (3d ed. 2007) (easement or tax lien recorded prior to mechanics lien is senior to mechanics lien, and survives foreclosure based on mechanics lien); Miller & Starr, California Real Estate § 11.95 (3d ed. 2007) (same rule for prior recorded lease).

If public ownership of a lesser interest would not preclude a lien claim on the underlying estate, then there would be no need for a payment bond as an alternative source of recovery for claimants.

By limiting the bond to cases where a public entity holds a fee simple interest in the property, the draft would not require a bond when only a lesser public

ownership interest was present. A Comment in the staff draft would state that result expressly.

Present v. Future Interest

However, in order for a fee simple public ownership interest in property to preclude a lien claim, it should probably be a *present* fee simple interest.

If a public entity holds only a *future* fee simple interest in property (e.g., a remainder following a life estate in the current private owner), a sale of the private owner's present interest should not disturb the public entity's future interest. Creditors of the private owner could only reach the private owner's interest and would take subject to the public entity's future interest.

Thus, it would appear that a purely future fee simple public ownership interest would not be disturbed if the private owner's present interest were liened. For that reason, the staff draft would require the payment bond only when the public entity has a *present* fee simple interest in the property.

Sole v. Joint Ownership

Fee simple ownership can be shared by two or more persons. Each co-owner has a full and undivided interest in the entire property. See *Tenhet v. Boswell*, 18 Cal. 3d 150, 554 P.2d 330, 133 Cal. Rptr. 10 (1976).

The staff draft does not differentiate between sole and joint ownership. If a public entity has a present undivided fee simple ownership interest, that interest would be defeated by foreclosure of a lien, regardless of whether the public entity was the sole owner or a joint owner.

Draft Language

Consistent with the discussion above, the staff recommends that **the triggering language for application of the new remedy read as follows:**

> An owner that contracts for a work of improvement shall obtain a payment bond before commencement of work if … a public entity has a present fee simple interest in the property to be improved.

OPERATIONAL PROVISIONS

In order to implement the new mandatory payment bond remedy, the proposed law should include provisions detailing how the remedy would work (e.g. amount of the bond, procedures for making a claim against bond, etc.).

Provisions addressing most of these issues already exist in the proposed law. In fact, there are two sets of rules, one governing the optional private work payment bond, and the other governing the mandatory public work payment bond. It would be best to incorporate existing rules to the extent possible, to provide continuity. However, the Commission needs to decide (1) which of the two sets of provisions (or some combination thereof) should be applicable to the hybrid project remedy, and (2) how to draft the proposed law to implement that choice.

Application of Public Work Payment Bond Provisions

A simple way to make all public work payment bond operational provisions applicable to the new remedy would be to follow the approach used in Senate Bill 935 (Perata), a 2007 bill (not enacted) promoted by the Laborers Group.

SB 935 would have mandated a payment bond on works of improvement contracted for by a public utility. The bill would have simply "deemed" a public utility to be a public entity for purposes of the public work payment bond provisions, providing that the required bond "shall be enforced in the same manner as the payment bond for public works specified in [the mandatory public work payment bond provisions]."

The proposed law could similarly "deem" a developer of a hybrid project to be a public entity for purposes of the public work payment bond provisions, and provide that all such provisions apply to that work of improvement.

However, that approach would not be as simple as it looks, as discussed below.

Conflicting Payment Bond Provisions

If the public work payment bond rules are incorporated, the law would need to expressly state that the private work payment bond rules do not apply. Otherwise, the private work provisions might, by their terms, apply to a bond that is also covered by the public work provisions.

Public Work Provisions Not Tailored to Private Developer

The public work payment bond procedures were drafted with a public entity in mind. Some provisions would not work well if applied to a private developer, and could cause unexpected problems in practice.

For example, one of the key provisions of the public work payment bond remedy is the requirement that the public entity give notice of mandatory payment bond in its call for bids. Would this mean that the private developer, who otherwise may not be obligated to call for bids, would be required to do so? If not, would some other type of notice of the bond requirement be required?

The Commission could attempt to find and address those sorts of inconsistencies, but then the efficiency of wholesale incorporation by reference would be lost.

References to Non-Payment Bond Provisions

The public work payment bond provisions do not exist in isolation. They are part of the entire public work scheme. They rely on definitions and other general provisions that would not be incorporated by a narrow reference to the payment bond provisions. That could lead to confusion.

For example, notice of a claim against a public work payment bond is sometimes required to be given within a certain number of days after "completion." Proposed Public Contract Code Section 45060(b). However, "completion" of a public work is defined differently than "completion" of a private work. If a claim is made against a payment bond on a hybrid project, which definition of "completion" would apply?

Application to Payment Bond Claimants

If the public work payment bond provisions are made applicable to a hybrid project *developer*, would those same provisions govern *claimants* on a hybrid project? For example, which source of law would govern notices given by claimants, or the time for enforcement of a claim?

This issue would need to be carefully addressed in order to avoid significant confusion.

Conclusion

The primary advantage of incorporating the public work payment bond provisions is its apparent simplicity. However, as discussed above, those provisions could not be incorporated without addressing a number of ancillary details. That would significantly undercut the simplicity of that drafting approach. **The staff recommends against it.**

General Application of Private Work Payment Bond Provisions

A better approach would be to incorporate most of the private work payment bond provisions. That could be done by placing the new remedy in the same chapter as the other private work payment bond provisions. Those provisions would then apply to the mandatory bond as well (as would all related general rules and definitions in the private work provisions).

There would be no overlap between the private work and public work payment bond provisions, because a hybrid project would not be governed by the public work provisions at all.

Nor would there be any ill-fitting procedures that would need to be adjusted. The private work provisions were drafted with private owners in mind. It should be no problem to apply them to a private developer.

Such an approach is not only simple, it should come as no surprise to claimants who expect a project classified as a "private work" to be governed by the private work payment bond provisions.

Under this approach, the following operational rules would automatically govern the new remedy — proposed Civil Code Sections 7606 (specifying how bond is to be conditioned), 7608 (limiting bond claims to those providing work under the contract), 7610 (statute of limitations for a bond claim), and 7612 (notice required for a bond claim).

However, there are a few issues that should probably be governed by the slightly different approach provided in the public work provisions. These issues are discussed below.

Consequence for Failure to Obtain Bond

Since this new remedy requires a mandatory bond, should the remedy include an enforcement scheme with specified consequences if the bond is not obtained? If so, the Commission might look to the enforcement scheme relating to a mandatory public work payment bond as a model.

(This issue of enforcement is not addressed at all in the private work payment bond provisions, since the existing private work payment bond is optional.)

Public Work Enforcement Scheme

On a public work, the public entity and the direct contractor are each assigned significant responsibilities for ensuring that a mandatory payment bond is provided, and each is subject to significant adverse consequences if it is not.

The public entity's initial responsibility is to provide notice to the direct contractor of the payment bond requirement, in the entity's call for bids. Existing Civ. Code § 3247(a), proposed Pub. Cont. Code § 45010(a). Thereafter, the direct contractor is responsible for obtaining the payment bond, and the public entity is charged with ensuring that the payment bond meets statutory requirements. Existing Civ. Code § 3247(a), proposed Pub. Cont. Code § 45010(b).

If the public entity fails to comply with its statutory duties relating to the payment bond, it may be held liable in tort to all claimants on the project that are ultimately unpaid. *N.V. Heathorn, Inc. v. County of San Mateo*, 126 Cal. App. 4th 1526, 25 Cal. Rptr. 3d 400 (2005), *Walt Rankin & Associates, Inc. v. City of Murrieta*, 84 Cal. App. 4th 605, 101 Cal. Rptr. 2d 48 (2000).

If the direct contractor fails to comply with its statutory duties, it may forfeit the right to be paid under the public works contract. Existing Civ. Code § 3251, proposed Pub. Cont. Code § 45020(a).

Difficulties in Paralleling Public Work Enforcement Scheme

The public work enforcement scheme cannot be paralleled exactly.

First, as previously discussed, the public work enforcement scheme relies on the "call for bids" to provide notice that a payment bond is required. This notice is a crucial aspect of the overall enforcement scheme, as it justifies the imposition of a significant consequence on the direct contractor if it thereafter fails to provide the bond.

However, a private developer generally has no statutory obligation to call for bids on a project. So, if the new payment bond remedy were to incorporate the public work enforcement scheme, a different form of notice would need to be specified.

More significantly, on a public work, the consequence to a public entity for failing to comply with its payment bond obligations is not codified. It based on case law. See *N.V. Heathorn, Inc. v. County of San Mateo*, 126 Cal. App. 4th 1526, 25 Cal. Rptr. 3d 400 (2005), *Walt Rankin & Associates, Inc. v. City of Murrieta*, 84 Cal. App. 4th 605, 101 Cal. Rptr. 2d 48 (2000).

The fact that the consequence is matter of case law, rather than statutory law, would make it difficult to parallel in the hybrid project context. The proposed law could flatly impose tort liability for a breach of the mandatory payment bond remedy, but that might be a stricter rule than the rule for a breach by a public

entity (because the case law could be overruled or develop into a more nuanced approach).

Simplified Approach

In light of the difficulty involved in attempting to parallel the public work payment bond enforcement scheme, the staff draft takes a simpler approach.

Responsibility to obtain the bond would rest solely on the private developer. The direct contractor would have no statutory duty.

That is a considerable simplification that avoids the back and forth between the owner (who gives notice) and the direct contractor (who obtains the bond) and the owner once again (who must approve the bond before work commences). If the owner must give the notice and approve the bond (and probably bears the cost of the bond as part of the contract price), then it would make sense to cut out the middle man. The developer could still require that the direct contractor take care of the bonding transaction, as a requirement of the contract, but the statute would not mandate that arrangement.

As with the existing public work provisions, the staff draft does not specify a statutory penalty for an owner who fails to obtain the mandatory bond. Instead, the possibility of tort liability for a breach of the duty would exist (and would be mentioned in the Comment). The contours of any liability would be left to court development.

If the Commission would rather specify a penalty for breaching the duty, that could be done. Two possibilities would be to (1) expressly provide for tort liability, or (2) expressly provide that the developer must directly pay any claim that goes unpaid as a result of the absence of the bond. A simple reference to tort liability might allow for the possibility of consequential damages beyond the unpaid claims, which might be excessive (and controversial). Limiting the recovery to unpaid claims alone would probably be less controversial, but might provide claimants with significantly less protection than they enjoy under the public work provisions.

Amount of Payment Bond

On a public work, a mandatory payment bond must be for 100% of the contract price. Existing Civ. Code § 3248(a), proposed Pub. Cont. Code § 45030(a). On a private work, the optional payment bond need be for only 50%

of the amount of the contract. Existing Civ. Code § 3235, proposed Civ. Code § 7602(a).

The staff draft would require that the bond be for 100% of the contract price. That approach seems more consistent with the policy underlying a mandatory payment bond remedy, namely the protection of all contributors on a project that have no lien right.

Minimum Contract Price

On a public work, a payment bond is not required if the contract price is equal to or less than $25,000. Existing Civ. Code § 3247(a), proposed Pub. Cont. Code § 45010(a). (A minimum contract price is not addressed by the private work payment bond provisions.)

The $25,000 figure likely represents recognition that if a project is small enough, the financial and administrative cost of a payment bond is disproportionate to the bond's benefit, and it should not be required.

The staff sees no reason why that wouldn't also be true on a hybrid project. The staff draft includes the $25,000 limit**.**

DRAFT OF PROPOSED HYBRID PROJECT PAYMENT BOND PROVISION

Incorporating each of the decisions discussed above, the proposed new payment bond remedy would be implemented as follows:

> **§ 7603. Mandatory payment bond requirement**
>
> 7603. (a) An owner that contracts for a work of improvement shall obtain a payment bond before commencement of work if both of the following conditions are true:
>
> (1) The contract is for more than twenty-five thousand dollars ($25,000).
>
> (2) A public entity has a present fee simple interest in the property to be improved.
>
> (b) A payment bond given pursuant to this section shall be in an amount of at least one hundred percent of the contract price for the work of improvement.
>
> **Comment**. Section 7603 is new.
>
> The requirements of this section are similar in substance to the requirements of Public Contract Code Section 45010 et seq. The failure of a public entity to comply with those requirements could expose the public entity to tort liability. See *N.V. Heathorn, Inc. v. County of San Mateo*, 126 Cal. App. 4th 1526, 25 Cal. Rptr. 3d 400 (2005), *Walt Rankin & Associates, Inc. v. City of Murrieta*, 84 Cal. App. 4th 605, 101 Cal. Rptr. 2d 48 (2000).

Fee simple does not include a leasehold, easement, or lien. See *City of Manhattan Beach v. Superior Court*, 13 Cal. 4th 232, 914 P.2d 160, 52 Cal. Rptr. 2d 82 (1996).

See also Sections 7003 ("commencement" defined), 7006 ("contract" defined), 7008 ("contract price" defined), 7028 ("owner" defined), 7030 ("payment bond" defined), 7045 ("work" defined).

If the Commission elects to add the remedy to the proposed law, **a conforming revision should be made to proposed Civil Code Section 7608** (in order to accommodate a payment bond that is obtained directly by a developer, rather than by a direct contractor):

§ 7608. Limitation on part

7608. (a) This part does not give a claimant a right to recover on a ~~direct contractor's~~ payment bond given under this chapter providing coverage for claims against a direct contractor, unless the claimant provided work to the direct contractor either directly or through one or more subcontractors, pursuant to a contract between the direct contractor and the owner.

(b) Nothing in this section affects the stop payment notice right of, and relative priorities among, design professionals and holders of secured interests in the property.

SHOULD THE PROPOSED REMEDY BE ADDED TO THE PROPOSED LAW?

Now that the Commission knows what this new proposed payment bond remedy might look like, the Commission needs to decide whether the remedy should be added to the proposed law.

Likely Support and Opposition

All members of the public at the August meeting seemed to support a mandatory bond on a hybrid project.

The new remedy would certainly be welcomed by contributors on a hybrid project, as well as by the sureties that would be providing the new mandatory bond.

However, the staff has identified one group, which was not represented at the August meeting, that may object to the new remedy — the private developers of hybrid projects.

These developers are the entities that would have to bear the cost of the new bond. More importantly, it is possible that a breach of the bonding requirement

could result in tort liability (if a court decides to follow the public work payment bond cases). That new risk of liability is likely to be cause for concern.

Recommendation

The general policy served by a mandatory bond for hybrid projects is sound. It would offer financial protection to contributors to a hybrid project, who have no access to a lien remedy. The Legislature has already determined that mandatory bonding is appropriate for public works, where there is also no right to lien the property. The proposed remedy would simply expand on that existing policy.

However, it seems likely that developers would resist any provision that adds new costs and expands tort liability exposure.

There may also be unintended consequences of the new remedy, that aren't immediately apparent to the staff. Developers or other practitioners may be able to point out practical problems that the new remedy would cause. Or such problems might arise only after the new law goes into effect.

Ordinarily, the Commission would not recommend a change as substantive and potentially polarizing as the hybrid bond remedy would seem to be, without first circulating a draft for public comment. **The staff recommends that we follow our usual deliberative process in this case, and circulate the draft for public comment, including the major property development organizations.**

The proposed law should not be held up for that purpose. There is still a possibility that work can be completed on the proposed law at the December meeting, in which case implementing legislation could be introduced in 2008. That would be impossible if the proposed law were held while waiting for comment on the hybrid bond proposal. **Instead, the staff recommends that the hybrid bond proposal be circulated as a separate tentative recommendation.** The staff would present a draft of the tentative recommendation for approval at a future meeting.

Respectfully submitted,

Steve Cohen
Staff Counsel

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August 23, 2007

Via E-Mail Only

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Comments from California State Council of Laborers Legislative Dept. and Construction Laborers Trust Funds for Southern California on Public Works - Memorandum 2007- 34

Dear Members of the Commission:

On behalf of the California State Council of Laborers Legislative Department (Laborers), and the Construction Laborers Trust Funds for Southern California (Laborers Funds), we present the following comments to Memorandum 2007-34, regarding the Public Works component of the Mechanic Lien Law Revision.

Because of the late date, we send these by e-mail only, with PDF files attached.

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

Thank you for your consideration.

Sincerely,

J. David Sackman, of
Reich, Adell & Cvitan

following: Comments (attached as a separate files with e-mail).
SB 935

cc: Mike Quevedo, Southern California District Council of Laborers
Jose Mejia, Cal. State Council of Laborers
Ric Quevedo, Construction Laborers Trust Funds for Southern California
Mark J. Rice, Cox Castle & Nicholson (Markjrice@aol.com)
John Miller, Cox Castle & Nicholson
Alexander Cvitan, Reich, Adell & Cvitan

1. Payment Bonds for Hybrid Projects

The Associated General Contractors (AGC) has pointed out a hole in the law, for "hybrid" projects which cannot be subject to a mechanic lien, but are not considered public works subject to stop notice and bond requirements. **They suggest that a payment bond be required for these hybrid projects. We concur.**

Contrary to the Staff Comments, **this ambiguity IS present in existing law**. Clearing up an ambiguity in the proposed Public Contracts Code will NOT fully address the problem. This hole exists in existing law on construction projects which are not on private property subject to a mechanic lien, but are not considered "public works" subject to stop notice and bond requirements. It is not true that "a hybrid project thus necessarily falls into one or the other classification." Examples of "hybrid" projects in which there exists a hole in existing law include:

1) Construction work by contractors for public utilities, which are not publicly owned (e.g. SBC, Sempra). The real property worked on is nothing but an easement through private or public land. Because that easement is regulated by state and federal agencies, it cannot be bought and sold without their approval, and thus cannot be liened or foreclosed on. Because the entity contracting for the work is not a public entity, it is not considered a "public work."

2) Construction work on airport terminals. Airports are usually owned by municipalities, who lease the terminals to the private airlines. Because the airport itself is public land, it cannot be liened or foreclosed. Because the project is not contracted by a public entity, it is not considered a "public work." I have tried myself to place a mechanic lien on the leasehold of an airline, only to have it rejected by the County Recorder.

3) Other construction work contracted by private entities on public land. These are not subject to either mechanic liens or stop notice or bond remedies, for the same reasons as airport terminals.

4) "Build-Buy" projects where a private entity contracts for the work and then sells the land and the structures to a public entity, upon completion. While a mechanic lien can be placed on the private property before it is transferred, the transfer may occur before the limitation period to file liens, thus cutting off the ability of some claimants to file a lien.

5) Other miscellaneous projects on public land, which are not contracted by a public agency.

We have a bill pending to plug up one of these holes: Section 2 of SB 935 (attached) will require a payment bond on work contracted by public utilities regulated by the Public Utilities Commission. The statement in Section 3 of this bill applies equally to all the holes in the law:

> "The Legislature finds that the amendments made to existing law by this bill are intended to implement the provisions of Sections 1 and 3 of Article XIV of the California Constitution, ..."

While adding a payment bond requirement to such projects would be a substantive change in existing law, we believe this change is mandated by the Constitution. Article XIV § 3 provides that "**Legislature shall provide, by law, for the speedy and efficient enforcement of such liens**." By leaving these holes in existing law, the Legislature has failed in its Constitutional mandate. It is therefore the mandate of this Commission, to make proposals to the Legislature on how it can fulfill its own Constitutional mandate.

We ask that this issue be given further study, and that a separate Staff Report be issued with proposals for review by the public and this Commission.

2. Delivery of Notice to Public Entity

We concur that the designation of an alternate address should be optional, rather than compulsory. What is important is that any designated address be made easily available to the public. So we suggest that the use of a specific address only be allowed if the agency makes sure that the designation of the address is easily available to the public. Putting the address in the contract is not sufficient, since it may take a claimant a good deal of time and expense to obtain a copy of the contract and find the designation.

3. Proof of Notice by Mail

The Commission Staff propose amending § 42114 to allow proof of notice to be made by "documentation provided by the United States Post Office showing that payment was made to mail the notice . . . " and similar documentation "by an express service carrier" showing payment was made for delivery.

We query whether the stamp from a Postal machine, used in most large offices to send mail, would satisfy this requirement, or do claimants need to physically take their notices to a Post Office to be mailed in order to obtain a proper receipt? Similarly, will a printout of the online receipt and tracking information provided by most express service carriers suffice, or will claimants again be required to physically go to the office of the carrier to obtain a proper receipt?

4. Notice of Completion for Portion of Project

The proposed new § 42225 would allow a public entity to issue a Notice of Completion as to a portion of a project. Some public agencies already do this, although the practice is of dubious legality. Sometimes agencies also "bundle" several contracts together into a single project. They may then either issue a single Notice of Completion at the end of all the work, or "unbundle" the contracts to issue separate Notices of Completion.

The problem with this practice is that it can be quite confusing to claimants. How does a laborer or material supplier know which particular contract on a large project their work relates to? How will they know if a Notice of Completion as to one component of a project relates to their work or material?

If such a provision is to be added, it should be accompanied by strict notice requirements on the agency, to make sure they notify all possible claimants as to which particular contract(s) their work relates to, and which Notice of Completion may apply to them.

We thank you for your consideration.

SENATE BILL No. 935

Introduced by Senator Perata

February 23, 2007

An act to amend Section 1720 of, and to add Section 1720.1 to, the Labor Code, relating to public works.

LEGISLATIVE COUNSEL'S DIGEST

SB 935, as introduced, Perata. Public works: utility workers: wage protection.

Existing law generally requires the payment of the general prevailing rate of per diem wages to workers employed on public works projects costing over $1,000, unless the awarding body, as defined, elects to initiate and enforce a labor compliance program, as defined, for every public works project under the authority of that awarding body. Existing law generally defines "public works" to include construction, alteration, demolition, installation, or repair work done under contract and paid for, in whole or in part, out of public funds, but exempts from that definition, among other projects, work done directly by any public utility company pursuant to order of the Public Utilities Commission or other public authority.

This bill would delete that exemption and would, thus, define "public works" to include any construction, alteration, demolition, installation, or repair work done under contract and paid for, in whole or in part, by a public utility, as defined. This bill would also specify that a public utility, defined as a "public entity" for those limited purposes, must require the payment bond of its contractors, as provided, and must submit, upon request, copies of those payment bonds to the Public Utilities Commission or any worker or member of the public. This bill would also declare the intent of the Legislature to extend the protections offered to workers employed on public works projects to workers

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employed on construction projects for public utilities, and would endorse and approve the reasoning of the specified Public Utilities Commission's decisions.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 1720 of the Labor Code is amended to read:

1720. (a) As used in this chapter, "public works" means:

(1) Construction, alteration, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds~~, except work done directly by any public utility company pursuant to order of the Public Utilities Commission or other public authority~~. For purposes of this paragraph, "construction" includes work performed during the design and preconstruction phases of construction including, but not limited to, inspection and land surveying work.

(2) Work done for irrigation, utility, reclamation, and improvement districts, and other districts of this type. "Public work" does not include the operation of the irrigation or drainage system of any irrigation or reclamation district, except as used in Section 1778 relating to retaining wages.

(3) Street, sewer, or other improvement work done under the direction and supervision or by the authority of any officer or public body of the state, or of any political subdivision or district thereof, whether the political subdivision or district operates under a freeholder's charter or not.

(4) The laying of carpet done under a building lease-maintenance contract and paid for out of public funds.

(5) The laying of carpet in a public building done under contract and paid for in whole or in part out of public funds.

(6) Public transportation demonstration projects authorized pursuant to Section 143 of the Streets and Highways Code.

(b) For purposes of this section, "paid for in whole or in part out of public funds" means all of the following:

(1) The payment of money or the equivalent of money by the state or political subdivision directly to or on behalf of the public works contractor, subcontractor, or developer.

(2) Performance of construction work by the state or political subdivision in execution of the project.

(3) Transfer by the state or political subdivision of an asset of value for less than fair market price.

(4) Fees, costs, rents, insurance or bond premiums, loans, interest rates, or other obligations that would normally be required in the execution of the contract, that are paid, reduced, charged at less than fair market value, waived, or forgiven by the state or political subdivision.

(5) Money loaned by the state or political subdivision that is to be repaid on a contingent basis.

(6) Credits that are applied by the state or political subdivision against repayment obligations to the state or political subdivision.

(c) Notwithstanding subdivision (b):

(1) Private residential projects built on private property are not subject to the requirements of this chapter unless the projects are built pursuant to an agreement with a state agency, redevelopment agency, or local public housing authority.

(2) If the state or a political subdivision requires a private developer to perform construction, alteration, demolition, installation, or repair work on a public work of improvement as a condition of regulatory approval of an otherwise private development project, and the state or political subdivision contributes no more money, or the equivalent of money, to the overall project than is required to perform this public improvement work, and the state or political subdivision maintains no proprietary interest in the overall project, then only the public improvement work shall thereby become subject to this chapter.

(3) If the state or a political subdivision reimburses a private developer for costs that would normally be borne by the public, or provides directly or indirectly a public subsidy to a private development project that is de minimis in the context of the project, an otherwise private development project shall not thereby become subject to the requirements of this chapter.

(4) The construction or rehabilitation of affordable housing units for low- or moderate-income persons pursuant to paragraph (5) or (7) of subdivision (e) of Section 33334.2 of the Health and Safety Code that are paid for solely with moneys from a Low and Moderate Income Housing Fund established pursuant to Section 33334.3 of the Health and Safety Code or that are paid for by a

combination of private funds and funds available pursuant to Section 33334.2 or 33334.3 of the Health and Safety Code do not constitute a project that is paid for in whole or in part out of public funds.

(5) "Paid for in whole or in part out of public funds" does not include tax credits provided pursuant to Section 17053.49 or 23649 of the Revenue and Taxation Code.

(6) Unless otherwise required by a public funding program, the construction or rehabilitation of privately owned residential projects is not subject to the requirements of this chapter if one or more of the following conditions are met:

(A) The project is a self-help housing project in which no fewer than 500 hours of construction work associated with the homes are to be performed by the homebuyers.

(B) The project consists of rehabilitation or expansion work associated with a facility operated on a not-for-profit basis as temporary or transitional housing for homeless persons with a total project cost of less than twenty-five thousand dollars ($25,000).

(C) Assistance is provided to a household as either mortgage assistance, downpayment assistance, or for the rehabilitation of a single-family home.

(D) The project consists of new construction, or expansion, or rehabilitation work associated with a facility developed by a nonprofit organization to be operated on a not-for-profit basis to provide emergency or transitional shelter and ancillary services and assistance to homeless adults and children. The nonprofit organization operating the project shall provide, at no profit, not less than 50 percent of the total project cost from nonpublic sources, excluding real property that is transferred or leased. Total project cost includes the value of donated labor, materials, architectural, and engineering services.

(E) The public participation in the project that would otherwise meet the criteria of subdivision (b) is public funding in the form of below-market interest rate loans for a project in which occupancy of at least 40 percent of the units is restricted for at least 20 years, by deed or regulatory agreement, to individuals or families earning no more than 80 percent of the area median income.

(d) Notwithstanding any provision of this section to the contrary, the following projects shall not, solely by reason of this section, be subject to the requirements of this chapter:

(1) Qualified residential rental projects, as defined by Section 142 (d) of the Internal Revenue Code, financed in whole or in part through the issuance of bonds that receive allocation of a portion of the state ceiling pursuant to Chapter 11.8 of Division 1 (commencing with Section 8869.80) of the Government Code on or before December 31, 2003.

(2) Single-family residential projects financed in whole or in part through the issuance of qualified mortgage revenue bonds or qualified veterans' mortgage bonds, as defined by Section 143 of the Internal Revenue Code, or with mortgage credit certificates under a Qualified Mortgage Credit Certificate Program, as defined by Section 25 of the Internal Revenue Code, that receive allocation of a portion of the state ceiling pursuant to Chapter 11.8 of Division 1 (commencing with Section 8869.80) of the Government Code on or before December 31, 2003.

(3) Low-income housing projects that are allocated federal or state low-income housing tax credits pursuant to Section 42 of the Internal Revenue Code, Chapter 3.6 of Division 31 (commencing with Section 50199.4) of the Health and Safety Code, or Section 12206, 17058, or 23610.5 of the Revenue and Taxation Code, on or before December 31, 2003.

(e) If a statute, other than this section, or a regulation, other than a regulation adopted pursuant to this section, or an ordinance or a contract applies this chapter to a project, the exclusions set forth in subdivision (d) do not apply to that project.

(f) For purposes of this section, references to the Internal Revenue Code mean the Internal Revenue Code of 1986, as amended, and include the corresponding predecessor sections of the Internal Revenue Code of 1954, as amended.

(g) The amendments made to this section by either Chapter 938 of the Statutes of 2001 or the act adding this subdivision shall not be construed to preempt local ordinances requiring the payment of prevailing wages on housing projects.

SEC. 2. Section 1720.1 is added to the Labor Code, to read:

1720.1. (a) For purposes of Article 2 (commencing with Section 1770) and Article 3 (commencing with Section 1810), both of the following definitions apply:

(1) "Public works" also includes any construction, alteration, demolition, installation, or repair work done under contract and paid for, in whole or in part, by a public utility.

(2) "Awarding body" also includes a public utility contracting the public work where the work is performed by a contractor or subcontractor of that public utility.

(b) (1) For purposes of Chapter 7 (commencing with Section 3247) of Title 15 of the Civil Code, a public utility is deemed to be a public entity and shall require its contractors to post a payment bond, as specified in Sections 3247 and 3248 of the Civil Code.

(2) A bond payment required by a public utility pursuant to this section and Chapter 7 (commencing with Section 3247) of Title 15 of the Civil Code shall be enforced in the same manner as the payment bond for public works specified in that chapter.

(3) A copy of the payment bond shall be made available to the Public Utilities Commission, upon its request, and shall also be made available by the public utility to any worker or member of the public, upon request and without charge. A public utility that fails to require a payment bond, or fails, upon request, to make a copy of the bond available to a worker or member of the public, shall be liable for the same obligations, and to the same extent, as its contractor or subcontractor, as guaranteed by the payment bond, without any limitations on the time period to make a claim or bring an action, except that an action to enforce this liability against a public utility must be brought within four years after completion of the project.

(c) For purposes of this section, "public utility" means any person or entity, as defined in Section 216 of the Public Utilities Code, and any electrical provider, as defined in Section 218.3 of the Public Utilities Code, that is subject to rate regulation by the Public Utilities Commission.

(d) This section does not modify, expand, or limit any existing requirements applicable to public works.

SEC. 3. (a) The Legislature finds that the amendments made to existing law by this bill are intended to implement the provisions of Sections 1 and 3 of Article XIV of the California Constitution, and to extend to workers employed on construction projects for public utilities the same protections that are offered to workers employed on public works projects.

(b) The Legislature also declares that it endorses and approves the reasoning of the Public Utilities Commission Decision 04-12-056, as corrected by its Decision 04-12-063.

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