

Second Supplement to Memorandum 2007-45

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

This supplement analyzes comment on matters discussed in CLRC Memorandum 2007-45 from the California State Council of Laborers Legislative Department and Construction Laborers Trust Funds for Southern California (collectively, "Laborers Group"). The comment from Laborers Group is attached as an Exhibit to this memorandum.

Issues in this memorandum that clearly require discussion have been marked with the following symbol: ☞.

All other issues in this memorandum are presumed to be noncontroversial "consent" issues. The staff does not intend to discuss any consent issue, unless a Commission member or member raises the issue at the meeting.

STOP PAYMENT NOTICE ISSUES

Exclusivity of Stop Payment Notice Remedy

The Laborers Group repeats its criticism of proposed Public Contract Code Section 44110, which provides that a claim against a public work construction fund may only be made pursuant to either a stop payment notice, or a direct written contract with the holder of the fund. Exhibit, p. 3; CLRC Memorandum 2007-45, pp. 12-14.

Conflict with Other Statutory Provisions

In CLRC Memorandum 2007-45, the staff acknowledged that read literally, Section 44110 (as well as Civil Code Section 3264, the section of existing law continued by Section 44110), could conflict with specific statutes outside the mechanics lien law that authorize recovery from funds designated for public construction, by means other than those described in Section 44110. See e.g.,

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

Code Civ. Proc. § 708.760 (satisfaction of judgment against direct contractor on public work), Labor Code § 1727 (public entity to withhold amounts needed to satisfy prevailing wage violations from funds due direct contractor on public work).

The Laborers Group again argues that Section 44110 should be deleted from the proposed law, in order to eliminate any conflict with these and other provisions.

For reasons stated in CLRC Memorandum 2007-45, the staff continues to recommend against deletion or revision of Section 44110. See CLRC Memorandum 2007-45, pp. 12-14.

Application to Public Work

Laborers Group also argues that Civil Code Section 3264, the provision of existing law continued by Section 44110, is ambiguous as to whether it even applies to public work. The group argues that by continuing Section 3264 in the Public Contract Code, the Commission is inappropriately resolving that ambiguity in favor of a finding that the provision does apply to public work.

However, the staff continues to believe there is no ambiguity to resolve. As noted in CLRC Memorandum 2007-45, Section 3264 expressly incorporates provisions that apply *only* to a public work. If Section 3264 was not intended to apply in part to a public work, this language would have no meaning at all.

Failure to Extend Private Work Mechanics Lien Provision to Public Work Stop Payment Notices

Finally, Laborers Group argues that the harm caused by continuing Section 3264 is exacerbated by the Commission's failure to make existing Civil Code Section 3152, a provision preserving a lien claimant's right to bring an independent personal action, applicable to public work stop payment notices.

However, as previously noted, Section 3152 appears in a chapter in the mechanics lien law that is expressly *inapplicable* to any public work. Civ. Code § 3109, CLRC Memorandum 2007-34, pp. 10-11. Laborers Group is thus advocating the creation of an entirely new public work provision, which would duplicate the provisions of Section 3152. The staff continues to believe that doing so would represent a significant and unwarranted change in existing law.

Recommendation

Proposed Public Contract Code Section 44110 accurately continues existing law. The change in existing law advocated by Laborers Group would effectively make a public work stop payment notice simply an optional procedure for a claimant asserting a claim against a public construction fund.

The staff continues to recommend that Section 44110 be retained as drafted. However, on the issue of theoretical statutory conflict, it occurs to the staff that perhaps an addition to the section Comment might help.

The staff therefore recommends that **the following language be added to the Comment to Section 44110:**

There may be specific statutory provisions that authorize payment by a public entity from a fund designated for a public work, notwithstanding the provisions of Section 44110. See, e.g., Code Civ. Proc. § 708.760 (satisfaction of judgment against direct contractor on public work), Labor Code § 1727 (public entity to withhold amounts needed to satisfy prevailing wage violations from funds due direct contractor on public work).

Notice to Claimant of Time to Enforce Stop Payment Notice

Public Contract Code Section 44170 requires a public entity, within 10 days of the occurrence of a specified event, to give notice to any person that has previously given the entity a stop payment notice (and paid the entity \$10.00) of the time period within which the claimant must enforce the stop payment notice in court.

As presently drafted, Section 44170 requires this notice to be given only upon completion of a public work. However, existing law provides that the notice must be given upon completion, *or* upon recordation of a notice of completion, whichever is later. Civ. Code § 3185.

In CLRC Memorandum 2007-45, the staff has recommended the restoration of existing law on that point. CLRC Memorandum 2007-45, p. 24. Failure to include recordation of a notice of completion as an alternative event triggering the notice under Section 44170 would be a substantial change in the law, as recordation dictates a much shorter period of time for enforcement of a stop payment notice — 30 days from recordation, as compared to 90 days from completion. Proposed Pub. Cont. Code § 44140.

Laborers Group does not object to restoring recordation of a notice of completion as an event triggering the notice requirement. However, the group

contends that the “whichever is later” language in the staff’s recommended revision of Section 44170 (and in existing law) creates a due process infirmity. Exhibit, p. 4.

The group argues that the recordation of a notice of completion can occur long after actual completion. This would mean that a claimant could receive a Section 44170 notice (based on recordation) for the first time more than 90 days after completion. That would be beyond the last date on which the stop payment notice claim could be enforced, rendering the Section 44170 notice worthless.

However, under proposed Public Contract Code Section 42220, a notice of completion *may not be recorded more than 15 days after completion*. Therefore, the latest a Section 44170 notice can be given based on recordation of a notice of completion is 25 days after completion. The recipient of that notice would then be obligated to file the enforcement action within the shorter 30 day period from the date of recordation, and the 90 day period from the date of completion would be irrelevant.

The staff continues to recommend that **Section 44170 be revised as recommended in CLRC Memorandum 2007-45.**



Stop Payment Notice Release Bond

Proposed Public Contract Code Section 44180 provides that if a contractor or subcontractor disputes a claimant’s stop payment notice, a public entity *may* accept a release bond from the direct contractor and release the withheld funds. However, the section provides that the entity retains discretion *not* to accept an offered bond. Section 44180 continues existing law.

Various commenters have argued for a change from existing law, suggesting that a public entity should not have discretion to refuse a release bond issued by an admitted surety insurer. CLRC Memorandum 2007-45, pp. 28-29. The staff views the issue as a close question, and its analysis concludes with no recommendation one way or another, pending discussion at the upcoming Commission meeting.

Laborers Group urges that the Commission decide the issue by continuing existing law. Exhibit, p. 4. The group argues that if a public entity retains discretion to reject an offered bond, and exercises that discretion arbitrarily, its decision might be challengeable in court. However, if a public entity is instead forced to accept a bond from a surety that, although an admitted surety insurer, nevertheless appears to be in financial distress, and the entity is thereafter

compelled to release a previously given stop payment notice, claimants may ultimately be left with neither a stop payment notice remedy *nor* a bond remedy.

The staff believes there is some merit in the argument of the Laborers Group. **The Commission should take that view into account in deciding how to proceed on this issue.**

PAYMENT BOND ISSUES

Construction of the Payment Bond

Proposed Public Contract Code Section 45040 sets forth various rules relating to how a public work payment bond is to be construed.

The American Insurance Association, National Association of Surety Bond Producers, and Surety & Fidelity Association of America (“joint surety commenters”) have argued, for various reasons, that this section should be deleted from the proposed law. CLRC Memorandum 2007-45, pp. 37-38; CLRC Memorandum 2006-39, Exhibit p. 95.

In CLRC Memorandum 2007-45, the staff has recommended against any revision of Section 45040 based on the comment of the joint surety commenters. Laborers Group agrees with the staff’s recommendation, asserting that any change in the section would be a “significant policy shift” that the group would oppose. Exhibit, pp. 4-5.



Statute of Limitation

Proposed Public Contract Code Section 45050 provides that the limitation period within which a claimant may seek to enforce a payment bond claim is “six months after the period in which a stop payment notice may be given under [proposed Public Contract Code] Section 44140.”

In CLRC Memorandum 2007-45, in response to a suggestion from the joint surety commenters, the staff recommends a revision of Section 45050 that would directly state the calculated time period for enforcing a payment bond claim, without reference to a time period prescribed in another section.

Laborers Group disagrees with this recommended revision, asserting that the revision would create a disconnect between Sections 44140 and 45050. It would leave open the possibility that at some point in the future the time limit in Section 44140 could change or be reinterpreted, without a matching change in Section 45050.

That is possible. On the other hand, there is value in stating a concrete time limit in Section 45050 that does not require reference to and interpretation of another statutory provision. It is also unclear that the time limit as stated in the recommended revision to Section 45050 would be problematic, even if the time limit for giving a stop payment notice in Section 44140 *were* to later change.

If any practitioner can articulate why it is important that the time limit for enforcing a payment bond claim be some fixed period after the time for giving a stop payment notice, Section 45050 should be retained as drafted.

Otherwise, the staff continues to recommend that **Section 45050 be revised as indicated in CLRC Memorandum 2007-45.**

Respectfully submitted,

Steve Cohen
Staff Counsel

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October 12, 2007

Via E-Mail and U.S. Mail

California Law Revision Commission
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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- 45

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 2007-45, regarding the Public Works component of the Mechanic Lien Law Revision. These comments are meant for your consideration with the items on your Agenda for October 26, 2007. We are separately submitting comments on the proposed "Hybrid Bond" requirement, Memorandum 2007-45 Supplement 1.

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

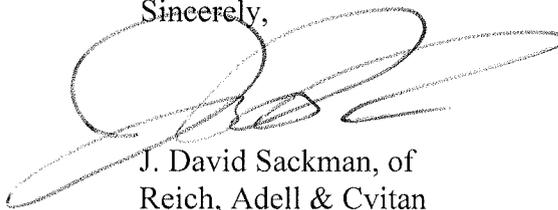
EX 1

Comments from California State Council of Laborers Legislative Department
and Construction Laborers Trust Funds for Southern California
on Public Works - Memorandum 2007- 45
October 12, 2007
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Thank you for your consideration.

Sincerely,

A handwritten signature in black ink, appearing to read "J. David Sackman", written over a large, stylized oval shape.

J. David Sackman, of
Reich, Adell & Cvitan

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

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. Exclusivity of Stop Payment Notice Remedy (Proposed Contract Code § 44110)

Staff acknowledges that Public Contracts Code § 44110 conflicts with other statutes, which expressly provide remedies against money held by public entities for construction projects. The Staff recommends perpetuating this conflict, by leaving the language intact.

This seems contrary to the mandate of the California Law Review Commission itself, to streamline the law and eliminate such conflicts. We cannot comprehend how perpetuating conflicts in the law is consistent with this mandate.

Adopting this Proposed § 44110 will also do more than perpetuate existing conflicts. This provision is currently in Civil Code § 3264, which applies to both private and public works. There is thus an ambiguity as to whether a "fund for payment of construction costs" refers to funds held by public entities. We would argue that it does not. However, if Proposed § 44110 is enacted, specifically in the Public Contract Code, that very enactment could be taken as meaning that this language is indeed intended to apply to public funds. By enacting this provision as proposed, the Commission would be giving ammunition to one side in arguing how that conflict should be resolved.

The enactment of Proposed § 44110 would be made worse by the failure to carry over another provision from existing law into the new Public Contract Code. As we pointed out in prior comments, the proposed Public Contracts Code additions failed to carry forward the provisions of current Civil Code § 3152, which provides that:

Nothing contained in this title affects the right of a claimant to maintain a personal action to recover a debt against the person liable therefor either in a separate action or in the action to foreclose the lien, nor any right the claimant may have to the issuance of a writ of attachment or execution or to enforce a judgment by other means. In an application for a writ of attachment, the claimant shall refer to this section. A lien held by the claimant under this chapter does not affect the right to procure a writ of attachment. The judgment, if any, obtained by the claimant in a personal action, or personal judgment obtained in a mechanic's lien action, does not impair or merge a lien held by the claimant under this chapter, but any money collected on the judgment shall be credited on the amount of the lien.

This current provision, which applies to both private and public works remedies "in this title," makes it clear that these remedies are not exclusive. This has been carried forward into the private works provision (Proposed Civil Code § 7474), but not the Public Contracts Code. The failure to carry this provision over to the new law is made worse by Proposed § 44110.

We urge that § 44110 be DELETED, and that the equivalent of Civil Code § 3152 we proposed be added instead.

2. Notice to Claimant of Time to Enforce Stop Payment Notice (Proposed Contract Code § 44170)

Proposed § 44170 carries forward a due-process infirmity of current law. Both require that the notice be given, only ten days after the *later* of a notice of completion or actual completion. Since actual completion can occur long before the filing of a notice of completion, it is conceivable that the notice will not be given until after the time to enforce a stop payment notice has already expired!

This is certainly a denial of the due process rights of claimants, especially those who provided labor or material early in the project, and have no way of knowing when it is completed, other than this notice. Notice should be given within ten days of whatever event triggers the running of the period to file suit. Thus, to avoid Constitutional due process arguments, the statute should read:

Not later than 10 days after the recordation of a notice of completion ~~or~~ and not later than 10 days after completion of a public works contract, whichever is later,

This means that the notice would have to be given twice, in the event a notice of completion is filed after actual completion. But this is only fair, since a notice of completion shortens the time to enforce a stop payment notice, and claimants deserve notice of this.

3. Discretion of Public Entity to Refuse Release Bond (Proposed Contract Code § 44180)

We disagree with the suggestion by Sureties that the discretion of a public entity to reject a release bond should be eliminated, i.e., that it must accept a bond by an admitted surety. As the Staff noted, accepting a bond from a surety in financial distress (but still "admitted") would create a risk that valid claims could go unpaid. Since the release bond is meant to *replace* the stop notice remedy, a public entity should retain discretion to reject a bond that may not actually be adequate. If a public entity is arbitrary or capricious in its rejection of a release bond, its decision can be challenged on that basis in court. However, if the public entity is forced to accept an inadequate surety, the result could be the loss of any remedy for the claimants.

4. Construction of Payment Bond (Proposed Contract Code § 44040)

The Laborers agree with the Staff recommendation NOT to eliminate proposed § 44040, which is based on current Civil Code § 3226. This section states the policy behind the payment bonds, that it is for the benefit of laborer and material supplier claimants. It is not surprising that the Sureties would like to eliminate this provision, which prevents them from asserting defenses which are extraneous to the merits of the claim itself. Any change would be a significant policy shift, which we would oppose.

5. Statute of Limitations (Proposed Contract Code § 44050)

Staff proposes adopting the suggestion that the statute of limitations be restated in this section, rather than referring back to the time provided in Proposed § 44140. We disagree. This would restate the statute of limitations in two sections, and open the possibility that they could be interpreted differently. The better drafting would be to refer back to the other section for the time to file a stop payment notice.

We thank you for your consideration.