Study H-821 July 8, 2005

First Supplement to Memorandum 2005-24

Mechanics Lien Law (Discussion of Issues)

Attached to this memorandum is a note from Sam Abdulaziz commenting on Memorandum 2005-24, relating to mechanics lien law.

UNENFORCEABLE CLAIM OF MECHANICS LIEN

Notice of Claim of Lien

Mr. Abdulaziz agrees with the proposal to require a lien claimant to notify the owner of the recordation of the claim of lien.

Judicial Relief

Mr. Abdulaziz agrees with the concept of awarding reasonable fees for the elimination of a stale claim of lien.

BFP Protection

Memorandum 2005-24 describes draft provisions the Commission has developed that would clear title by operation of law if an enforcement action has not been commenced or an extension of credit recorded within 90 days after recordation of a claim of lien.

Mr. Abdulaziz is concerned about automatically voiding the lien after 90 days. He gives as an example a situation where the owner has signed an extension of credit, but the attempted recordation is rejected by the county recorder on a formality. The lien claimant must send a new extension form to the owner to sign, which can take some time.

Mr. Abdulaziz proposes that, rather than voiding the claim of lien after 90 days, the claim of lien should be subordinate to the interest of a BFP who acquires the interest after the 90th day but before recordation of an extension of credit.

The staff does not know how the title insurers would react to this concept. We are still waiting to hear back from them on the concept of voiding the lien absolutely if nothing is recorded within the 90 day period.

Other Remedies

Memorandum 2005-24 discusses the ease with which a claim of mechanics lien may be recorded, the difficulty of removing a false claim of lien, and the desirability of deterring a false recording to begin with. The staff recommends in the memorandum that the law be revised to make clear that common law remedies for disparagement of title and fraud are available.

Sam Abdulaziz is concerned about this proposal. There is no evidence that the number of false claims is so great as to justify a change in existing law, and in any event a falsely filed claim may be expunged if not enforced within 90 days, regardless of its validity. His experience is that although a person may file a false claim in a minor amount, that person is not going to litigate it. The 90-day enforceability period is sufficiently short that the public is protected, and additional remedies directed to false claims are unnecessary — "I would not want to see a great deal of litigation as to the validity of the lien."

The staff thinks that is not an unreasonable position. However, we do know that false claims are filed, and they are not uncommon. Moreover, expungement remedies are time consuming and costly; the detriment to the property owner of a false claim of lien is more than simply waiting for 90 days.

Will the availability of a common law remedy cause more litigation than it cures? The proposed remedy is available only for intentional misconduct — negligence would not trigger liability — and the burden of proof is on the property owner. The staff is skeptical that a provision such as this will trigger frivolous litigation, to the detriment of a good faith lien claimant.

If the Commission is concerned about potential harm to a good faith lien claimant from making available a remedy for intentionally filing a false claim of lien, **we could consider a couple of options**:

(1) One option would be to allow a reasonable attorneys fee to the prevailing party. That would penalize a frivolous litigant, with significant deterrent effect.

(2) Another option would be to allow a damages lawsuit only if the property owner demands that the lien claimant release the claim of lien, and the lien claimant fails or refuses to do so. It is arguable that, notwithstanding the inconvenience of a false claim of lien, there is no real damage to the property owner if the lien claimant releases the lien on demand.

Contractors' State License Board

The discussion in Memorandum 2005-24 of remedies for filing a false claim of lien notes that the Contractors' State License Law prohibits a home improvement contractor from recording a security interest against property and provides actual damages plus penalties for a violation.

Mr. Abdulaziz would take all monetary remedies dealing with liens completely out of CSLB jurisdiction. Liens are difficult to understand and CSLB has no expertise concerning them.

The existing mechanics lien law provides for CSLB disciplinary action against a licensee in certain instances where the licensee has failed to take steps that would in effect protect lien rights of laborers. These statutes were enacted at the instance of labor unions. **The staff would be reluctant to propose any diminution of protections in this politically sensitive area.**

PAYMENT BOND

Memorandum 2005-24 discusses provisions relating to payment bonds. Under existing law, a payment bond may be given either by two or more individual sureties, or one admitted surety insurer.

Mr. Abdulaziz notes that a lien release bond requires an admitted surety insurer. He would apply the same rule to payment bonds and other bonds under the mechanics lien law.

The staff is not opposed in principle to this proposal. It would simplify drafting somewhat, and is probably consistent with the constitutional concept that an adequate substitute may stand in the stead of a mechanics lien. An admitted surety insurer is undoubtedly a more adequate substitute than personal sureties.

However, such a provision would go against the general public policy of the state to allow either an admitted surety insurer or two or more personal sureties on a statutory bond. Moreover, it would be yet another improvement in the law that favors lien claimants over property owners, a feature of our work that has concerned the staff. **We think a balanced approach is essential if our statutory overhaul is to be acceptable to the Legislature.**

One possibility would be tentatively to require an admitted surety insurer for a bond under the mechanics lien law, with a note that we will revisit this decision

at the end of the project to test whether, on balance, the proposed mechanics lien law revision treats all interests even handedly.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

Exhibit

COMMENTS OF SAM ABDULAZIZ

June 28, 2005

Sent Via Email Only
<mailto:sterling@clrc.ca.gov>

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RE: Memorandum 2005-24

Dear Mr. Sterling:

I have quickly reviewed your Memorandum. I have not reviewed the various proposed statutes that are attached. The reason for that is that sooner or later, people are going to come out of the woodwork. I do not want to start looking at the minutia yet.

With that said, the following matters apply to your discussion draft.

Notice of Claim of Lien

I agree with you that the owners should get a Notice of Claim of Lien. That could be recorded in the same manner as the Lis Pendens. That would then put the owner on notice of the claim. It would require a mailing and recordation.

Fraudulent Claims

I have more of a problem with this area. I don't have a clue how many fraudulent claims there are. The answer to that question is very similar to the answer that I would give dealing with construction litigation. People ask, "Is there a great deal of construction litigation?" My answer is, "That is all I hear about." So, in my office, there is a great deal of construction litigation. No one ever walks in here saying that they "finished the job early and the owner gave us a bonus even though there wasn't one required in the contract."

I would not want to see a great deal of litigation as to the validity of the lien (I am not referring to stale liens). The lien has a very short time period anyway. I am not sure that 90 days is a problem.

Stale Liens

I tend to agree with you with respect to reasonable fees for the elimination of stale liens. I would leave it up to the judge.

Time for Commencement of Action

I would check with a title insurance company on this matter. I see no reason to automatically make the lien stale if a Notice of Extension of Credit has not been recorded. I am sitting with just such a case now. The owner is a long ways away from the county where the Notice must be recorded. We have already had one person at the County Recorder's Office reject a Notice of Extension of Credit that we have used over and over again. This has been sent by Federal Express to the owner again.

I believe that if the record is void of a valid lien then a transfer, or some change during that period of time would take precedence as to that person alone. That would protect that person as being a bonafide purchaser.

Contractor's Board

I would take all of the monetary remedies dealing with liens completely out of the Contractors' State License Board's jurisdiction. First, the liens are tough to understand and the Contractors' State License Board has no expertise to handle that. I have no problems with punishing someone, but I do not believe that the Contractors' State License Board is the vehicle. I have a problem with making more work for attorneys.

Along this same line of thinking, did you know that the Contractors' State License Board has a penalty for failing to record a lien on Home Improvement Projects. That sure seems counter-productive. If I were having Home Improvement work done, I sure would like it if someone "failed" to record a mechanic's lien.

False Claims

I have some problems with your false claims issues. My experience is that although one may file a false claim in a minor amount, that same person is not going to litigate it. Therefore, the 90-day requirement would be sufficient to protect the public.

Sureties

I definitely would require sureties that are licensed in this state for releases or as other bonds.

Notice To Bonding Company

The Notice to the Bonding Company is going to be a political issue. Typically, bonding companies know the business that they are in, and therefore they have the

ability and requirement to set aside a reserve when a claim comes in. However, the Notice to the Surety that could be served at the same time, and in lieu of a Preliminary 20-Day Notice is not that kind of animal. First, it is relatively new. So there is no statistics upon which a bonding company can adequately assess the reserve requirement. It is probably used very little.

Put yourself in the position of a surety. What does a Preliminary 20-Day Notice mean to you other than some day in the future, I may do some work on this project, I may not get paid in full, and I will look to you for the difference?

I hope this is helpful.

Very truly yours,

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