

Change Is Coming to California's Mechanics Lien Law

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Introduction

On July 1, 2012, the most sweeping changes to California Mechanics Lien Law in more than 50 years will go into effect. Generally speaking, the revised law will resemble your trusty Ford Taurus with 100,000 miles with a new paint job—it will run the same, but will look better.

Although substantive changes were meant to be limited, SB 189 (and related clean-up legislation) will affect the way that any person or entity involved in the construction of private or public projects does business. Thus, it is essential for owners, contractors, material suppliers, design professionals, construction managers, and others involved in the construction industry to understand the many fundamental changes that are coming to California's Mechanics Lien Law.

As discussed below, highlights of the new Mechanics Lien Law include a new statutory scheme, changes in terminology, new definitions of terms, standardization of notice requirements, changes in permitted methods of service of notices, and revisions to current forms, including the statutory releases. In practice, all of the most common notice, claim, and release forms used today will have to be updated and put into practice as of July 1, 2012.

It should be noted that the term "Mechanics Lien Law" does not simply refer to a single construction remedy. Although many inexperienced practitioners believe that the Mechanics Lien Law merely refers to a lien recorded against a private work of improvement, in reality, the Mechanics Lien Law encompasses all construction remedies in the California Civil Code, whether in connection with private or public projects, including the stop payment notice, stop work notice, and payment bond claims.

Historical Perspective

The concept of the right to claim a lien against real property has been in existence since the second century. Under the Roman ruler Marcus Aurelius, a lender of money for improvements had the right to claim a lien on the structure and land on which the structure was built. The concept was simple and functional: Instead of allowing tradesmen to physically remove the benefit provided by their labor and materials and thereby destroy the improvement, the owner's property was impressed with a lien and sold intact (ideally for a greater value) if the debt remained unpaid. This practical and utilitarian concept of lien rights was also adopted in the United States from its earliest origins. In 1791, Maryland enacted the country's first mechanics lien statute. By the time California was admitted into the United States in 1850, the principle of a mechanics lien had been well established throughout the country.

Originally, the mechanics lien rights in California were established by the California Legislative Act of April 12, 1850. Subsequently, mechanics lien rights were incorporated into the California Constitution in 1879, where they remain today. As a result, persons furnishing labor or providing materials have a constitutional right to claim a lien against real property benefited by such labor or materials. Cal Const art XIV, §3. Significantly, a mechanics lien is the only creditor's remedy that is derived from the California Constitution. In deference to the constitutional origin of these special remedies, the courts tread carefully when weighing policy concerns and balancing the competing interests of the lien claimant and the property owner.

In 1872, the first comprehensive mechanics lien statutes were enacted in California. They were initially contained in the Code of Civil Procedure and the Government Code. Although these statutes underwent minor revisions on a continual basis, they endured for more than 75 years before being substantially overhauled in 1951. This revision moved the mechanics lien statutes to Chapter 6 of the

Civil Code. It should be noted, however, that much of the 1951 revisions still contained the arcane and outdated language from the original 1872 Act. After 1951, the legislature enacted minor modifications to these statutes on a piecemeal basis until 1965, when it added sections to the Business and Professions Code mandating bonding requirements for contractors and to the Civil Code providing standards for certain notice requirements.

For the past 60 years, courts have used the Civil Code to define and enforce this important constitutional right and balance the different interests of the owner, lender, contractor, and material supplier. Because of the fundamentally practical underlying principles, construction industry professionals have generally understood the rights and obligations of the parties under the Mechanics Lien Law, as well as their responsibilities and the actions required to protect their individual interests with regard to these statutory remedies. In other words, the system basically worked, but it was not without its flaws.

The California legislature, with the assistance of key advisory groups from owners, contractors, subcontractors, material suppliers, and surety insurers, has now enacted a revised statutory scheme that is meant to centralize all of the mechanics lien statutes and “add a few substantive improvements designed to make it easier for owners to learn about the existence and validity of a recorded lien, and to challenge a clearly invalid lien.” 37 Cal L Rev’n Comm’n Reports 527, 530 (2007). The following is an overview of the changes made to the Mechanics Lien Law by SB 189 and subsequent clean-up legislation.

SB 189-A New Statutory Scheme

Senate Bill 189 (Stats 2010, ch 697), which becomes effective July 1, 2012, revises and recasts statutory provisions and makes both substantive and technical changes to the Mechanics Lien Law. To more easily understand the requirements and protections of the mechanics lien statutes, SB 189 moves all of the applicable mechanics lien statutes to CC §§8000–9566. In addition, the statutes have been grouped as follows:

- **Title 1: Works of Improvement Generally** (CC §§8000–8154). These provisions apply to all aspects of the new statutes, such as definitions, notice provisions, waiver and release provisions, bond provisions, and miscellaneous provisions. For the first time, everyday terms such as “contractor,” “design professional,” “work,” “payment bond,” “contract price,” and “admitted surety insurer” are defined. See CC §§8002, 8010, 8012, 8014, 8030, 8048.
- **Title 2: Private Works of Improvement** (CC §§8160–8848). Title 2 is broken into eight subsections that govern private work construction. Subsections contain provisions regarding completion and notice of completion, preliminary notices, design professional liens, mechanics liens, stop payment notices, payment bonds, owner security requirements, prompt payment, and stop work notices.
- **Title 3: Public Works of Improvement** (CC §§9000–9566). These provisions pertain to public works of improvement and govern such items as completion, preliminary notices, stop payment notices, and payment bonds.

Although the legislative committee did indicate that the revised statutes were not intended to propose radical changes to the operation of the existing construction law remedies, some substantive changes were intended. 37 Cal L Rev’n Comm’n Reports 527, 530 (2007). In addition to the relocation and rearrangement of code sections, SB 189 included substantive changes that are meant to facilitate the understanding of the requirements of the Mechanics Lien Law and avoid confusion that had occurred in interpreting prior statutes. The main substantive changes involve standardizing notice requirements and forms and modifying key terminology to more accurately describe the participants and documents involved.

Because of the significance of the changes, the legislature approved the revised statutes well before their implementation to allow the construction industry some time to become familiar with the revised statutory scheme. However, the legislature did not elect to “phase in” these changes over time; rather, it decided to make all changes effective July 1, 2012.

The Mechanics Lien Law is critical to all persons involved in the construction industry. The following will help practitioners identify the changes to the prior laws and facilitate an understanding of the most important parts of the new law.

Effective Date

Because the Mechanics Lien Law is a series of very detailed statutory procedures that are significant prerequisites to court actions for enforcing claimants' rights to mechanics liens, stop payment notices, and bond claims, the legislature did not make the new changes retroactive. Instead, it declared that "the effectiveness of a notice given or other action taken on a work of improvement before July 1, 2012, is governed by the applicable law in effect before July 1, 2012."

***EXAMPLE:** The recordation of a mechanics lien or the service of a stop payment notice in June 2012 triggers the application of statutory law in effect before July 1, 2012, for determining the validity of that lien or notice, as well as the required preliminary notice, even if the court action to enforce the mechanics lien or stop notice is not filed until August 2012.*

The Most Significant Changes—Highlights

Some of the most sweeping changes to the Mechanics Lien Law are amendments to the basic notice prerequisites to the enforcement of a mechanics lien, stop payment notice, or payment bond remedy. These changes include:

- Modification of the terminology used in the forms themselves;
- Standardization of the notice provisions utilized for all mechanics liens, stop payment notices, payment bond claims, and other notices and forms;
- Changes to the statutory release forms; and
- Modification of certain rules affecting "disputed" stop payment notices.

Changes in Terminology

As noted above, many new terms are defined for the first time in the revised Mechanics Lien Law. In addition, some previously defined terms have been modernized. For example, the term "materialman" has been updated to the gender-neutral term "material suppliers." See CC §8028.

The new law makes three key terminology changes. While some of these changes appear superficial and simple, coupled with the all-new statutory scheme and new code sections, all of the most commonly used forms must be updated to reflect the new terminology and statutory scheme.

First, the term "original contractor" has been changed to "direct contractor." See CC §8018. The antiquated term "original contractor" never achieved widespread use in the construction or legal community. Moreover, more common terms such as "general contractor" or "prime contractor" did not fit in the owner/builder context, in which the owner also acts as a contractor. As such, the legislature selected the term "direct contractor" and defined it as "a contractor that has a direct contractual relationship with an owner." CC §8018.

Second, the prior term "20-day preliminary notice" is now simply known as the "preliminary notice." See CC §8034. Because the preliminary notice is a prerequisite to the enforcement of almost any statutory construction remedy and the forms of these notices are strictly construed by California courts, the preliminary notice form should be immediately updated to reflect the new requirements. California courts have previously found preliminary notices to be invalid for minor and technical deficiencies such as missing bold text and incorrect statutory warning language. See, e.g., *Harold L. James, Inc. v Five Points Ranch, Inc.* (1984) 158 CA3d 1, 204 CR 494, reported at 8 CEB RPLR 55 (Apr. 1985). Because existing case law still will be used to interpret and enforce many aspects of the Mechanics Lien Law, it is imperative to evaluate the new law in light of the case precedents.

Third, the term "stop notice" has been changed to "Stop Payment Notice." See CC §8044. This change was made to prevent common confusion with the regulatory notice (*i.e.*, red tag), clarify the purpose of the notice, and distinguish this notice from the stop work notice. Some interpreted the "stop notice" as a notice requiring actual work to stop on the project rather than the notice's actual

function, which is to *stop payments* between the owner and the general contractor or between the lender and the owner.

Partial Standardization of Notice Requirements

Civil Code §§8100–8118 set forth the standard notice requirements to be utilized for nearly every aspect of the Mechanics Lien Law. In addition to other information required for the particular type of notice, CC §8102 provides the basic required notice components, such as the identification of the owner, direct contractor, lender, project site, and the party giving notice and its relationship to other construction participants, as well as the amount demanded or in dispute. In essence, there will be partial uniformity in the notice requirements for almost all notices, including the preliminary notice, stop payment notice, notice of nonresponsibility, notice of completion or cessation, and notice of recordation of a notice of completion.

To demonstrate the scope of application of these uniform notice requirements, either §8102 or §§8100–8118 are referenced in CC §§8104 (notice to unpaid laborer), 8182 (notice of completion), 8188 (notice of cessation), 8190 (notice of completion or cessation), 8200 (preliminary notice), 8202 (preliminary notice), 8214 (preliminary notice), 8424 (lien release bond), 8444 (notice of nonresponsibility), 8482 (notice requesting release of lien), 8502 (stop payment notice), 8506 (stop payment notice), 8520 (stop payment notice), 8522 (notice regarding payment bond), 8534 (notice of objection to sureties), 8538 (notice of election), 8550 (notice of commencement), 8614 (notice of claim against payment bond), 8712 (notice demanding security), 8800 (notice demanding progress payment), 8816 (notice regarding disputed work), 8832 (stop work notice), 8834 (notice of intent re stop work notice), 8836 (notice to construction lender), 8840 (notice of resolution of claim), 9202 (notice of cessation), 9204 (notice of completion), 9302 (preliminary notice), 9303 (preliminary notice), 9352 (stop payment notice), 9354 (stop payment notice), 9362 (notice of time for commencing action), 9402 (direct contractor’s affidavit regarding release of funds), 9404 (notice of right to serve counteraffidavit), 9406 (claimant’s counteraffidavit), 9408 (notice of hearing regarding stop payment notice), 9412 (notice of court order regarding release of funds), and 9562 (notice of claim against payment bond). In addition, several sections reference CC §§8200–8216 for additional notice requirements, which in turn reference §§8100–8118. See, *e.g.*, CC §§8410, 8508, 8612.

Methods of Service Permitted

SB 189, while providing many of the same delivery methods for service of notices and claims used in the past, modifies the allowable methods of service. For the first time, “overnight delivery by express service carrier” is allowed, but “first class mail” has been eliminated under CC §8110. Thus, practitioners must advise their clients that, as of July 1, 2012, they may no longer serve preliminary notices on public works projects via first class mail.

The Law Review Commission recognized that the construction industry is one of the most paper-intensive industries and would greatly benefit by permitting electronic notices. 37 Cal L Rev’n Comm’n Reports 527, 566 (2007). Although the subject was debated, it was eventually dropped from the legislation.

Changes to Statutory Waivers and Releases

There are four statutory waiver and release forms that are commonly used in the construction industry. These conditional and unconditional waiver and release forms are used to induce the payment of progress and final payments to contractors and material suppliers and generally protect owners, lenders, and direct contractors from “double liability” downstream. The new Mechanics Lien Law breaks up existing CC §3262 and its subparts into smaller, more manageable sections. More specifically, as of July 1, 2012, CC §3262(d)(1), (d)(2), (d)(3), and (d)(4) will be moved to CC §§8132, 8134, 8136, and 8138, respectively.

The most significant changes to statutory waivers and releases, however, are in the language of the forms themselves. Starting July 1, 2012, parties must revise their existing statutory waiver and release

forms to comply with the new statutes, or else the owners, lenders, and direct contractors that rely on such waivers and releases may find that the releases are ineffective and unenforceable.

Stop Payment Notice Changes

SB 189 includes three key changes that facilitate a party's ability to provide a stop payment release bond. Formerly, only the owner, lender, direct contractor, or subcontractor could post a stop payment release bond. Effective July 1, 2012, any party may obtain a stop payment release bond. CC §8510(a).

The statutory language has also been revised to provide that a stop payment notice release bond must be issued by an "admitted surety insurer." CC §8510(a). Formerly, under CC §3171, the bond was required to be issued by a "good and sufficient surety." This change in the language of the statute leaves unanswered whether a claimant can disqualify an "admitted surety insurer" based on its financial condition or otherwise.

The new statutes eliminate the requirement contained in the prior law that a contractor must first dispute the validity of a stop payment notice before obtaining a release bond. Now, perhaps because a contractor wants to maintain a business relationship upstream, any party can procure a stop payment release bond for any reason.

Summary of Other Substantive Changes

SB 189 states that the revisions made to the California statutes were intended to be mostly nonsubstantive. The bill, however, specifically identifies the following new Civil Code sections as having substantive changes from the former statutory scheme. A short description of these substantive changes is provided below.

<i>New CC Section</i>	<i>Comment</i>
8014	Landscape architects are now entitled to a mechanics lien.
8064	Owner can execute documents on behalf of co-owner.
8122	Subcontractors cannot waive lien rights of others by contract.
8128	Clarifies stop payment notice release and reduction notice release.
8132	Revised lien waiver form.
8182	Notice of completion now can be filed within 15 days of completion.
8186	Time allowed for recording notice of completion is eliminated.

		xa7;&	xa7;8100&	x2013;8118.
8190	Owner must provide a notice of the filing of a notice of completion to the direct contractor and claimants that provided a preliminary notice under &			
8200				Clarifies that the direct contractor must provide a preliminary notice to the construction lender.
8424				Penal sum of mechanics lien release bond is now 125 percent (not 150 percent) of claim.
8460	Combines previous &	xa7;&		xa7;3144 and 3145 regarding time to foreclose and effect of not filing suit.
8482				Before bringing a petition to release property from a lien, an owner must now demand in writing that a claimant release the lien at least 10 days before filing the petition.
8486				Court must rule on petition to remove invalid lien within 60 days; notice is required 15 days before hearing.
8488				Burden of proof on petitioner to prove defects in a lien, while claimant has burden of establishing the validity of lien amount.
8510	Any person may obtain release bond from &		x201c;admitted surety insurer.&	x201d;
8604				If lender accepts payment bond, it may not later object to validity.
8606	Bonds must be issued by an &		x201c;admitted surety insurer.&	x201d;
8800	Notices demanding	xa7;&	xa7;8100&	x2013;8118. An owner who fails to pay within 30 days

	progress payments must meet the notice requirements of &			of receipt of the notice is liable for 2-percent interest per month unless there is a good faith dispute.
		xa7;&	xa7;8100&	x2013;8118.
8834	Notice of the intent to issue a stop work notice must be posted 5 days before giving the stop work notice and must comply with the notice requirements of &			
8844				Owner may now seek expedited hearing for liability on stop payment notice.
9200				Defines completion for public project.
9204				Notice of completion may be recorded within 15 days of completion.
9362				Claimant must pay stop payment notice fee of \$10 (previously \$2) to receive notices from the public entity after completion of a public works contract and recordation of notice of cessation or completion.
		xa7;&	xa7;8100&	x2013;8118 is deemed complete 5 days after mailing.
9408	Notice under &			
9550				While a direct contractor who is awarded a public contract in excess of \$25,000 must provide a payment bond, the section clarifies that a design professional is not a direct contractor for purposes of this section, and thus is not required to provide a payment bond to the public entity when it contracts directly with the public entity.
9558				Suit on payment bond now only allowed by claimants, not by assigns.

The following former Civil Code sections have been discontinued under the new statutory scheme:

Former CC Section

Comment

3086(b)

The previous criteria for completion and acceptance by the owner have been removed.

3105

The definition for the term &

x201c;subdivision&

x201d; has been removed.

3123(c)

The owner no longer has to notify the direct contractor or construction lender if the contract price is exceeded by 5 percent.

x2013; &

xb6;2

3131 &

The separate distinction of completion of a residential unit containing multiple condominium units is no longer included in determining the time for filing an action on a single residential unit.

3149

Deleted former provision for separate claims on property to be joined and consolidated by the court.

3204

Deleted former provision precluding any code section from eliminating the right to a jury trial under the California Constitution; a party may waive that right.

x2013; &

xb6;1

3260(c) &

A public entity&

x2019;s issuance of a certificate of occupancy is no longer a criterion for establishing the date of completion for purposes of calculating the start of the 45-day period when retention payments are due.

x2013; &

xb6;2

3260(c) &

The date of completion on a notice of completion issued by a public entity

is no longer a criterion for establishing the date of completion regarding the start of the 45-day period when retention payments are due.

Clean-Up Legislation—SB 293

Part of the clean-up legislation for SB 189 includes SB 293 (Stats 2011, ch 700), which affects CC §§8612 and 9560. As of July 1, 2012, revisions to statutes drastically limit the use of the “15/75-day” preliminary bond claim notice. Previously, material suppliers and subcontractors that neglected to serve a preliminary notice had a safeguard, provided that the claimant timely and properly served a preliminary bond claim notice on the direct contractor and payment bond surety.

Specifically, sub-subcontractors and material suppliers that furnish labor or materials to a first-tier subcontractor in contractual privity with a direct contractor may give preliminary notice to the surety and bond principal. CC §8612(c). However, such claimants are precluded from enforcing a payment bond claim based on the 15/75-day notice to the payment bond surety and bond principal to the extent that the surety or principal has made payment (or has a good faith dispute regarding payment) to the first-tier subcontractor. CC §8612(d). In essence, under the new law, direct contractors now have a new defense to last-minute claims. Many material suppliers and sub-tier subcontractors will not be able to rely on the safeguards of the 15/75-day bond notice.

Conclusion

Clearly, although intending to simplify and clarify the requirements and protections regarding mechanics liens, stop payment notices, and payment bond issues, SB 189 has significantly modified the previous California statutes. Even though the majority of these changes involve notice requirements or relocation within the statutes, owners, contractors, and material suppliers must become familiar with the new statutes to protect their individual interests.

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