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John Leary

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The Conflict Between the California Mechanics' Lien Statutes and the Public Utilities Code

by
JOHN LEARY*

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* Associate, White & Case, Los Angeles. B.S.F.S., Georgetown University, 1987; J.D., University of California, Hastings College of the Law, 1992.

Introduction

The breakup of AT&T created opportunities for the growth of local telephone companies.¹ Many of these companies have sought to construct new telephone lines to provide expanded service.² Such construction may lead to a problem that California law does not currently address.

This note discusses the conflict between the California Public Utilities Code ("Public Utilities Code") and the portions of the California Civil Code ("Civil Code") that address mechanics' liens and stop notices.³ A conflict exists in that public utilities, as defined by the Public Utilities Code,⁴ seem to be exempt⁵ from mechanics' liens placed on their property; yet according to the Civil Code, only "public entities" are exempt from mechanics' liens.⁶ A recent California case held that public utilities do not fall within the statutory definition of "public entities," implying that they are not exempt from mechanics' liens.⁷

The conflict between the two codes arises in situations such as where the Public Utilities Commission ("PUC") approves a private company's application to offer telephone service to the public.

1. See Ronald Rosenberg, *Competitors Putting Heat on N.E. Telephone*, BOSTON GLOBE, Feb. 9, 1992, at 81. The article describes the growth of "alternative access providers" in the Boston area. These companies are "local" in that they provide telephone service within limited geographic areas.

2. *Id.*

3. See CAL. CIV. CODE §§ 3109-3214 (Deering 1986). Mechanics' liens are liens that are placed on works of improvement by subcontractors to ensure that the subcontractors are paid for the labor or material they provided. The liens are a creature of statute, ensuring that the subcontractors have a remedy against the owners of the works of improvement. At common law, the subcontractors, lacking privity of contract with the owner, would not have a remedy.

Stop notices are similar to liens in that they attach to property of the owner, but not to real property. If a stop notice is properly filed, it acts to place a lien of sorts on the construction fund (the amount of the undisbursed monies the owner owes the original contractor). A stop notice obligates the owner to make no further disbursements from the construction fund until the claim of the stop notice claimant is satisfied or the fund is exhausted.

4. CAL. PUB. UTIL. CODE § 216(a) (Deering 1990 & Supp. 1991).

5. *Id.* § 851 (Deering 1990).

6. California Civil Code section 3109 states that mechanics' liens do not apply to any "public work." Section 3100 defines "public work" as "any work of improvement contracted for by a public entity." Section 3099 defines "public entity" as "the state, Regents of the University of California, a county, city, district, public authority, public agency, and any other political subdivision or public corporation in the state." CAL. CIV. CODE § 3099 (Deering 1990). Public utilities are conspicuously absent.

7. *Automatic Sprinkler Corp. v. Southern Cal. Edison Co.*, 266 Cal. Rptr. 662 (Ct. App. 1989). See discussion *infra* at notes 81-87 and accompanying text.

The company is thereafter considered a public utility.⁸ This newly created utility may decide to construct underground conduits to house its phone lines. To this end, the company hires a general contractor to build the conduits. If, during the course of construction, the general contractor runs out of funds and cannot meet its obligations to subcontractors,⁹ the subcontractors may attempt to place mechanics' liens on the conduit.¹⁰

There are indications that a public utility is exempt from mechanics' liens, but the law is not well established.¹¹ Section 851 of the Public Utilities Code states that no one may encumber the property of a public utility that is necessary and useful for service to the public without the approval of the PUC.¹² The PUC and California courts of appeal have

8. CAL. CONST. art. XII, § 3. An entity may also be considered a utility if it operates telephone lines for the use or accommodation of a definite portion of the public. See CAL. PUB. UTIL. CODE § 216.

9. For the purposes of this note, "subcontractors" will be used to refer to all people entitled to mechanics' liens, as defined in California Civil Code section 3110.

10. The conduit, is known as a "work of improvement." California law defines "work of improvement" as,

the construction, alteration, addition to, or repair, in whole or in part, of any building, wharf, bridge, ditch, flume, aqueduct, well, tunnel, fence, machinery, railroad, or road, the seeding, sodding, or planting of any lot or tract of land for landscaping purposes, the filling, leveling, or grading of any lot or tract of land, the demolition of buildings, and the removal of buildings.

CAL. CIV. CODE § 3106 (Deering 1990).

11. See *infra* notes 56-60 and accompanying text.

12. California Public Utilities Code section 851 states:

No public utility other than a common carrier by railroad subject to Part I of the Interstate Commerce Act (Title 49, USC) shall sell, lease, assign, mortgage, or otherwise dispose of or encumber the whole or any part of its railroad, street railroad, line, plant, system, or other property necessary or useful in the performance of its duties to the public, or any franchise or permit or any right thereunder, nor by any means whatsoever, directly or indirectly, merge or consolidate its railroad, street railroad, line, plant, system, or any other property or franchises or permits or any part thereof, with any other public utility, without having first secured from the commission an order authorizing it to do so. Every such sale, lease, assignment, mortgage, disposition, encumbrance, merger, or consolidation made other than in accordance with the order of the commission authorizing it is void. The permission and approval of the commission to the exercise of a franchise or permit under Article 1 (commencing with § 1001) of Chapter 5 of this part, or the sale, lease, assignment, mortgage or other disposition or encumbrance of a franchise or permit under this article shall not revive or validate any lapsed or invalid franchise or permit, or enlarge or add to the powers or privileges contained in the grant of any franchise or permit, or waive any forfeiture.

Nothing in this section shall prevent the sale, lease, encumbrance or other disposition by any public utility of property which is not necessary or useful in the performance of its duties to the public, and any disposition of property by a public utility shall be conclusively presumed to be of property which is not useful or necessary in the performance of its duties to the public, as to any purchaser, lessee or encumbrancer dealing with such property in good faith for value; provided, however,

interpreted section 851 to mean that the PUC has the power to invalidate any liens placed on public utility property without PUC approval.¹³ Yet there is no express procedure within the PUC for applying for such approval.

The relevant statutes within the Civil Code governing mechanics' liens do not mention utilities.¹⁴ They say only that mechanics' liens may not be placed on the works of "public entities,"¹⁵ and as noted above, a recent decision has held that utilities are not "public entities."¹⁶

Under the Civil Code, the liens are presumed valid if properly filed.¹⁷ Under the Public Utilities Code, the liens are presumed invalid.¹⁸ There lies the conflict.

Subcontractors will maintain that the Civil Code should prevail. They will argue that a court should allow their liens on utility property, because mechanics' lien law is to be interpreted broadly to ensure that they have a remedy¹⁹ and to ensure that the owner of the work of improvement is not unjustly enriched.²⁰

The owner (the public utility) will maintain that the Public Utilities Code should prevail. The utility will urge a court to declare any lien invalid because public policy disallows the property of a utility used to serve the public to be encumbered by a lien and therefore subject to foreclosure and sale. The utility will also argue that section 851 specifically addresses the issue, while the mechanics' lien statutes are silent.

As applied to telephone conduits, the utility can make numerous other arguments turning on how the conduit is characterized: whether it is a fixture, whether it is personal property, and whether the conduit lies on an implied easement through the land. These distinctions may be important, because the manner in which the conduit is characterized determines to what the lien attaches.

that nothing in this section shall apply to the interchange of equipment in the regular course of transportation between connecting common carriers.

(Deering 1990).

13. *In re Golconda Utils. Co.*, 65 P.U.C. 174, 175-76 (1965); *Hosford v. Henry*, 238 P.2d 91, 97 (Cal. Ct. App. 1951).

14. CAL. CIV. CODE §§ 3109-3154 (Deering 1990 & Supp. 1991).

15. *Id.* § 3099 (Deering 1986).

16. *Automatic Sprinkler Corp. v. Southern Cal. Edison Co.*, 226 Cal. Rptr. 662 (Ct. App. 1989).

17. CAL. CIV. CODE §§ 3109-3154 (Deering 1986).

18. See CAL. PUB. UTIL. CODE § 851, which declares that any encumbrance is invalid if it is not first approved by the PUC.

19. *Corbett v. Chambers*, 41 P. 873, 875 (Cal. 1895).

20. See *John R. Gentle & Co. v. Britton*, 111 P. 9 (Cal. 1910) (interprets mechanics' liens as providing a method by which the owner is estopped from enjoying the subcontractor's efforts without compensating the subcontractor).

Stop notices, another device by which subcontractors can secure payment, seem to provide an alternative remedy. Stop notices, however, were created to provide a remedy for subcontractors working for "public entities."²¹ Thus, when working for a utility (which is not a "public entity"²²), subcontractors would seem justified in relying on mechanics' liens to provide relief from a defaulting contractor. Yet if mechanics' liens cannot attach to the property of a utility, the only remedy for subcontractors is the stop notice.

This creates two problems. First, subcontractors are not on notice that their only remedy is the stop notice because the issue of mechanics' liens on the property of a utility has never been fully addressed. Unaware that their only remedy is a stop notice, subcontractors may opt only to file mechanics' liens. Second, under the Civil Code, a subcontractor's only remedy is a stop notice when the owner is a public entity, and the public entity is required by law to post a payment bond.²³ Because utilities are not "public entities,"²⁴ they need not post such a bond, so it is conceivable that subcontractors are protected by neither mechanics' liens nor stop notices. The mechanics' liens are no protection if the PUC declares them void, and the stop notices are no protection if the construction fund is exhausted without a payment bond to ensure payment.²⁵

This note will discuss the situations in which the need for mechanics' liens and stop notices arises and the procedures for obtaining them. The note will then discuss the Public Utilities Code. The conflict between the two areas of law will be analyzed, and a solution offered.

I

Background

A. Mechanics' Liens and Stop Notices

When someone (usually the owner of the underlying property) hires a contractor to undertake a work of improvement, the contractor will hire subcontractors specializing in various trades to assist him. The contractor is paid directly by the owner. The owner may pay in installments

21. *Weldon v. Superior Court of Los Angeles County*, 71 P. 502 (Cal. 1903).

22. *See infra* notes 82-86 and accompanying text.

23. CAL. CIV. CODE § 3247 (Deering 1984 & Supp. 1991). The California Civil Code requires every contractor who is awarded a public works contract exceeding \$25,000 to post a payment bond. *Id.*

24. *See infra* notes 82-86 and accompanying text.

25. A stop notice acts as a lien against the res, the construction fund. The stop notice acts *only* against the fund, and any payments to the subcontractors are limited by the amount remaining in the fund when the owner receives the first stop notice. If the amount of claims exceeds the amount of the fund, the fund is interpleaded and divided among the claimants. *See infra* notes 36-45 and accompanying text.

corresponding to the progress on the work of improvement. The subcontractors are not in contract with the owner and look to the contractor for payment. If the contractor does not pay the subcontractors, under common law rules of contract, the subcontractors are not able to look to the owner (the beneficiary of their efforts) for compensation because they lack privity of contract. The mechanics' lien statutes were promulgated to remedy this problem.²⁶

Whenever a subcontractor provides labor or material for a work of improvement, the subcontractor must send to the owner a Preliminary Notice in order to preserve its lien rights.²⁷ The Preliminary Notice alerts the owner to the fact that the contractor has hired a subcontractor and tells the owner how much the subcontractor expects to be paid for its efforts.²⁸ If the subcontractor is not paid within ninety days of the completion of the work of improvement (thirty days if the owner has posted a Notice of Completion), the subcontractor may file a lien on the improved property with the County Recorder.²⁹

A mechanics' lien works as any other lien; it attaches to and encumbers title to the property.³⁰ If, ninety days after filing the lien, the subcontractor has not been paid, the subcontractor may file suit to foreclose the lien, and be paid what he is owed from the proceeds of a foreclosure sale.³¹

Mechanics' liens are authorized in the state constitution.³² They are an equitable remedy³³ designed to ensure that the providers of labor and material are compensated for their efforts.³⁴ As such, the mechanics' lien statutes in the Civil Code are to be liberally construed.³⁵ This is important, because it adds credence to the argument favoring enforcement of the liens when enforcement would conflict with the Public Utilities Code.

If the subcontractor chooses not to file a mechanics' lien, it has an additional remedy in the stop notice.³⁶ Stop notices are statutory alternatives to mechanics' liens. They were created for situations where the owner is a "public entity."³⁷ Foreclosing on property owned by a public

26. *Nolte v. Smith*, 11 Cal. Rptr. 261 (Ct. App. 1961).

27. CAL. CIV. CODE §§ 3114, 3160 (Deering 1986).

28. *Id.* § 3097 (Deering 1986 & Supp. 1991).

29. *Id.* § 3116 (Deering 1986).

30. *Ritter v. Stevenson*, 7 Cal. 388, 389 (1857).

31. CAL. CIV. CODE § 3144 (Deering 1986).

32. CAL. CONST. art. XIV, § 3.

33. *John R. Gentle & Co. v. Britton*, 111 P. 9, 10 (Cal. 1910).

34. *Borchers Bros. v. Buckeye Incubator Co.*, 379 P.2d 1, 3-4 (Cal. 1963).

35. *Baker v. Hubbard*, 161 Cal. Rptr. 551, 555 (Ct. App. 1980); *Continental v. Hutton*, 78 P. 21, 21 (Cal. 1904).

36. *See* CAL. CIV. CODE §§ 3156-3175 (Deering 1986 & Supp. 1991).

37. *Bates v. County of Santa Barbara*, 27 P. 438, 439 (Cal. 1891).

entity does not serve the best interests of the public, so when the owner is a public entity, stop notices are the sole remedy.³⁸ Stop notices, however, are not limited to situations where the owner is a public entity. They may be used in addition to, and cumulative with, mechanics' liens if the owner is a private entity.³⁹

Stop notices are considered equitable garnishments.⁴⁰ They do not attach to land or property, but to the construction fund the owner owes to the contractor.⁴¹ An owner who receives a stop notice (which also must be recorded with the County Recorder) is not obligated to make further payments to the contractor.⁴² The money that the owner would normally be paying the contractor under the terms of the contract remains with the owner, as the construction fund. Between ten and ninety days after the work of improvement is completed, the subcontractors who have not been paid and who have filed valid stop notices may sue to enforce their notices.⁴³ At that time, the owner may deposit the construction fund with the court, and the court will disburse it among the subcontractors in an interpleader action.⁴⁴ If the amount of the fund is insufficient to satisfy all the claims, the fund will be apportioned, with each subcontractor receiving a pro rata share.⁴⁵

B. The Public Utilities Code

To become a public utility, an entity need only file a petition with the PUC.⁴⁶ In the case of telephone companies, this petition would be a

38. See *supra* text accompanying note 6.

39. *Calhoun v. Huntington Park First Sav. & Loan Ass'n*, 9 Cal. Rptr. 479, 484 (Ct. App. 1960).

40. *Id.*

41. *Harsco Corp. v. Department of Pub. Works*, 98 Cal. Rptr. 337, 339 (Ct. App. 1971).

42. The owner has a duty to make no further payments unless the owner posts a payment bond pursuant to California Civil Code section 3235. CAL. CIV. CODE § 3161 (*Deering 1986 & Supp. 1992*).

43. *Id.* § 3172 (*Deering 1986*).

44. *Id.* § 3175 (*Deering 1986*).

45. *Id.* § 3167 (*Deering 1986*).

46. California Public Utilities Code section 1001 (*Deering 1990*) states that in order for an entity to commence any construction of facilities to serve the public it must first obtain a Certificate of Convenience and Necessity from the PUC. Once an entity has been granted such a certificate, the PUC recognizes it as a utility.

An entity may be considered to be a utility without applying for such a certificate, however. The California Constitution sets broad guidelines, declaring all entities which own, operate, control or manage a line, plant, or system for the transportation of people and property, the transmission of telephone messages, or the production, generation, transmission, or furnishing of heat, light, or water are public utilities subject to control of the PUC. CAL. CONST. art. XII, § 3.

For cases interpreting these guidelines, see *Allen v. Railroad Comm'n of Cal.*, 175 P. 466 (Cal. 1918); *Greyhound Lines v. Public Utils. Comm'n*, 438 P. 2d 801 (Cal. 1968).

request for a Certificate of Public Convenience and Necessity to provide telephone service to the general public.⁴⁷ The petition must contain such information as the projected service area and client base, the nature of the telephone services to be offered, the financial stability of the proposed utility, and the means by which the utility's customers would be served (e.g., using existing lines or building new ones).⁴⁸ If the PUC grants the utility's petition, it issues an Order allowing the utility to proceed and a Certificate declaring the entity a public utility.

The PUC oversees and regulates utilities in accordance with the Public Utilities Code.⁴⁹ The Public Utilities Code places strict restrictions on utilities and allows the PUC to regulate nearly every aspect of a utility's operations that affect the public. Some examples of the PUC's authority include the regulation of rates,⁵⁰ the construction of new facilities,⁵¹ and the transfer of property.⁵² Although it is a relatively simple procedure to be declared a public utility, utilities' activities must be strictly regulated because utilities are unique entities providing essential services to the public.⁵³ The demand for these services is generally inelastic, so there is potential for abuse and exploitation if the utilities are not strictly regulated.⁵⁴

The crux of this note involves section 851 of the Public Utilities Code, which declares that no utility may encumber any of its property that is "necessary and useful" in its service to the public without the prior approval of the PUC.⁵⁵ There are two California cases which indicate that this prohibition on encumbrances applies to liens.

In *Hosford v. Henry*,⁵⁶ the defendant Henry operated a water and power company licensed by the PUC. He borrowed money from Hosford, securing his debt with a deed and a note. Prior to borrowing the money, Henry applied to the PUC for permission to encumber the portion of property secured by the note. He obtained PUC approval, but in the PUC application, only two small parcels of land were mentioned as security. Hosford claimed that pursuant to an earlier understanding, the entirety of Henry's utility property was secured by the deed. He asked the trial court to reform the contract, grant a lien over all the utility

47. CAL. PUB. UTIL. CODE § 1001 (Deering 1986).

48. *See id.* §§ 1001-1011 (Deering 1986).

49. *Id.* § 701 (Deering 1986).

50. *Id.* §§ 726-745 (Deering 1986).

51. CAL. PUB. UTIL. CODE §§ 761-786 (Deering 1986).

52. *See id.* §§ 851-56 (Deering 1986).

53. *Pacific Tel. & Tel. Co. v. Public Utils. Comm'n*, 401 P.2d 353 (Cal. 1965).

54. *Id.*

55. CAL. PUB. UTIL. CODE § 853 (Deering 1980).

56. 238 P.2d 91 (Cal. Ct. App. 1951).

property, and foreclose on the lien. The trial court did so. The appellate court reversed, saying that PUC approval was absolutely necessary for the placement of a lien, regardless of how the trial court reformed the contract.⁵⁷ The appellate court upheld the authority of the PUC, saying that a court in equity had no power to impose a lien that had not been previously approved by the PUC.⁵⁸

In *In re Golconda Utilities Company*,⁵⁹ the PUC declared a sheriff's foreclosure sale on utility property void because it was undertaken without PUC approval. The sheriff's sale was the result of the foreclosure of a mechanics' lien. The PUC said that the sale was directly contrary to section 851 of the Public Utilities Code and therefore invalid. The PUC did suggest, however, that authorization for the transfer "might possibly have been obtained by the transferee upon a showing that the transfer would not impair . . . service to the public," but the PUC failed to delineate the procedure by which the transferee might make such a showing.⁶⁰

II Analysis

The section above demonstrates the conflict between the mechanics' lien statutes and the Public Utilities Code. The conflict can easily arise when a telephone company, seeking to construct new lines, hires a contractor who defaults on payments to the subcontractors. Under the mechanics' lien law, subcontractors have the option of filing a mechanics' lien, a stop notice, or both.⁶¹ If they elect to file a mechanics' lien, they may not be able to foreclose on the lien because of the language of section 851 of the Public Utilities Code.

There is nothing in the Public Utilities Code addressing mechanics' liens other than section 851, and public utilities are never specifically mentioned in the mechanics' lien statutes, so one must turn to the case law for a resolution. Unfortunately, there is no case law on point, perhaps because the deregulation of the telephone industry is a fairly recent occurrence.⁶² Thus, the only way to find a solution to the conflict is to attempt to analogize the situation to existing law.

57. *Id.*

58. *Id.* at 98. The *Hosford* court interpreted sections 51 and 52 of the Public Utilities Code, which have since been repealed. However, section 851 of the Code incorporates the relevant language of these sections almost verbatim.

59. 65 P.U.C. 174 (1965).

60. *Id.* at 176.

61. *Bates v. County of Santa Barbara*, 27 P. 438 (Cal. 1891).

62. *See Rosenberg, supra* note 1.

There are several ways to approach and analyze the situation. One may try to discern if it is even proper for a lien to attach to anything. Under mechanics' lien law, the lien normally attaches not only to the work of improvement itself but also to the property on which it sits.⁶³ This is so because the owner of the land will most likely benefit from any improvement to the property, and a lien preserves the rights of the sub-contractors if the work of improvement is torn down or destroyed. In the case of telephone lines, however, the owner of the underlying property is usually the city or county in which the utility operates. Telephone conduits that carry lines are usually constructed beneath streets or on poles along sidewalks.

To construct a telephone conduit beneath a city's streets, a utility need only apply to the city for a permit.⁶⁴ Initially, the permit gives the utility a license to lay and maintain the conduit on the public land.⁶⁵ Over time, the license may expressly or impliedly become an easement.⁶⁶ Thus the work of improvement (the conduit) remains distinct from the real property on which it sits.

The California Supreme Court has held that a lien may exist on the work of improvement alone and need not attach to the underlying property. In *English v. Olympic Auditorium*,⁶⁷ the court said that the word "property" as used in the constitutional provision providing for mechanics' liens⁶⁸ "obviously refers to the building or other structure for which the materials have been furnished or labor bestowed . . ."⁶⁹ The court also stated that "a lien may exist on a structure independently of the land upon which it is erected . . ."⁷⁰

Although this case arose in a situation where the work of improvement was on rented land, a court could easily infer that such a holding applies when the work of improvement lies on a license or easement. A court choosing to make such an inference would hold that a lien attaches to the conduits without regard to the public streets under which they lie.

A second important issue regarding the conduits is whether a court would consider them real property or personal property. Two cases in-

63. CAL. CONST. art. XX, § 15 (repealed 1972); CAL. CIV. CODE §§ 3110 and 3128 (Deering 1986).

64. *Pettis v. General Tel. Co. of Cal.*, 54 Cal. Rptr. 476, 478 (Ct. App. 1966) *superseded* by 426 P.2d 884 (Cal. 1967).

65. *Id.* at 479.

66. *Id.*

67. 20 P.2d 946 (Cal. 1933).

68. The court interprets article XX, section 15 of the California Constitution. Section 15 was repealed in 1976, but article XIV, section 3 (adopted 1976), is identical but for the substitution of "persons furnishing materials" for "materialmen."

69. *English*, 20 P.2d at 951.

70. *Id.*

volving water pipelines address this issue,⁷¹ and they conflict. If the conduits are classified as real property, then there is no problem with a lien attaching to them. But if the conduits are classified as personal property, then they may or may not be subject to a lien. A recent case has held that personal property is subject to a mechanics' lien only if it has metamorphosed into a fixture.⁷²

Whether or not something is a fixture is a question of fact,⁷³ and a wide variety of items have been held to be fixtures.⁷⁴ The Civil Code offers little guidance, merely stating that an object is a fixture if it is attached to or imbedded in the land.⁷⁵ The case law directs the courts to look to the permanency of the object as well as to the intent of the parties.⁷⁶ Because of the permanent nature of a telephone conduit, it seems likely that a jury would find a conduit to be a fixture, and therefore subject to a mechanics' lien. This raises another problem. Section 1013 of the Civil Code states that when a person affixes property to the land without an agreement to remove it, the thing affixed becomes the property of the owner of the land. This seems to indicate that the conduit belongs to the city (absent an agreement to remove it), but this is hardly likely in light of the discussion of licenses and easements above.⁷⁷

Even if telephone conduits can be characterized as property that is subject to mechanics' liens, a problem arises from the language of section 851 of the Public Utilities Code. As noted earlier, section 851 states that any encumbrance of utility property without the consent of the PUC is void.⁷⁸ A lien is an encumbrance, and the case law seems to indicate that the PUC can declare such a lien void if obtained without its approval.⁷⁹ Yet there may be some dispute as to whether "encumber" applies to the subcontractors, or just to the utility. For example, section 851 states, "No public utility . . . shall . . . encumber . . ."⁸⁰ This prohibits the utility from actively encumbering property. Yet with the filing of a mechanics' lien, it is the subcontractors who are encumbering the property, not the utility. Of course, the property is still encumbered, but the utility has not actually encumbered it directly through its own actions.

71. *Robinson v. City of Glendale*, 187 P. 741 (Cal. 1920); *City of Vallejo v. Burrill*, 221 P. 676 (Cal. Ct. App. 1923).

72. *Energrey Enters. v. Oak Creek Energy Sys., Inc.*, 119 B.R. 739, 742 (E.D. Cal. 1990).

73. *Gosliner v. Briones*, 204 P. 19, 20 (Cal. 1922).

74. See 44 C.J.S. *Mechanics' Liens* § 38 (1978).

75. CAL. CIV. CODE § 660 (Deering 1986).

76. *Collins Elec. v. Shasta County*, 101 Cal. Rptr. 285 (Ct. App. 1972) (quoting *County of Ventura v. Channel Islands State Bank*, 59 Cal. Rptr. 404, 409 (Ct. App. 1967)).

77. See *supra* notes 64-66 and accompanying text.

78. See *supra* note 12 for the text of § 851.

79. See *supra* notes 56-60 and accompanying text.

80. CAL. PUB. UTIL. CODE § 851 (Deering 1990).

A likely explanation is that the authors of the Public Utilities Code did not anticipate any encumbrances of utility property in which the utility did not take an active role.⁸¹

The Public Utilities Code does not provide a procedure for third parties to follow if they wish to obtain permission to encumber a utility's property with a lien. This may be an oversight. On the other hand, it may be that allowing liens on property used by a utility for public service presents too many logistical problems, such as how a foreclosure sale would operate and whether only utilities would be allowed to bid. To allow property that had been used to serve the public to fall into private hands seems contrary to public policy. Yet if liens cannot attach, then the subcontractors who did not file stop notices are left without a remedy, and the owner is perhaps unjustly enriched.

In a recent case, *Automatic Sprinkler Corp. v. Southern California Edison Co.*,⁸² the plaintiff sought to have utilities declared "public entities" under the definition in the Civil Code.⁸³ The plaintiff suggested that because it is against public policy for liens to attach to utility property, utilities should be declared public entities, forcing them to post a bond for every construction project, and making stop notices the sole remedy.⁸⁴ The court refused to classify the utility as a public entity, saying that utilities are not public entities under the statutory definition.⁸⁵ The court declined to comment on whether the mechanics' lien was enforceable against the utility, because the lien was not filed in the proper county and was therefore invalid.⁸⁶

The court erred. Following the flawed reasoning of the *Hosford* and *Golconda* decisions, the court merely said that section 851 does not preclude the recording and enforcement of mechanics' liens.⁸⁷ The court stated that section 851 permits a lien if "the Public Utilities Commission first issues an authorizing order." "Thus," the court continued, "the section does not 'preclude' a mechanics' lien."⁸⁸ Unfortunately, the court

81. The case law is silent on this particular point, but when looking at section 851, one should note that all the verbs that follow the proscription, "No public utility. . . shall. . ." are active verbs ("sell, lease, assign, mortgage, dispose . . ."). The utility, the subject of the sentence, is the actor with regard to all the verbs, presumably including the verb "encumber." To a utility, a mechanics' lien is a passive encumbrance, occurring as a consequence of actions by a party other than the utility. Thus, it can be argued that mechanics' liens are not contemplated by section 851.

82. 266 Cal. Rptr. 662 (Ct. App. 1989).

83. See CAL. CIV. CODE § 3099 (Deering 1990); see also *supra* note 6 and accompanying text.

84. *Automatic Sprinkler*, 266 Cal. Rptr. at 663.

85. *Id.*

86. *Id.* at 667.

87. *Id.*

88. *Id.*

did not look beyond section 851 to recognize that in practice it *does* preclude the recordation and enforcement of a mechanics' lien.

It precludes a mechanics' lien in two ways. First, as noted above, there is no procedure by which a subcontractor can petition for PUC authorization to record and enforce a lien. Second, a subcontractor is not on notice that section 851 applies to mechanics' liens because section 851 is not mentioned anywhere in the mechanics' lien statutes. Even if a subcontractor were deemed to have constructive notice of the applicability of section 851 when working on a work of improvement owned by a utility, there is no statutory method by which a subcontractor receives notice that the owner is a utility. Without any requirement that the owner/utility give notice that it is a utility and that section 851 applies, there is no reason for a subcontractor to suspect that it is working for a utility and therefore must petition the PUC to obtain a lien.

An examination of Civil Code section 3099⁸⁹ reveals an extensive list of what is considered a "public entity." The *Automatic Sprinkler* court scanned the list and did not find public utilities. The court could have easily inferred that public utilities fell into this category, but it felt bound by the exact language of the statute. Therefore, it is the legislature's duty to remedy the situation.

III Proposal

There are several possible solutions to the problem. One option would be to enact a statute allowing subcontractors to encumber the property of a utility without obtaining the permission of the PUC. This is not the best alternative, because a lien could lead to a foreclosure sale, in which property used to serve the public is purchased by a private entity. Such a private entity would not be approved by the PUC, nor granted a permit by whichever governmental body owns the land on which the property sits. This option has the undesirable potential to remove from the public domain property devoted to the public good.

Alternatively, the legislature could enact a statute making it clear that mechanics' liens are invalid against utilities and that utilities are not required to post payment bonds. This would provide the subcontractors with notice that their only remedy is a stop notice, but would not protect them from the early draining of a construction fund.

Another option would be for the PUC to enact a regulation under which utilities would be required to disclose their status as utilities to all subcontractors and provide notice of section 851. This could be done

89. CAL. CIV. CODE § 3099 (Deering 1990); see also *supra* note 6 and accompanying text.

easily, by requiring the utility to mail notice of its status to every entity from which it receives a Preliminary Notice.⁹⁰ In conjunction with that regulation, the PUC could enact a regulation outlining and streamlining the process to apply to encumber the property of a utility. The problem with this solution is that, eventually, liens would attach to the property of utilities. This is contrary to the public interest. If liens can attach to the property of a utility, eventually one of the liens may be foreclosed. When that happens, the property may be sold at auction. This would take property devoted to the public good out of the public domain, therefore harming the public in order to benefit one subcontractor.

A further option would be to do nothing. This is the approach favored by the legal department of Southern California Edison, the defendant utility in *Automatic Sprinkler*. They find that it is to their benefit to allow liens to be filed, because a large number of them are not properly filed and therefore dismissed.⁹¹ The liens that are properly filed (known as "perfected") are paid off by the utility prior to any judicial action.⁹² Southern California Edison believes that this procedure is better than requiring utilities to post bonds as public entities, because such requirements may make some construction projects prohibitively expensive.⁹³ A problem with this approach is that if subcontractors are led to believe that their liens can attach, a utility may one day decide not to pay the liens and argue that the liens should not be allowed to attach under section 851.

The final and soundest alternative would be to declare that public utilities are to be considered "public entities" for the purposes of mechanics' lien law and to require utilities to send to subcontractors notice of their status as public entities.⁹⁴ This solution would require general contractors to post payment bonds whenever they undertake a work of improvement for public utilities.⁹⁵ The law of payment bonds⁹⁶ was enacted to afford a remedy to subcontractors who lose the remedy of

90. See *supra* notes 27-28 and accompanying text.

91. Telephone Interview with Donna Rovero, Counsel to Southern California Edison (Aug. 8, 1990).

92. *Id.*

93. *Id.*

94. Notice should be given in the manner suggested in the text accompanying note 84. The notice requirement is a crucial aspect of this proposal. There is not a notice provision in the payment bond statutes (CAL. CIV. CODE §§ 3247-3252 (Deering 1986)). A reason for this may be that most public entities are readily identifiable as such by their name (eg., The City of San Francisco, UC Hastings), therefore providing constructive notice of their status as public entities. Telephone companies and other utilities often do not have names that denote their status as utilities, so they should give notice.

95. CAL. CIV. CODE §§ 3109-3154 (Deering 1986 & Supp. 1991).

96. *Id.* §§ 3247-3252.

mechanics' liens when they work on a public work.⁹⁷ The remedy of stop notices would remain, but subcontractors would have an additional distinct remedy, an action on the payment bond.⁹⁸

This alternative would clarify the existing law, provide notice of the clarification, and remove utilities from the danger of having their property encumbered and foreclosed upon. It would require general contractors to post a payment bond, which would escalate the cost of construction. Nonetheless, the additional cost would be passed to the utility, who would pass the cost to its customers. The customers would therefore bear the ultimate cost of ensuring that construction undertaken for their benefit is paid for.

IV Conclusion

The problem this note has addressed is the uncertainty caused by the conflict between the mechanics' lien statutes and the California Public Utilities Code. This conflict can have disastrous consequences for subcontractors, who may be left without a remedy to obtain payment for goods or services they have provided.

There are potential remedies, but the best course of action would be to amend section 3099 of the California Civil Code to include public utilities within the definition of "public entities." If utilities were declared "public entities," then any work of improvement they undertook would be considered a public work, and the general contractor would be required to post a payment bond. The contractor would presumably pass this extra cost of construction to the utility, increasing the cost of construction and possibly increasing rates. Yet these are increases the public should bear. California subcontractors should contract freely, secure in the knowledge that the California Civil Code is safeguarding their interests.

97. *California Elec. Supply Co. v. United Pac. Life Ins. Co.*, 38 Cal. Rptr. 479, 482 (Ct. App. 1964).

98. *Globe Indem. Co. v. Hanify*, 20 P.2d 689 (Cal. 1933).

