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Limitation of Owner's Liability for Mechanics' Liens

By JOHN H. BARNARD*

DURING 1962 a committee of attorneys appointed by the State Bar delegates conducted an intensive study of the mechanics' lien laws of California.¹ One of the areas given particular attention was the means by which an owner could protect himself against mechanics' liens in excess of the price he agreed to pay for his work of improvement.

The Law on Limitation of Liability

Apart from some protection given to a landlord, the only section relating to limitation of an owner's liability for mechanics' liens is section 1185.1 of the Code of Civil Procedure.² This section could be clarified, but its fundamental purpose is apparent. It provides that, except as to the contractor, mechanics' liens shall not be limited to the contract price unless the owner files his original contract in the office of the county recorder of the county where the property is situated and causes the contractor to record a payment bond. Today, this section may appear to embody a simple rule of law; but the rule was not so clear in 1911 when the section was enacted in substantially its

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¹ STATE BAR OF CALIFORNIA, FINAL REPORT OF COMMITTEE TO STUDY 1958 CONFERENCE RESOLUTION NO. 70 (dealing with mechanics' lien laws), Sept. 11, 1962 (unpublished report in University of California Law School Library, Berkeley [hereinafter cited as STATE BAR REPORT]).

² "The liens provided for by this chapter shall be direct liens and shall not in the case of any claimants other than the contractor be limited, as to amount, by any contract price agreed upon between the contractor and the owner except as hereinafter provided. Such liens shall not in any case exceed in amount the reasonable value of the labor done or the material furnished, or both, for which the lien is claimed, nor the price agreed upon for the same between the claimant and the person by whom he was employed. Such liens shall not, in any case where the claimant was employed by a contractor or subcontractor, extend to any labor or materials not embraced within or covered by the original contract between the contractor and the owner, or any modification thereof made by or with the consent of such owner, and of which such contract or modification thereof the claimant shall have had actual notice before the performance of such labor or the furnishing of such materials. . . It is the intent and purpose

present form.³ It culminated a battle lasting over fifty years between the California courts and the legislature. Until *Roystone Co. v. Darling*⁴ the courts repeatedly struck down or substantially abridged all efforts of the legislature to provide that mechanics' lien claimants would be paid in full regardless of the price the owner had agreed to pay for his improvement.⁵ In essence the courts' position was that the right to contract was a constitutional right not to be abridged, that mechanics' liens did not exist at common law and are purely a creature of statute, and that legislation which would make the owner liable for more than his contract price was an abridgement of his right to contract and therefore unconstitutional.⁶ The legislature answered these

of this section to limit the owner's liability, in all cases, to the measure of the contract price where he shall have filed or caused to be filed in good faith with his original contract a valid bond with good and sufficient sureties in the amount and upon the conditions as herein provided. It shall be lawful for the owner to protect himself against any failure of the contractor to perform his contract and make full payment for all work done and materials furnished thereunder by exacting such bond or other surety as he may deem necessary." CAL. CODE CIV. PROC. §§ 1185.1(a), (d).

³ Cal. Stat. 1911, ch. 681, § 1, at 1313.

⁴ 171 Cal. 526, 154 Pac. 15 (1915).

⁵ "Prior to the adoption of the constitution of 1879 the lien of mechanics and materialmen for work done and materials furnished in the erection of buildings was entirely a creature of the legislature. The former constitution contained no declaration on the subject. Numerous decisions of the supreme court had declared that all such liens were limited by the contract between the owner and the contractor, and could not, in the aggregate, exceed the contract price. The doctrine that the right of contract could not be invaded by legislative acts purporting to give liens beyond the price fixed in the contract between the owner and the contractor, or regardless of the fact that the price had been wholly or partially paid, was so thoroughly established that litigation involving it had virtually ended. . . . In this condition of the law the constitution of 1879 was adopted." *Id.* at 530, 154 Pac. at 17. See *Dore v. Sellers*, 27 Cal. 588 (1865) (construing Mechanics' Lien Act of 1862); *Bowen v. Aubrey*, 22 Cal. 566 (1863) (construing Mechanics' Lien Act of 1858); *McAlpin v. Duncan*, 16 Cal. 126 (1860) (construing Mechanics' Lien Act of 1858); *Knowles v. Joost*, 13 Cal. 620 (1859) (construing Mechanics' Lien Act of 1856).

⁶ "The provision in the constitution respecting mechanics' liens (art. XX, sec. 15) is subordinate to the Declaration of Rights in the same instrument, which declares (art. I, sec. 1) that all men have the inalienable right of "acquiring, possessing and protecting property," and (in sec. 13) that no person shall be deprived of property "without due process of law." The right of property antedates all constitutions, and the individual's protection in the enjoyment of this right is one of the chief objects of society. He has the right to enjoy his property and improve the same according to his own desires in any way consistent with the rights of others, subject only to the just demands of the state. This right is invaded if he is not at liberty to contract with others respecting the use to which he may subject his property, or the manner in which he may enjoy it. . . . If, after the owner has agreed with the contractor to compensate him with property other than money, they may, with knowledge of the terms of such contract, still enforce a lien upon the building for the value of materials and labor furnished by them to the contractor, the owner would be deprived of his property without due process of law, by being compelled to pay more for the improvement than he had con-

arguments by causing the right to a mechanics' lien to be embodied in article XX, section 15 of the Constitution of 1879.⁷ The courts then concluded that the two constitutional rights were equal and continued to be critical of any legislation that might give a lien claimant an edge over the owner.⁸ The legislature of 1885 took another approach to the problem of obtaining full liability for the owner. Sections 1183 and 1184 of the Code of Civil Procedure were amended so as to regulate the *mode* of the contract between the owner and contractor.⁹ In essence, the contract between the contractor and owner had to comply with certain requirements of a writing, filing, and payment by installments. Compliance with the regulations would result in a lien confined to the unpaid portion of the contract price, while all contracts which were not in such form would be void and would subject the owner

tracted for." *Stimson Mill Co. v. Braun*, 136 Cal. 122, 125-26, 68 Pac. 481, 482 (1902). *Hoffman-Marks v. Spres*, 154 Cal. 111, 97 Pac. 152 (1908); *Latson v. Nelson*, 2 Cal. Unrep. 199 (1883).

⁷ "Mechanics, materialmen, artisans, and laborers of every class shall have a lien upon the property upon which they have bestowed labor or furnished material, for the value of such labor done and material furnished; and the legislature shall provide, by law, for the speedy and efficient enforcement of such liens." CAL. CONST. art XX, § 15.

⁸ *Latson v. Nelson*, 2 Cal. Unrep. 199 (1883), discussed in *Roystone Co. v. Darling*, 171 Cal. 526, 531, 154 Pac. 15, 17 (1915), "In effect, it declared that section 15, article XX, of the constitution was not intended to impair the right to contract respecting property guaranteed by section 1, article I, thereof, and that the provisions of the code purporting to give a lien upon property in favor of third persons, in disregard of and exceeding the obligations of the owner concerning that property, was an invalid restriction of the liberty of contract. Although it is not very clearly stated, the theory of that decision is, and it has always been understood to be, that section 1 of article I, declaring that all men possess "certain alienable rights," among them the right of "acquiring, possessing, and protecting property," is a guaranty which includes the right to contract concerning the use, enjoyment, and disposition of property, and which cannot be taken away or restricted by the legislature, except by reasonable regulations made in the exercise of the police power."

⁹ CAL. STAT. 1885, ch. 152, §§ 1-2, at 142-43, amending CAL. CODE CIV. PROC. §§ 1183, 1184. "The legislature of 1885 . . . apparently recognizing and conceding the force of the decision in *Latson v. Nelson*, undertook to secure and enforce the constitutional lien by other means, that is, by regulating the mode of making and executing contracts, rather than by disregarding the right of contract. It amended sections 1183 and 1184 of the code by providing that in all building contracts, the contract price should be payable in installments . . . , should be in writing, and should be filed in the office of the county recorder before the work was begun thereunder, that if these regulations were followed, liens should be confined to the unpaid portion of the contract price, but that all contracts which did not conform thereto, should be void, that in such case the contractor should be deemed the agent of the owner, and the property should be subject to a lien in favor of any person performing labor or furnishing material to the contractor upon the building for the value of such labor or material. This law, with some amendments remained in force until the enactment of the revision of 1911 . . ." *Roystone Co. v. Darling*, 171 Cal. 526, 532, 154 Pac. 15, 17-18 (1915).

to full liability for all liens. The scheme of regulation embodied in these statutes did not work well, and the superseding act of 1911 was "obviously designed for the purpose of removing, as far as possible, the objections to the former law."¹⁰ This statute, while requiring a writing, filing, and payment by installments, provided further that the owner should obtain security in the form of a bond for the labor and materials furnished to his contractor.¹¹ The court in *Roystone Co.* held that the statute was constitutional. The net result of the decision, which remains the law today, is that the original contract must be filed and a bond must be recorded in order to limit the liability of the owner to the contract price. In the language of the court, section 1185.1

describes two classes of liens. One class consists of liens in cases where the bond has not been filed, in which case, the state of accounts between the owner and the contractor, and even the contract price, are immaterial to the lien, except as to the contractor. The other classes consist of all cases in which the proper bond and contract are duly filed. In the cases, by the express language of the section, the contract price is made to control, and the account of the indebtedness thereon from the owner to the contractor is decisive of the amount of the liens which can be adjudged against the property.¹²

After the *Roystone Co.* decision there are few reported cases on the subject. What had been a turbulent area quieted down and is seldom litigated today. It is submitted that this resulted not so much from the efficacy of the 1911 statutes as from a change in the customs of our community.

Owners Are Not Aware of the Law

In the past a man saved his money, bought his lot, and built his home. He was therefore directly involved with the problem of mechanics' liens. Today, most of us buy completed homes from a subdivider and borrow money to do so. Before the lender puts up this money it makes certain that there is no problem of mechanics'

¹⁰ *Roystone Co. v. Darling*, 171 Cal. 526, 534, 154 Pac. 15, 18 (1915).

¹¹ "The law of 1911 here involved does not deprive the owner of the right to contract for the improvements of his property. It allows him to contract freely for such improvement and upon such terms as he may deem for his best interests. All it exacts from him, as a condition of such exemption from liability, and in order to make his contract effective, is that he shall provide a reasonable security for the constitutional lien given for labor and materials furnished to his contractor. It is not an unreasonable burden. It is one which we think the people have the power to impose, and which we believe to be within the scope of the constitutional mandate in the section conferring such liens, and of the police power." *Id.* at 540, 154 Pac. at 21.

¹² *Id.* at 538, 154 Pac. at 20.

liens. The average home owner is not concerned with, and knows very little of, the concept of mechanics' liens. If this change in custom had completely settled the problem everything would be fine. There is no need to disinter old conflicts for historical interest. But some people still build their own homes, and businessmen still build commercial structures. Their problem, or more accurately, their ignorance, has become more acute. There is no longer any general knowledge in the community of the problems that mechanics' liens can present. In all likelihood the prospective owner is building for the first and only time in his life. His relationship with his contractor is, as it should be, one of trust and confidence. The thought that the contractor might default is not considered. Certainly the owner is not aware that if the contractor defaults he may have to pay more than the contract price. The fact that the statutes do not make the owner personally liable for mechanics' liens makes little difference when the liens start coming. If he wants to protect his property and his investment he has to pay them off.

How Best To Inform Owners of the Law?

The solution to the problem, if one exists, is to find a means to warn the prospective owner of it and the protection afforded by statute. But this is not easily accomplished. In the course of its study of mechanics' lien laws the State Bar Committee contacted, and was contacted by, numerous organizations representing general contractors, special contractors, building material dealers, and lending institutions. However, there was no organization to contact representing the individual owner. There is presently no organization functioning to disseminate information to this particular class. If the owner is to be forewarned it will have to be by increasing the general knowledge of the community or by finding a means to call the law to his attention when he undertakes the project.

One way suggested by the committee was to clarify section 1185.1 in the hope that, being more easily understood, it would become more generally known.¹³ Study along these lines led to the suggestion that the provisions relating to filing the original of the contract would profit by a completely new approach. The purpose of filing the original of the contract is twofold. First, it gives constructive notice to persons furnishing labor or materials that they are not entitled to a lien for anything not required by the contract. Second, it provides a means by

¹³ STATE BAR REPORT 72-85.

which a person desiring to furnish labor or materials may examine the contract to see if the contract price is sufficient.¹⁴ However, the requirement that the original of the contract be filed has produced problems. There is a natural reluctance on the part of owners, and probably their attorneys, to permit the original of such a document to be taken and filed. There is also the problem of determining what documents constitute the original contract. Are plans and specifications part of the original contract?¹⁵ An amendment to the statute to clarify what documents are included within the meaning of the term "original contract," and to provide for its recordation in lieu of filing, would result in voluminous photostating and costly filing fees. Another approach would solve this problem, as well as some others.

The statute could be amended to provide for recording a notice of improvement in lieu of filing the contract. Such a notice should be simple in order to encourage its use. It should provide (1) the name and address of the owner, (2) the name and address of the general contractor, (3) a description of the property, (4) a general description of the nature of the work of improvement, (5) the place where the building contract and any plans and specifications may be examined, (6) the name of the surety on the performance bond, if any, and (7) the name of the building fund lender, if any. The premise is that all of the purposes of filing the original contract can be satisfied by providing for such a notice of improvement instead. It would be the counterpart of a notice of completion, a concept already known.¹⁶ As simplified, and as associated with the notice of completion, it might become more generally known to the public.

In any event, a new approach is needed. For whatever reason, the present means of protection is not being utilized. In the summer of 1964 every county recorder in California was asked whether owners were filing their contracts and performance bonds.¹⁷ All counties responded to the inquiry. In a few counties there is an occasional filing by an owner on a private work, but only when the amount involved is considerable. In most counties none have been filed in recent years. There was a slightly greater incidence of recording payment bonds, but the number was still negligible. Some of the more

¹⁴ Greig v. Riordan, 99 Cal. 316, 319, 33 Pac. 913, 915 (1893).

¹⁵ See Bird v. American Sur. Co., 175 Cal. 625, 629, 166 Pac. 1009, 1011 (1917).

¹⁶ CAL. CODE CIV. PROC. §§ 1192.1(b), 1193.1(c). A notice of completion is a notice filed by the owner which states that the work has been completed. The notice shortens the time within which the various claimants may assert their claims.

¹⁷ Survey made by the author in the summer of 1964.

experienced recorders observed that this condition had remained the same for the last two to three decades.

The reference to the payment bond in the suggested notice of improvement is to call the owner's attention to this part of the statutory requirements to limit his liability. Admittedly it is an indirect way to do this, but at least it puts him on notice that such bonds exist. If a more direct way is to be found it will have to arise as a necessary element of the owner's undertaking the work of improvement. The only element common to all owners who enter a contract for a work of improvement is just that—all will enter a contract. To be certain that owners are informed of the necessary steps to limit their liability to the contract price, such information will have to be in the contract. It has been suggested that such information could be contained in building permits, but building permits are provided for in local ordinances, not State statutes. Moreover, the contractor, as part of his services, frequently takes out the building permit. It has been suggested that the information might be furnished by building and loan institutions. But not every owner must borrow. It has even been suggested that the priority of the loan of the building and loan institution over the claims of mechanics' liens be made to depend upon the institution requiring a payment and performance bond from an owner or contractor. This suggestion is interesting, but whatever merit it has depends upon its being utilized throughout the full scope of the mechanics' lien statutes. Such legislation might solve most of the owner's problems but it would involve fundamental issues and conflicting forces of momentous import. The limited goal here is not to change the law relating to limitation of owner's liability, but to better acquaint the owner with the existing law.

The suggestion that information be imparted to a party through a required form of contract is not new. Information is required to be set forth in certain contracts in other fields, such as retail installment contracts and automobile conditional sales contracts. As to building contracts, the legislature earlier adopted the approach that it could control the form of the contract and did so prior to the enactment of the present section 1185.1.¹⁸ There should be no constitutional problems raised by legislation providing that a building contractor can recover nothing on his contract unless it contains a provision that the owner has been informed that a mechanics' lien claimant is not limited to the contract price unless the owner files a notice of improvement and

¹⁸ *Roystone Co. v. Darling*, 171 Cal. 526, 154 Pac. 15 (1915).

causes the contractor to record a payment bond prior to commencing the work.

Conclusion

The concept that an owner in undertaking a work of improvement can expose himself to liability greatly in excess of his contract price is so unique that few owners realize the dangers involved. On the other hand, it is not logical to assume that the building contractor, the other party to the contract, will voluntarily give such a warning or inform the owner of the means of protection. The only way to give the owner adequate warning is to simplify the means of obtaining protection and require that these means be set forth in the building contract.