



- Recent California Legal Decisions, Legislation, Trends & Developments -

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Legal Decisions

Unlicensed contractor may not offset cost of materials in claim by plaintiff to recoup money paid for unlicensed work. *White v. Cridlebaugh*, 175 Cal. App. 4th 1535 (2009). Where a corporation did not possess an active contractor's license (because its RMO was no longer actively involved), and the plaintiffs were thereby entitled to recover all compensation paid for unlicensed work, plaintiffs' recovery could not be reduced by a claim of offset for materials and services provided in connection with the unlicensed work. The unlicensed contractor not only had to give back all payments received, but could not obtain a credit or offset for the reasonable value of the materials sold. The failure to maintain its license forfeited all offset claims.

General Contractor may be held directly liable to the employees of its unlicensed subcontractors for their unpaid wages and interest. *Sanders Construction Company, Inc. v. Cerda*, 09 C.D.O.S. 8357 (2009). The Court of Appeal ruled that the employees of an unlicensed subcontractor were the general contractor's statutory employees who obligated the general contractor to pay their wages plus interest. Labor Code § 2750.5. This result steepens the already significant penalties for hiring an unlicensed contractor, which now may include payment of the unlicensed subcontractor's employees' wages, worker's compensation liability for the subcontractor's employees, liability to EDD for unpaid contributions and withholding taxes for its unlicensed subcontractor's employees, and potentially waiting time penalties equivalent up to 30 days' wages under Labor Code § 203.

On the specific facts of a case, construction management services company was not considered a “contractor” or required to have a contractor’s license. *Fifth Day, LLC v. Bolotin*, 172 Cal. App. 4th 939 (2009). Fifth Day, LLC provided construction management services to a private owner developing commercial real estate. The owner failed to pay and Fifth Day sued. The owner claimed in defense that because Fifth Day did not hold a valid contractor’s license, Fifth Day could not sue to collect. The trial court granted summary judgment in favor of defendants. The Court of Appeal reversed the judgment. The court concluded that Fifth Day was not a contractor because it neither contracted to perform nor performed any of the activities listed in Bus. & Prof. Code § 7026, which defines “contractor.” The Court keyed on the fact that Fifth Day “had no responsibility or authority to perform any construction work on the project, or to enter into any contract or subcontract for the performance of such work.” Here, the owner entered into a construction contract with a licensed general contractor to perform and or supervise all construction on the project.

Project Manager may potentially claim a mechanic’s lien upon correction and clarification of the project engineer’s design. *Congrove v. Western Mesquite Mines, Inc.*, 2009 U.S. Dist. LEXIS 15584 (2009). The U.S. District Court for the Southern District of California denied an owner’s motion to dismiss project manager’s lien claim, finding that a project manager may be a claimant under the California’s Mechanic’s Lien Act not for a supervisory role, but where his services were consumed or incorporated into the work of improvement. Civil Code § 3110. The Court found issues of fact as to whether plaintiff’s services revising, clarifying, and correcting the engineer’s project design “(go) beyond a mere supervisory role in managing the project and asserts that Plaintiff’s services were actually used on the work of improvement.”

A statute entitling a prevailing party to attorney’s fees in an action to recover progress payments does not apply to an action to recover a final payment. *Murray’s Iron Works, Inc. v. Boyce*, 158 Cal. App. 4th 1279 (2008). Murray’s Iron Works installed decorative ironwork at the home of Phillip Boyce. The contract required the Owner to pay 50% down, with the remainder due after the completion of the project. Murray’s substantially completed its work, and the owner even noted it was “beautiful work.” However, the owner refused to pay the balance of ~\$66,000 because of repairs to water sealant work Murray’s refused to perform when the owner refused to pay. The court affirmed an award of the ~\$66,000 in principal, but reversed an award of 2% penalties and attorney’s fees and costs of \$120,000. The court held that Murray’s was not entitled to penalties or fees because both were based on Civil Code Section 3260.1, which applies only to construction contracts which provide for progress payments. Unfortunately for Murray’s the contract did not contemplate progress payments but rather one 50% payment before work started and one final payment. Because the last payment was a final payment and not a progress payment, Murray’s was not entitled to recover any prompt payment penalties or the \$110,000 in attorney’s fees it expended.

Charter city on public works contract financed solely from city revenues not required to comply with prevailing wage law requirements. *State Bldg. and Const. Trades Council of California, AFL-CIO v. City of Vista*, 173 Cal. App. 4th 567 (2009). The charter city of Vista proceeded with the first of two capital improvement projects and approved design-build contracts for fire stations without including within those contracts provisions required by the Prevailing Wage Law. The labor federation Council sought a writ of mandate against the City and its mayor requiring the City to include prevailing wage

requirements in its contract. The trial court denied the petition and the appellate court affirmed. The Court found that a public works contract financed solely from charter city revenues is a municipal affair over which a city has paramount power under article XI.5.(a) of the California Constitution, and thus was not required to comply with prevailing wage law requirements.

Without an RMO, partnership was deemed an unlicensed contractor that could not substantially comply with the law and thus was required to refund a homeowner money she paid for construction work. *Oceguera v. Cohen*, 172 Cal. App. 4th 783 (2009). The Court of Appeal affirmed the trial court's decision in favor of plaintiff homeowner in a refund action for money paid for construction work on her home because a general partnership and its two partners were unlicensed contractors and did not act in substantial compliance with the license laws. Prior to the partnership's entry into the construction contract, the only RMO had executed a disassociation. The two remaining partners, who knew they were unlicensed when entering into the contract, failed to show substantial compliance. Bus. & Prof. Code § 7031(e). The court observed that the qualification of a partnership for a license required the presence of a licensed general partner or responsible managing employee and that cancellation of a license was automatic upon disassociation of such person. Bus. & Prof. Code §§ 7068(b)(2), 7076(c), 7075.1(a), (b)(2) [the license also could not be transferred]. Thus, the partnership was unlicensed when the work was performed and was subject to disgorge all monies received on the Project.

“No Equitable Indemnity Without Liability.” *Prince v. Pacific Gas & Elec. Co.*, 45 Cal. 4th 1151 (2009). PG&E invoked statutory indemnity (Civ. Code § 846) to a ten-year-old boy's claim for injuries sustained when the boy entered private land and attempted to dislodge a lost kite entangled in electric lines with an aluminum pole. The boy's guardian then sued the property owner. The owner cross-claimed against PG&E as an easement holder with implied obligations to prevent injury to third persons and the landowner. The Supreme Court found that PG&E's statutory immunity to the underlying boy barred the property owner's claim against PG&E of implied contractual indemnity because that type of claim is an equitable liability that presupposes both the purported indemnitor (PG&E) and indemnitee (property owner) were liable to the underlying plaintiff. In sum, PG&E owed no indemnity without possible liability for the underlying claim. The Court allowed the boy to pursue the property owner under an exception to Civ. Code Section 846 because the owner may have invited the boy to enter unto the property.

Ten year statute of limitations on construction defects is not delayed by sale of developed property. *Gundogdu v. King Mai, Inc.*, 171 Cal. App. 4th 310 (2009). A notice of completion for construction was filed in November 2005. The homeowners filed their action against the contractor for negligence and breach of implied warranty, seeking damages for latent construction defects in April 2006. The Court found the action barred by the 10 year statute of limitations. Code of Civ. Proc. § 337.15. The statute of limitations was not made inapplicable by the fact that the developer owned the property for a year and a half after the contractor built it. The Court affirmed that the statute of limitations begins to run *at the date of substantial completion* and is not delayed for any time between completion and sale of the property.

“Willful misconduct” exception to California’s 10 year statute of limitations for construction defects applies to a developer’s indemnity claims against subcontractors. *Pine Terrace Apartments, L.P. v. Windscape, LLC*, 170 Cal. App. 4th 1 (2009). A developer employed numerous subcontractors to build two apartment complexes completed in 1991. In 2003, buyer bought the complexes and discovered defects, including a lack of window flashing. Buyer sued developer, who cross-complained against its subcontractors. The developer and the subcontractors moved for summary judgment based upon the 10 year statute of limitations for latent defects. However, the owner, invoking the “willful misconduct” exception to the statute of limitations, presented expert testimony that the window flashing failure was so obvious the developer must have willfully allowed the defect to remain in the buildings and then concealed that defect from the buyer. The trial court denied the developer’s motion for summary judgment but granted the subcontractors same motion. On appeal, the Court ruled that the “willful misconduct” exception applies to both direct and derivative actions for indemnity. Code of Civ. Proc. § 337.15(f).

A payment bond claimant, in order to prevail on a summary judgment motion, need not disprove affirmative defenses. *Oldcastle Precast, Inc. v. Lumbermens Mutual Casualty Co.*, 170 Cal. App. 4th 554 (2009). Oldcastle was a supplier to a subcontractor on a project to build a county jail, who was underpaid \$148,530. During performance however, a release stating that Oldcastle was

owed nothing was mistakenly created and then rescinded. Despite rescission, the subcontractor passed the \$0 release on to the contractor. Following reversal of a jury verdict for the contractor on the \$0 release, Oldcastle moved for summary judgment on its payment bond claim on the undisputed material facts of its public works sub-subcontract, the provision of materials, lack of payment, existence of the payment bond, and compliance with notice requirements. The sureties argued Oldcastle’s motion for judgment could not be granted because Oldcastle had failed to establish facts *negating* the affirmative defenses related to the \$0 release, release and estoppels. The court granted the summary judgment motion and the Court of Appeal affirmed, ruling that a bond claimant, in order to prevail on a summary judgment motion, need not disprove affirmative defenses, citing to Cal. Code of Civil Proc. § 473c.

Jury award for plaintiffs who filed a negligent recommendation claim related to a construction project. *Dinstell v. Black Diamond Landscape and Design*, Contra Costa Co. Superior Court No. CIVMSC08-00267 (**unpublished** 2009). Plaintiffs asked Basalite Concrete Products for companies experienced in installing BCP’s interlocking concrete blocks for use in retaining walls. BCP suggested Black Diamond Landscape. Black Diamond built retaining walls for Plaintiffs that ultimately failed. Plaintiffs sued BCP claiming it negligently recommended Black Diamond. The jury awarded \$519,000 in damages to Plaintiffs.

Pending and Recently Enacted Legislation

Effective 2011, Contractors Must Send A Notice of Mechanic's Lien to Property Owners Prior To Recording A Lien.

Assembly Bill 457 (Monning) Chaptered. This new law, effective January 1, 2011, amends Sections 3084 and 3146 of the Civil Code to require contractors to serve a "Notice of Mechanic's Lien", containing certain specific information regarding the legal effect of the lien, via registered or certified mail, on the owner or reputed owner of the property, or on the construction lender or the original contractor if those parties cannot be served. The proof of service affidavit showing completed service of the "Notice of Mechanic's Lien" must be included in the recorded lien. Failure to serve the "Notice of Mechanic's Lien" or the mechanic's lien would cause the lien to be unenforceable as a matter of law.

New Civil Code Sections Regarding OCIP Disclosure Requirements for Residential Projects.

Civ. Code Section 2782.9. The Legislature added Section 2782.9 to the Civil Code, which provides that residential construction contracts entered into after January 1, 2009, on which a wrap-up insurance policy is applicable and which require a participating subcontractor or other participant to indemnify, hold harmless or defend another for a claim or action covered by the program and arising out of the project, are unenforceable. Under this section, builders or general contractors are not prohibited from requiring a reasonably allocated contribution from subcontractors or other participants to a self-insured retention or deductible required under the wrap-up policy or consolidated insurance program, so long as the maximum amount and method of collection of the participant's contribution is disclosed in the contract and is reasonably limited so that each participant has some financial obligation in the

event of a claim alleged to be caused by that participant's work. Such contribution is to be collected when any such SIR or deductible is incurred and in an amount bearing a reasonable and proportionate relationship to the alleged liability arising from the claims allegedly caused by the participant's scope of work when viewed in the context of the entirety of claims.

Civ. Code Section 2782.95. This section requires that the owner, builder or general contractor obtaining a wrap-up policy or other consolidated insurance program must disclose the total amount or method of calculation of any credit or compensation for premium required from a subcontractor or participant for the wrap-up policy in the contract documents.

Civ. Code Section 2782.96. If an owner, builder or general contractor obtains a wrap-up policy or other consolidated insurance program for a public work or any other project other than residential construction that is put out for bid after January 1, 2009, the total amount or method of calculation of any credit or compensation for premium required from the subcontractor or other participant must be clearly delineated in the bid documents. Specific information regarding the policy must also be disclosed.

Indemnity for Construction Defect Claims on Residential Projects. In order to close certain loopholes, effective January 1, 2009 the California Legislature again amended Civil Code section 2782 in an attempt to limit the applicability of Type I indemnity for construction defects claims in residential construction projects. The statute now invalidates clauses that would require subcontractors to indemnify a builder, developer, general contractor, contractors, and others as specifically described, against liability for construction defect claims on residential

projects to the extent that such claims arise out of, pertain to, or relate to the negligence of such indemnitee. In light of this change, each party will be held liable for its respective share of fault. If an indemnitee tenders a claim to a subcontractor, the subcontractor must, within specified deadlines, agree to defend the claim except to the extent it results from the scope of work, actions, or omissions of the indemnitee or any other party. Or, the subcontractor may elect to pay "on an ongoing basis" during the pendency of the claim "no more than a reasonable allocated share" of the indemnitee's defense fees and costs. Such payments are subject to later reallocation, and all parties' rights to seek equitable indemnity are preserved. In the event the subcontractor fails to honor its defense obligations, the indemnitee may pursue a claim against the subcontractor for any resulting compensatory damages, consequential damages, reasonable attorney's fees, and interest on defense and indemnity

costs incurred. The subcontractor has a right of reallocation upon resolution of the claim. If the indemnitee wrongfully fails to reallocate defense fees to subcontractors within 30 days after final resolution of the claim, the subcontractor may pursue a claim against the indemnitee for any resulting compensatory and consequential damages and interest thereon. The amendment does not affect the law governing an insurer's duty to provide an immediate defense for uncovered as well as covered claims. The statute does not apply to bodily injury or wrongful death claims.

Pending Senate Bill 629 Would Cap Retention at 5%. Senate Bill 629 (Liu) would cap retention amounts at five percent (5%) on all private projects unless the general contractor asks for performance and payment bonds in the solicitation for bid and the subcontractor fails to provide the bonds requested.

Trends and Developments: Valid License Refresher

Given the impact of the decision in Sanders Construction Company, Inc. (GC must pay unlicensed Sub's employees wages and interest) and other recent case decisions involving licensing discussed above, the time is ripe for a refresher on the consequences of unlicensed contractor work in California.

Labor's Lost: The Consequences of Performing Contractor Work in California Without A License

Imagine contributing hundreds of thousands of dollars worth of time, labor and materials to a construction project and not being able to obtain payment for that work. Now imagine having no legal recourse to recover your damages. In California, an unsuspecting contractor may find itself in this nightmarish

situation by simply failing to strictly adhere to the licensing laws at all times.

To recover for any unpaid monies due for contractor work in California, a contractor must be able to prove that it was licensed *at all times* during the construction of the project. Bus & Prof. Code § 7031. Under California law, the definition of a "contractor" is sweepingly expansive, and applies to:

. . . any person who undertakes to or offers to undertake to, or purports to have the capacity to undertake to, or submits a bid to, or does himself or herself by or by or through others, construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish any building, highway,

road parking facility, railroad, excavation, **or other structure, project, development, or improvement, or to do any part thereof**, including the erection of scaffolding or other structures or works in connection therewith, or the cleaning of grounds or structures in connection therewith, or the preparation and removal of roadway construction zones, lane closures, flagging, or traffic diversions, or the installation, repair, maintenance, or calibration of monitoring equipment for underground storage tanks, and whether or not the performance of work herein described involves the addition to, or fabrication into, any structure, project, development or improvement herein described of any material or article of merchandise. "Contractor" includes subcontractor and specialty contractor.

Bus. & Prof. Code §§ 7031, 7026.

Therefore, any person or entity working on a construction project, residential or commercial, public or private, must have a contractor's license during all phases of construction for doing any type of the foregoing construction work, even if the work is as minor as "the cleaning of grounds" or "the erection of scaffolding."

Without a license, one who provides construction work may be unpaid by the owner and have no legal recourse for obtaining payment. The law is strictly enforced even if the contractor was only unlicensed for a portion of the time (including just one day of license lapse) it provided the contractor work, or even if the work provided seems relatively minor.

Two cases illustrate the gravity of lacking a license while performing contractor work. In *Hydrotech Systems Ltd. v. Oasis Water Park*, 52 Cal. 3d 988 (1991), Hydrotech produced and

installed machinery that created simulated ocean waves. Wessman Construction Company, a general contractor, contracted with Hydrotech to design and build a surfing pool at a water park. Hydrotech sued Wessman for \$110,000.00, alleging that it only wanted to supply the equipment without constructing the surfing pool, and that the owner and Wessman promised to have a contractor provide any ancillary construction work, but broke that promise. Despite these allegations, the court found Hydrotech could not recover for breach of contract because it failed to allege it had a valid contractor's license. The court also dismissed Hydrotech's other claims, including Wessman's and the owner's fraud in inducing Hydrotech into the contract, because Hydrotech was unlicensed.

Similarly, in *Great West Contractors, Inc. v. WSS Industrial Construction, Inc.*, 162 Cal. App. 4th 581 (2008), a subcontractor sued a general contractor to recover monies due under a construction contract. WSS, the steel subcontractor, was not licensed during the time it submitted shop drawings and provided anchor bolts to the project. The court found that a license was required to perform these limited acts because preparing shop drawings and ordering and providing supplies constituted contractor work. The court also found that WSS could not recover for any of the work it provided, even the work it provided *after* it obtained a license, because all of the acts were integral to the contract and could not be segregated.

Not only may an unlicensed contractor be unable to recover money for work it performed, but an unlicensed contractor may face a number of other penalties, including misdemeanor charges, per diem fines, and losing a public contract bid, if it is not properly licensed. Bus. & Prof. Code §§ 7208, 7028.15(a), Cal. Lab. Code §§ 1020 – 1024.

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Although limited exemptions from the licensing requirements apply to certain parties, including material suppliers not performing contractor work, (Bus & Prof. Code § 7052), laborers working for wages, (Bus & Prof. Code § 753), and owner/builders working on their own homes, (Bus. & Prof. Code § 7044), any person planning on performing contractor work should become properly licensed under

California requirements before conducting any type of contractor work.

For more information on licensing information, see the California Contractors State License Board at <http://www.cslb.ca.gov> or contact Leonidou & Rosin, P.C.

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