

CONSTRUCTION LAW

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CONTRACTOR LICENSING REQUIREMENTS AND MONETARY EFFECT OF FAILURE TO MEET SAME

By Bradley A. Post

In *MW Erectors, Inc. v. Niederhauser Ornamental & Metal Works Co., Inc.* (2005) 36 Cal.4th 412, the Supreme Court held that a contractor's failure to comply with the licensure requirements of the Contractors State License Board will result in that contractor being unable to maintain any legal action to recover compensation for any work it performed, even if the contractor receives or renews its license shortly after the work commences. This is true no matter how harsh or unfair the result.

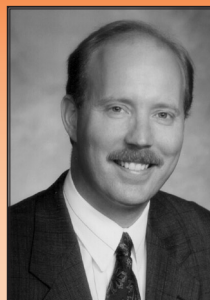
The Supreme Court based its ruling on Section 7031(a) of the Business and Professions Code which bars a contractor from suing to recover compensation for *any* work performed under an agreement for services which requires a contractor license unless proper licensure was in place *at all times* during such contractual performance. The statutory exception for substantial compliance is not available to a contractor who had not been duly licensed for some time *before beginning performance* under the contract. However, if fully licensed at all times during contractual performance, a contractor is *not* barred from recovering compensation for the work solely because he was unlicensed when the contract was *signed*.

Generally The Contractors Licensing Law Does Not Allow A Contractor, Who Is Not In Compliance With Licensing Requirements, To Use The Courts To Recover For Work He Performs

Premised upon its stated motivation to protect the public from unlicensed contractors, the Contractors State License Law imposes strict and harsh penalties for a contractor's failure to obtain and/or maintain proper licensure. By statute, a contractor may not maintain any action to recover compensation for "the performance of any act or contract" unless duly licensed "at all times during the performance of that act or contract." (Bus. & Prof. Code § 7031, subd. (a) (section 7031(a)).

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Bradley A. Post



Bradley A. Post is the Managing Partner in the Modesto office of Borton Petrini LLP. Brad received his undergraduate degree from University of the Pacific in 1981. He attended McGeorge School of Law, obtaining his J.D. in 1986 and was admitted to the bar the same year. Brad is a specialist in cases dealing with wrongful termination, sexual harassment, civil rights violations, public entity law, products liability, premises liability, construction defect, agricultural litigation, and business litigation.

NEW LEGISLATION REQUIRES BUILDERS TO UPDATE THEIR SUBCONTRACTS

By Calvin R. Stead

Prior to January 1, 2006, California law provides that agreements affecting any construction contract that purports to indemnify a builder (or general contractor) against liability for damages for death or bodily injury to persons, injury to property, or any other loss, damage, or expense arising from the sole negligence or willful misconduct of the builder or the builder's agents, servants, or independent contractors who are directly responsible to the builder, or for defects in design furnished by those persons, are against public policy and are void and unenforceable.

A new law passed in 2005, and signed by Governor Schwarzenegger on September 29, 2005, AB758 provides that, all agreements affecting any residential construction contract and amendments thereto entered into after January 1, 2006, that purport to indemnify the builder by a subcontractor against liability for claims of construction defects or other injury to property arising from, pertaining to, or relating to the negligence of the builder or the builder's other agents, servants, or independent contractors who are directly responsible to the builder, or for defects in design furnished by those persons, or for claims that are unrelated to the scope of work in the agreement, are unenforceable.

The relevant portions of the new law read as follows:

"For all construction contracts, and amendments thereto, entered into after January 1, 2006, for residential construction . . . , all provisions, clauses, covenants, and agreements contained in, collateral to, or affecting any such construction contract, and amendments thereto, that purport to indemnify, including the cost to defend, the builder, as defined in Section 911, by a subcontractor against liability for claims of construction defects are unenforceable to the extent the claims arise out of, pertain to, or relate to the negligence of the builder of the builder's other agents, other servants, or other independent contractors who are directly responsible to the builder, or for defects in design furnished by those persons, or to the extent the claims do not arise out of, pertain to, or relate to the scope of work in the written agreement between the parties. This section shall not be waived or modified by contractual agreement, act, or omission of the parties. Contractual provisions, clauses, covenants, or agreements not expressly prohibited herein are reserved to the agreement of the parties."

AB 758 does not prohibit a subcontractor and builder from mutually agreeing to the timing or immediacy of the defense and provisions for reimbursement of defense fees and costs, so long as that agreement, upon final resolution of the claims, does not waive or modify the provisions above.

WHAT IT MEANS

A subcontract agreement from the builder's perspective is a means of shifting the risk of loss associated with construction-related claims, which may arise out of the work of a particular

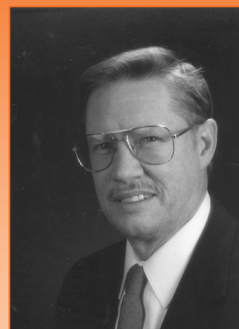
subcontractor. These claims primarily take the form of construction defect and personal injury claims. Since the builder is retaining subcontractors to perform specific aspects in the actual construction, it is appropriate that the subcontractor should bear the risk of loss associated with his work, and should insulate the builder in the process. The best way to accomplish the transfer of this risk is through the subcontract agreement. One of the primary vehicles to be used in this regard is the indemnity provisions in the subcontract agreement.

California's AB758 applies to any "builder," which is defined as a builder, developer, general contractor, contractor or original seller, who was in the business of selling the subject property. "Builder" does not include the general contractor or contractor who is not a partner, member, or a subsidiary of the builder selling the subject property. As such, AB758 does not apply to "non-affiliated" general contractors and contractors.

Because of this distinction between builder affiliated and non-affiliated contractors, your subcontract agreements now need to provide for two different types of indemnity clauses. If you are a builder under the definition of ABC758, in other words affiliated in some way with the actual sale of the property, you will need to use two indemnity provisions in your subcontracts. One indemnity provision is for construction defect claims, the other is for non-construction defect claims. If you are a "non-affiliated" contractor or general contractor who retains subcontractors, you only need to use one indemnity provision, which agrees with the prior law as it existed before AB758 came into effect.

Because of the complexity of these new provisions, we urge anyone attempting to revise their contracts to contact a lawyer competent in this area to make sure that all of your contract documents are revised appropriately.

Calvin R. Stead



Calvin R. Stead is a partner in the Bakersfield office of Borton Petrini LLP. Cal's areas of legal expertise include construction defects, realtor errors and omissions, commercial and environmental litigation, land use planning, oil field litigation and toxic tort litigation. Cal has represented builders, developers and sub-contractors on a wide variety of construction issues,

including grading, soils, foundation, asphalt, concrete, flat work, tile, framing, floor coverings, roofing, masonry and stucco. Within the area of toxic torts, he has handled a vast array of cases, including toxic molds, vaccine reactions, asbestosis, cancer phobia, chemically induced asthma, pesticide and herbicide contamination, EMF, and AIDS contamination and phobia claims.

Contractor Licensing Requirements And Monetary Effect Of Failure To Meet Same
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Some earlier court decisions had softened the severity of this law by allowing contractors, who were technically unlicensed at the time of performance, to show they had substantially complied with the licensure requirements. However, the law has since limited the availability of the substantial compliance exception: “substantial compliance shall not apply” unless the contractor “had been duly licensed as a contractor in this state prior to the performance of the act or contract” for which licensure was required. [§ 7031, subd.(e)].

The Latest California Supreme Court Decision Demonstrates The Harsh Penalties Which Result From A Contractor’s Failure To Comply With Licensing Requirements.

In *Mw Erectors, Inc. v. Niederhauser Ornamental and Metal Works Company, Inc.*, the Disney Corporation constructed a hotel, with Turner Construction as the general contractor. Turner contracted with defendant Niederhauser Ornamental and Metal Works to perform specialized metal work on the project. Niederhauser, awarded two subcontracts to MW Erectors. On October 11, 1999, Niederhauser and MW signed a contract for MW’s performance of “structural” steel work. On or about November 12, 1999, the same parties entered a second contract for MW’s performance of “ornamental” steel work.

MW began work under the structural contract on December 3, 1999, but did not obtain a C-51 structural steel contractor license until December 21, 1999. Work on the ornamental contract began in early January 2000. MW subsequently sued Niederhauser, seeking alleged amounts due of \$955,553.00, for work under the structural contract and \$366,694.00, for work under the ornamental contract.

Niederhauser moved for summary judgment, alleging that MW’s claim was barred under Section 7031(a), because MW had not been properly licensed at all times during the performance of its contracts. Niederhauser also claimed that MW could not demonstrate its substantial compliance with the C-51 license requirement because it had never held a California contractor license before beginning work under the contracts in December 1999. MW admitted that it needed a C-51 license for its work under both contracts, and that this license was not technically in place when MW began work on the structural contract. MW also claimed that it was in substantial compliance with the C-51 license requirement at all times during its performance of both contracts.

The trial court granted summary judgment for Niederhauser and dismissed MW’s action. The Court of Appeal for the Fourth Appellate District reversed the Superior Court’s decision. Niederhauser subsequently petitioned the California Supreme Court for review.

In short, the Supreme Court ruled almost entirely against MW (the so-called unlicensed contractor.) Specifically, the Court ruled that MW was not duly licensed “at all times” during performance of the structural contract, and could not establish its substantial compliance with the licensure requirements in that it had never held a valid California contractor license “prior to” beginning its performance under the “structural” contract. As such, MW could not sue to recover any compensation for work performed under that contract.

In order to establish substantial compliance the contractor must: (1) be duly licensed prior to performance; (2) have acted reasonably and in good faith to maintain proper licensure; (3) have not known or reasonably should not have known that he was not duly licensed when the contract was signed; and (4) acted promptly and in good faith to reinstate his or her license upon learning it was invalid.

An Agreement Or Contract Entered Into By An Unlicensed Contractor May Remain Valid.

Niederhauser also claimed that MW had no valid California contractor’s license when it signed the ornamental contract and urges that an agreement for work requiring a contractor license is illegal, void, and unenforceable from the outset if the contractor was unlicensed at the time the agreement was signed. However, the Supreme Court ruled that MW may recover compensation under a contract for work requiring a license if he or she satisfied licensure requirements at all times while *performing* the work under the contract, even if he or she was not licensed when the agreement was *signed*. As to the “ornamental” contract, MW’s license was obtained before beginning its performance under the contract and, as such, MW could sue Niederhauser for all money owed MW under the contract.

“. . .an agreement for work requiring a contractor license is illegal, void and unenforceable from the onset if the contractor was unlicensed at the time the agreement was signed.”

Practical Considerations

If you are a licensed contractor in California make sure your license is valid and up-to-date.

If for some reason your license becomes invalid at some point take appropriate steps to correct the situation immediately. In addition, take special care with respect to the execution of contracts or actual work performed while your license is invalid.

For entities doing business with Contractors, confirm the license status of those individuals or entities with whom you do business or with whom you enter into agreements. Much of this information is readily available from the Contractors State License Board web-site.

If you are involved or become involved in litigation with an entity that requires a contractor’s license, check on the status of that license because an invalid license will offer you some aggressive avenues in your defense or prosecution of actions involving unlicensed contractors.

DISCLAIMER: THE INFORMATION PROVIDED IN THIS UPDATE IS NOT A SUBSTITUTE FOR LEGAL ADVICE. READERS SHOULD BE ADVISED THAT IF THEY HAVE QUESTIONS ABOUT THIS OR ANY OTHER AREA OF CONSTRUCTION LAW, THEY SHOULD SEEK THE ADVICE OF COMPETENT COUNSEL SPECIALIZING IN CONSTRUCTION LAW.



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