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Under California Law, Unlicensed Contractors Work for Free. But What About Their Employees?

Under California law, unlicensed contractors work for free. To be sure, California code prohibits an unlicensed contractor from making a claim for compensation if the

Employees of an unlicensed subcontractor may assert a wage claim against the general contractor.

contractor is unlicensed at any time during construction of the project (Business and Professions Code Section 7031). But what about employees of an unlicensed subcontractor? In a recent case, California's courts added wages of a subcontractor's employees to the list of items that a general contractor is liable for when engaging an unlicensed subcontractor (workers' compensation, unpaid contributions to the Employment Development Department and tax withholdings also make the list). Thus, employees of unlicensed subcontractors may make claims against general contractors for unpaid wages.

In *Sanders Construction Company, Inc., v. Martin Cerda* (2009 DJDAR 9714), Sanders, the general contractor, hired a subcontractor in June 2006 to install drywall in connection with the construction of a hotel. Sanders paid the subcontractor through September 2006, when a dispute arose over payment and the quality of the subcontractor's work. The unlicensed subcontractor informed its employees that they would be paid directly by Sanders and continued to perform work on the project until January 2007. However, the subcontract at issue was based on a contract price that included labor and materials. Sanders discovered, prior to completion of the work, that the subcontractor's license had expired. The court applied the interpretation of Labor Code Section 2750.5 set forth in *Hunt Building Corp. v. Bermick* (79 Cal.App.4th 213, 2000), which provides that "a general contractor is the employer of . . . those employed by the unlicensed subcontractors." Under such an interpretation, the employees of the unlicensed contractor are deemed to be statutory employees of the general contractor, despite the fact that a general contractor has no right to control hours or rates of pay of said employees.

In rendering its decision, the court relied on Labor Code Section 2750.5 and Business and Professions Code Section 7053 to distinguish employees from independent contractors, and concluded that Business and Professions Code Section 7031 (the "unlicensed contractors work for free" statute) is not applicable to a person who: (1) receives wages as his or her sole compensation, (2) does not engage in an independent business and (3) cannot control how the work is performed. Accordingly, such employees are not independent contractors and may bring an action for unpaid wages against the general contractor, as the statutory employees of said

general contractor.

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Sanders is a critical reminder that general contractors should review policies, procedures and subcontract agreements to ensure that (1) all subcontractors obtain and maintain a valid contractor's license at all times during construction of its projects and (2) all subcontracts contain indemnity and/or similar provisions protecting the general contractor against all liability resulting from a subcontractor's failure to be properly licensed. General contractors should also carefully consider all possible liabilities and options upon learning that a subcontractor was not properly licensed during a project, including any potential liability to the general contractor for payment of such subcontractor's employees' wages and the general contractor's ability to recover any resulting damages from the subcontractor under its subcontract agreement.

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