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## When Do Real Estate Agents Become Contractors?

### THIS ISSUE

Often in the sale of real property, money is held back in the transaction to be used to complete certain repairs to the home. If the real estate agent takes charge of organizing the repairs and paying the contractors, does the agent become a contractor herself?

### BACKGROUND

We are seeing more and more frequently that the sale of residential real property will involve repairs the seller wants completed as part of the transaction. In a “buyer’s market” this is much more common, when buyers are unwilling to take the properties “as is.”

Money may be withheld with permissions from the seller, either left in escrow or paid to one of the agents in the transaction, to be paid to contractors to complete the work.

The work may be something simple, such as replacing an old water heater or radiant heating boiler, or complex such as repairing termite-damaged and dry rot wood throughout the home. Most typically, though, the buyer’s wish list amounts to something akin to a punch list: painting an unpainted door, replacing screens, fixing a broken toilet or connecting the refrigerator’s ice maker. These are often “handyman” items that amount to a few thousand dollars at most.

In her zeal to represent her clients, a real estate agent may be tempted to “direct traffic,” calling upon her lengthy list of connections – the handyman, painter, termite repairman, and radiant-heat specialist to perform the works of improvement on a home.

## WHAT IS A CONTRACTOR?

The California Contractor License Laws define a “contractor” as one who undertakes to or offers to undertake to or submits a bid, either by himself or through others, to “construct, alter, repair, add to, subtract from, improve, move, wreck or demolish any building ... or to do any part thereof.”

Anyone, including a real estate agent, who hires a contractor to perform some work of improvement on someone else’s property and pays the contractor either directly or by authorizing release of funds from escrow, may be acting as a General Contractor under the California Contractor License Laws. This is true, even if those hired to perform the work were themselves licensed contractors.

Thus a helpful real estate agent who organizes the various contractors, ensures that the work is done timely and in a competent manner, and pays the contractors out of escrow or from the agent’s own trust account, may find that she unintentionally acted as an unlicensed contractor.

## WHY IS THIS IMPORTANT?

In California, unlicensed contractors are not entitled to payment for any work for which a contractor’s license was required. In our fact scenario the agent is probably not looking for payment for acting as a contractor.

But what about the fee for acting as a real estate agent? Does a real estate agent’s fee get wrapped into “any act or contract” for which a contractor’s license is required? California courts have held that if a contractor was unlicensed for any portion of a job for which a license was required, he cannot collect for the entire job. In other words, if a court were to find that a real estate agent acted as a contractor as part of the real estate agency contract, the court *could* order that the agent is not entitled to collect any part of the money owed under that contract.

Adding to the potential woes of someone acting as an unlicensed contractor is the fact that, under California law, an unlicensed contractor must return all money paid in connection with the unlicensed work. That even includes money that has been paid out to others, used to purchase materials, and even, as in our scenario above, used to pay for perfectly completed construction work on the home.

Thus, the unlicensed contractor must return money that has already been spent – even if that money was used to improve the home, and even if the homeowner knew perfectly well at all times that the real estate agent was not a licensed contractor! Having already paid out the money, the real estate agent in our scenario above might find that she has to reimburse this money out of her own pocket, with no equitable offset for the improvement in value to the home.

## WHAT ABOUT FAIRNESS?

Let’s face it. This is simply unfair. The homeowner derives the benefit of all of the home repairs *and* is entitled to reimbursement from the “unlicensed contractor” who performed the work. The outrage against this result is completely justified. But the California Supreme Court has held that the unfairness to unlicensed contractors is outweighed by the public policy that protects against unlicensed contracting in California.

In two recent decisions, referred to as “*Hydrotech*” and “*MW Erectors*” the Supreme Court has confirmed that a contractor who is not licensed, or whose license is suspended, forfeits his or her right to enforce a contract and recover compensation, and must disgorge money previously paid. So strong is this policy that it applies without regard to the equities of the circumstances.

The Supreme Court in *Hydrotech* explained without qualification that “detering unlicensed persons from engaging in the contracting business outweighs any harshness between the parties.” The purpose of this: “to protect the public.”

And according to the Supreme Court’s holding in *MW Erectors*, if the contractor was unlicensed for *any portion* of the act or contract for which a license was required, the contractor is prohibited from recovering for *all portions* of the contract. In overruling the Court of Appeal on this issue, the Supreme Court held that when MW Erectors was unlicensed for only a small portion of a much larger job (18 days of unlicensed status on a job lasting about one year), it was thus not licensed for the “act or contract,” and was precluded from recovery of any portion of its contract.

As the Court put it: “The words ‘*at all times*’ convey the Legislature’s obvious intent to impose a stiff all-or-nothing penalty for unlicensed work by specifying that a contractor is barred from all recovery for such an ‘act or contract’ if unlicensed at any time while performing it. In the MW Erector’s case, the plaintiff’s failure to have a specialty license for structural steel for the *first 18 days* of a year-long job precluded it from recovering over \$1 million – including all of its costs incurred, labor, materials incorporated into the project, and profits, even though it had paid much of this money out to others.

Anyone acting as an unlicensed contractor in California will not get the benefit of an “equity” argument, and, when faced with a lawsuit seeking reimbursement of all money paid to the unlicensed contractor, cannot protest that it is unfair, even if, as in the scenario above, the person didn’t really intend to act as an unlicensed contractor.

Moreover, acting as an unlicensed contractor carries with it potential criminal penalties – fines up to \$10,000 and even potential jail time for a misdemeanor conviction. While being prosecuted for this kind of work may be unlikely under the factual scenario above, it is still possible, and expressly authorized by statute.

### HOW CAN THIS BE SAFELY HANDLED?

A real estate agent can safely assist in obtaining quality construction work for a client by simply referring the client to a licensed contractor to do the work. The homeowner should contract directly with the contractor, and the agent should not be involved in either “lining up the subs” or paying the contractor. The desire to help out by being the intermediary between the homeowner and the contractor subjects a real estate agent to potential losses far outweighing any benefit.

### CONCLUSION

This column is not intended to say that every real estate agent who helps find a quality contractor during a real estate transaction is necessarily acting as a contractor. But a careless agent who oversteps the bounds of that agency may find herself named in a lawsuit. Claims have been made against real estate agents on this very issue, resulting in serious and unanticipated losses for the agents involved as well as their brokers. Merely being aware of this potential issue can help a real estate agent avoid serious potential consequences.

### NEXT ISSUE

California’s Solar Rights and Shade Control Acts.

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