

1-1958

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### Recommended Citation

George C. Shelton Jr., *Contracts: Interpretation of Statute Barring Action of Unlicensed Contractor*, 10 HASTINGS L.J. 89 (1958).

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# NOTES

## CONTRACTS: INTERPRETATION OF STATUTE BARRING ACTION OF UNLICENSED CONTRACTOR

In the recent California case of *Lewis & Queen v. N. M. Ball Sons*<sup>1</sup> the Supreme Court of California decided that when an unlicensed subcontractor performs services for a general contractor and the general contractor receives payment for the work, the subcontractor cannot maintain any action against him to recover compensation for his services.

The essential facts in the case were as follows: plaintiffs George W. Lewis and Paul C. Queen were engaged in the contracting business as the partnership of Lewis and Queen. Lewis had an individual license but neither Queen nor the partnership of Lewis and Queen had licenses as required by sections 7028<sup>2</sup> and 7029<sup>3</sup> of the Business and Professions Code. Defendant Ball Sons was also a partnership engaged in the business of general contracting. In June, 1949, defendant was awarded two contracts by the state for the construction of a section of the Hollywood Parkway. Defendant then entered into contracts with the plaintiff whereby the latter would perform part of the work and rent equipment to the defendant.

After performance of the contracts the plaintiff brought an action against the defendant for damages for breach of equipment rental agreements and for the reasonable value of equipment alleged to have been held beyond the agreed rental term.

The Supreme Court, in applying the general rule that courts will not aid in the enforcement of an illegal contract, upheld the trial court's ruling that section 7031<sup>4</sup> of the Business and Professions Code barred plaintiff's action. The court stated:<sup>5</sup>

The reason for this refusal is not that the courts are unaware of possible injustice between the parties, and that the defendant may be left in possession of some benefit he should in good conscience turn over to the plaintiff, but that this consideration is outweighed by the importance of deterring illegal conduct.

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<sup>1</sup> 48 Cal. 2d 141, 308 P.2d 713 (1957).

<sup>2</sup> CAL. BUS. & PROF. CODE § 7028:

"*Engaging in business without a license.* It is unlawful for any person to engage in the business or act in the capacity of a contractor within this State without having a license therefore, unless such person is particularly exempted from the provisions of this chapter."

<sup>3</sup> CAL. BUS. & PROF. CODE § 7029:

"*Acting in joint venture or combination without additional license therefor.* It is unlawful for any two or more licensees, each of whom has been issued a license to engage separately in the business or to act separately in the capacity of a contractor within this State without first having secured an additional license for action in the capacity of such a joint venture or combination in accordance with the provision of this chapter as provided for an individual, co-partnership or corporation."

<sup>4</sup> CAL. BUS. & PROF. CODE § 7031:

"*Allegation and proof of license in action on contract.* No person engaged in the business or acting in the capacity of a contractor may bring or maintain any action in any court of this State for the collection of compensation for the performance of any act or contract for which a license is required by this chapter without alleging and proving that he was a duly licensed contractor at all times during the performance of such act or contract."

<sup>5</sup> 48 Cal. 2d at 150, 308 P.2d at 719.

In support of the above rule, the court cited as precedents a number of cases<sup>6</sup> which seem to be distinguishable on their facts. The court continued:<sup>7</sup>

In each such case, how the aims of policy can best be achieved depends on the kind of illegality and the particular facts involved. [Citations omitted.] But we are not free to weigh these considerations in the present case.

The court went on to say that section 7031 of the Business and Professions Code precluded them from weighing the aforesaid considerations, and applied section 7031 literally.

However, the court was by no means *bound* to interpret section 7031 so as to bar plaintiff's action. In fact, the California courts no longer interpret that statute so as to "leave the defendant in possession of some benefit he should in good conscience turn over to the plaintiff."

In *Norwood v. Judd*,<sup>8</sup> plaintiff and defendant had formed a partnership to conduct a contracting business. Defendant was a duly licensed contractor. However, neither the plaintiff nor the partnership had a license. The plaintiff brought an action to recover his share of the business proceeds from his partner. Recovery was allowed, the court declaring:<sup>9</sup>

It must be remembered that these licensing statutes are passed primarily for the protection and safety of the public. They are not passed for the benefit of a greedy partner who seeks to keep for himself all of the fruits of the partnership enterprise to the exclusion of another partner entitled to share therein. Where the illegal transaction has been terminated, public policy is not protected or served by denying one partner relief against another.

In the *Lewis & Queen* case the court attempts to distinguish the *Norwood* case on the ground that that case involved one partner suing another partner. Also that since the enterprise was not an illegal one as such but only for want of a license, and since the defendant was not a third person for whose protection the statute had primarily been passed, the plaintiff could recover. There the court recognized an exception to section 7031 for the purpose of attaining a just result. Why then should the court in the instant case not read an obvious exception in the statute to avoid that which the court itself admittedly considers to be an unjust result?

Another case in which the statute was not applied so as to bar a recovery was *Gatti v. Highland Park Builders, Inc.*<sup>10</sup> There an action was brought by two partners against a third person to recover for carpentry work. The defense was that the partnership was unlicensed, although Gatti and his partner, Moore, each held

<sup>6</sup> *Takeuchi v. Schmuck*, 206 Cal. 782, 276 Pac. 345 (1929) (plaintiff sought to recover down payment he made on behalf of his father, an alien—conspiracy to violate Alien Land Law); *May v. Herron*, 127 Cal. App. 2d 707, 274 P.2d 484 (1954) (plaintiff contractor advised defendants he would build them a house if they could get a relative, who was a veteran, to secure a government permit to do so—conspiracy to violate Federal Priorities Regulation No. 33); *Orlinoff v. Campbell*, 91 Cal. App. 2d 382, 205 P.2d 67 (1949) (court said statute prohibiting unlicensed carrier from suing intended to bring highway carriers under jurisdiction of P.U.C. and not to protect against possible dishonesty or incompetence); *Wise v. Raddis*, 74 Cal. App. 765, 242 Pac. 90 (1925) (suit by one unlicensed partner against another to recover his share of commission—not allowed). This case was overruled by *Denning v. Taber*, 70 Cal. App. 2d 253, 160 P.2d 900 (1945).

<sup>7</sup> 48 Cal. 2d at 151, 308 P.2d at 719.

<sup>8</sup> 93 Cal. App. 2d 276, 209 P.2d 24 (1949).

<sup>9</sup> *Id.* at 286, 209 P.2d at 30.

<sup>10</sup> 27 Cal. 2d 687, 166 P.2d 265 (1946).

individual licenses as contractors. Gatti contracted individually with the defendant to do the work involved. Later, Gatti and Moore entered into a partnership. Defendant agreed that the partnership could complete the work. No partnership license was ever secured. Recovery was allowed. The court pointed out that the Contractors Licensing Law was passed for the safety and protection of the public, and that such a law should not be used as a "shield for the avoidance of a just obligation."<sup>11</sup>

Another exception to the general rule of granting no relief to an unlicensed contractor is found in those cases holding that an unlicensed person is not precluded from recovery if he had a license at the time the contract and the cause of action arose, although at the time the contract was executed he was unlicensed.<sup>12</sup>

Where the action is between the contracting parties and the rights of third parties are not involved, California has recognized another exception to the general rule. It arises where the business engaged in is a lawful one and not against public policy, but the parties fail to secure a required license. If the cause of action is or can be based on a *new promise arising out of* the executed partnership agreement, rather than *directly on the partnership agreement*, relief will not be denied a party to a partnership contract against his partner. The leading case on this point is *Denning v. Taber*.<sup>13</sup> Here it was held that when the illegal transaction has been consummated and the proceeds for performance of the contract have been received, then the court is not asked to enforce a new and implied promise to deliver the proceeds to one who in good conscience is entitled to them. The court said:<sup>14</sup>

The plaintiffs do not require the aid of any illegal transaction to establish their case. It is enough that the defendants have in hand a thing of value that belongs to them. Some of the authorities show that, though an illegal contract will not be executed, yet, when it has been executed by the parties themselves, and the illegal object of it has been accomplished, the money or thing which was the price of it may be legal consideration between the parties for a promise, express or implied, and the Court will not unravel the transaction to discover its origin.

In all of the above cases a literal interpretation of the applicable statute would have barred recovery. There are other similar decisions.<sup>15</sup> These cases have been on the books for years and the legislature should be cognizant of the fact that they are not a literal interpretation of section 7031. Since the legislature has not seen fit to amend the statute so as to have the courts interpret it literally, it could be assumed that the legislature intended deviations from the express dictates of the statute in order to reach an equitable result. Thus there seems to be no valid reason to extend the application of section 7031 beyond the legislature's obvious intent. This section should be construed and applied so as to accomplish its purpose of protecting the public from dealings with incompetent or untrustworthy contractors.

<sup>11</sup> *Id.* at 690, 166 P.2d at 266.

<sup>12</sup> *Fewel & Dawes, Inc. v. Pratt*, 17 Cal.2d 85, 109 P.2d 650 (1941); *Brenneman v. Lane*, 87 Cal. App. 414, 262 Pac. 400 (1927); *Radich v. Cermokus*, 65 Cal. App. 452, 224 Pac. 124 (1924); *Houston v. Williams*, 53 Cal. App. 267, 200 Pac. 55 (1921).

<sup>13</sup> 70 Cal. App. 2d 253, 160 P.2d 900 (1945) (hearing was denied by the California Supreme Court without a single dissenting vote).

<sup>14</sup> *Id.* at 258, 160 P.2d at 902, quoting *Planter's Bank v. Union Bank*, 83 U.S. 483, 500 (1872).

<sup>15</sup> *Machett v. Gould*, 131 Cal. App. 2d 821, 281 P.2d 524 (1955); *Wold v. Luigi Consentino & Sons*, 109 Cal. App. 2d 854, 241 P.2d 1032 (1952); *Galich v. Brkich*, 103 Cal. App. 2d 187, 229 P.2d 89 (1951); *Citizen's State Bank v. Gentry*, 20 Cal. App. 2d 415, 67 P.2d 364 (1937).

In denying recovery in the *Lewis & Queen* case, the court arbitrarily determined that the defendant fell within the class to be protected by the statute. As pointed out in a dissenting opinion by Justice Carter,<sup>16</sup> the majority of the court seemed to reason backwards, *i.e.*, that because the plaintiff was within the statutory definition (subcontractor) he could not recover, instead of reasoning that because the defendant was not within the class to be protected, the defendant could not set up the statute as a bar.

By applying a literal interpretation of section 7031 as it did, the court allows a windfall to the defendant and imposes an unconscionable forfeiture on the plaintiff.

There is a clear distinction between an agreement to operate an illegal enterprise, such as the business of prostitution or gambling, and the mere conducting of a legal business without the license required by law.<sup>17</sup> Here the transaction was not one *malum in se*; there was nothing inherently illegal about the contract.

Where a large contract is involved it is very possible that the defendant will be enriched not only at the plaintiff's expense, but also at the expense of plaintiff's creditors. They may have to take what they can get in a bankruptcy proceeding. The penalty does not seem to be commensurate with the offense.<sup>18</sup>

Section 7120 of the Business and Professions Code provides that a contractor who wilfully or deliberately refuses to pay money due to one who provides him with materials or services is subject to disciplinary action. Though section 7031 bars plaintiff's cause of action, there is none the less an obligation owed to the plaintiff. It is the statute which precludes plaintiff from enforcing his right. Section 7031 is similar to the type statute of limitations which does not extinguish the plaintiff's cause of action but rather bars his remedy.

The court said in *Hollywood Wholesale Electric Co. v. John Baskin*,<sup>19</sup>

[Section] 7120 state[s] the grounds for disciplinary action against a contractor or subcontractor . . . who wilfully or deliberately fails to pay any moneys when due for materials or services rendered in connection with his operation as a contractor.

In *Beach v. Contractors State License Board*,<sup>20</sup> failure by a contractor to make payment to a subcontractor in accordance with section 7120 was one of the reasons the contractor's license was revoked. It would appear inconsistent that the legislature intended to give the defendant a bar to an action against him with one hand and make him amenable to disciplinary action for nonpayment with the other.

Since section 7031 was enacted to benefit the public and protect them against unscrupulous contractors, the court should interpret the statute so as to benefit the public and not to allow a windfall to one who in good conscience should compensate another for the consideration he has given. In allowing one in the defendant's position in the *Lewis & Queen* case to use the statute as a bar, a greater segment of the public, such as the plaintiff's creditors, is more likely to be injured than benefited.

James A. Brennan

<sup>16</sup> 48 Cal. 2d at 158, 308 P.2d at 724. Justice Schauer concurred.

<sup>17</sup> *Norwood v. Judd*, 93 Cal. App. 2d 276, 209 P.2d 24 (1949); 12 CAL. JUR. 2d, *Contracts* § 74 (1953).

<sup>18</sup> For a comprehensive discussion of the law regarding illegal contracts, see Wigmore, *A Summary of Quasi Contracts*, 25 AM. L. REV. 695 (1891); Notes, 40 VA. L. REV. 1063 (1954), 27 CALIF. L. REV. 601 (1938-39), 23 COLUM. L. REV. 665 (1923), 26 HARV. L. REV. 738 (1913). See also Wade, *Benefits Obtained under Illegal Transactions—Reasons For and Against Allowing Restitution*, 25 TEXAS L. REV. 31 (1946).

<sup>19</sup> 121 Cal. App. 2d 415, 430, 263 P.2d 665, 675 (1953).

<sup>20</sup> 151 Cal. App. 2d 117, 311 P.2d 51 (1957).

INSURANCE: RECOVERY FOR DEATH BY "ACCIDENTAL MEANS" WHEN DISEASE AND ACCIDENT COMBINE TO CAUSE DEATH.

In the case of *Underwriters at Lloyd's London, England v. Lyons*,<sup>1</sup> the insured who had a fatigued heart died shortly after accidentally discharging his shotgun in such a way as to cause one pellet to be lodged under the skin of his face. The issue was whether the insured's death was caused by accidental means solely and independently of any other cause. On conflicting medical testimony, the jury found death was caused solely by accidental means. The decision was affirmed on the principle that a fatigued heart is a dormant abnormality, and not a cause of death when an accident lowers resistance and permits the dormant condition to disable the insured. Though the insured might not have died if it had not been for a fatigued heart, the court allowed recovery. The minor accidental shotgun wound was then determined to be the sole and independent cause of death—the "accidental means."

A major problem in the field of accident insurance has been whether to allow recovery when disease and accident have combined to produce disability or death. The decisions are not easy to reconcile, because some courts have distinguished between accidental *means* and accidental *result*.<sup>2</sup> The distinction is made because accident insurance policies generally insure against death caused solely by accidental means. Courts which have recognized and applied the distinction between accidental means and accidental result have denied recovery when a serious and unexpected injury resulted from means which were not accidental.<sup>3</sup> In the *Lyons* case this problem was not directly involved as admittedly the gun was discharged unexpectedly; therefore by accidental means. But an understanding of the distinction and whether or not it should be made is necessary to an understanding of cases in the field.

In the case of *Landress v. Phoenix Mutual Life Insurance Co.*,<sup>4</sup> the deceased, in apparent good health, while playing golf was suddenly and unexpectedly overcome from the force of the sun's rays and died shortly afterwards. The policy insured against death caused solely by "accidental means." The court distinguished accidental result from accidental means, saying that the death was of an accidental nature; but as the policy insured against death caused by accidental means, and since there was nothing in the chain of causation which could properly be termed accidental or unexpected, recovery must be denied. Chief Justice Cardozo stated in dissent: "The attempted distinction between accidental results and accidental means will plunge this branch of the law into a Serbonian Bog."<sup>5</sup> Chief Justice Cardozo also stated that the words of accident insurance policies must be interpreted in the light of the understanding and usage of the average man.

The distinction between "accidental means" and "accidental result"<sup>6</sup> is technical, and the average insured would be unlikely to make the distinction. If he did so, he would probably hesitate before entering into an insurance contract containing the term "accidental means." Webster defines "accident" as an event that proceeds from an unknown cause and is therefore not expected.<sup>7</sup> An accident, then, occurs

<sup>1</sup> 248 F.2d 149 (1957).

<sup>2</sup> VANCE, INSURANCE 957 (3d ed. 1951).

<sup>3</sup> *Landress v. Phoenix Life Insurance Co.*, 291 U.S. 491 (1934).

<sup>4</sup> *Ibid.*

<sup>5</sup> *Id.* at 499.

<sup>6</sup> *Id.* at 500.

<sup>7</sup> WEBSTER, NEW COLLEGIATE DICTIONARY (2d ed. 1956).

when either the means or result is unexpected, unforeseen, or proceeds from an unknown cause. The courts, in the more recent decisions, have recognized no distinction between accidental "means" and "result."<sup>8</sup> If the phrase "due solely to accidental means" were interpreted literally and strictly, it is probable that no insured could recover because body infirmity or degeneration is frequently present as a contributing factor.

In *Lewis v. Ocean Accident and Guarantee Corp.*,<sup>9</sup> a young man in good health had a pimple on his lip. He apparently punctured the pimple with an instrument causing inflammation of the brain and death. Recovery was allowed although the means, *i.e.*, the act of puncturing the pimple, was intentional. The court observed: "The average man would say that the dire result so tragically out of proportion to its trivial cause was something unforeseen, unexpected, extraordinary, an unlooked for mishap, and so an accident."<sup>10</sup> Though an intentional act results in death, recovery is generally allowed where the intended act is done in a manner not intended,<sup>11</sup> or when the death results from a substance or instrumentality, the presence or nature of which is not known, as when one drinks poison by mistake. Recovery should be allowed when the result is not the natural and probable result of the act because the insured should not be held accountable for the unexpected results.

Recovery should be denied, as it was in *Railway Mail Association v. Stauffer*,<sup>12</sup> where an everyday act involving ordinary exertion brings death to an insured because he is a sufferer of heart disease. The average man would say that no accident had occurred.

Accident insurers have insured against death or disability caused "solely" by "accidental means" and "independently of all other causes." In addition, they sometimes specifically exclude coverage for death or disability "caused in whole or in part by disease." There are many cases involving the construction to be placed on accident insurance policies containing this and language of similar import; but the decisions are not uniform. The terms disease and infirmity in accident insurance policies are generally construed liberally in favor of the insured and refer only to diseases or infirmities of a somewhat serious or chronic nature.<sup>13</sup>

The courts agree that if the insured was free from disease before the accident occurred and if the accident caused death or disability, or caused disease which resulted in death or disability, the insurer is liable.<sup>14</sup> The courts also agree that when the insured suffered from a disease before the accident and where the accident would have caused death or disability even if the pre-existing disease had not been present, the insured can recover.<sup>15</sup>

The major difficulty, over which there has been so much controversy, is in determining the insurer's liability when the insured dies or is disabled due to the combined effect of pre-existing disease and accident. In such cases, there are almost

<sup>8</sup> *Burr v. Commercial Traveler's Assn.*, 295 N.Y. 294, 67 N.E.2d 248 (1946).

<sup>9</sup> 224 N.Y. 18, 120 N.E. 56 (1918).

<sup>10</sup> *Id.* at 19, 120 N.E. at 57.

<sup>11</sup> *United States Mutual Accident Assn. v. Barry*, 131 U.S. 100 (1889).

<sup>12</sup> 152 F.2d 146 (D.C. Cir. 1945).

<sup>13</sup> *Arnstein v. Metropolitan Life Insurance Co.*, 329 Pa. 158, 196 Atl. 491 (1938); *Silverstein v. Metropolitan Life Insurance Co.*, 254 N.Y. 81, 171 N.E. 914 (1930).

<sup>14</sup> *Barnett v. John Hancock Mutual Life Insurance Co.*, 304 Mass. 564, 24 N.E.2d 662 (1939).

<sup>15</sup> *Crowder v. General Accident Assurance Corp.*, 180 Va. 117, 21 S.E.2d 772 (1943).

as many approaches to the problem as there are decisions. The following cases will serve to illustrate divergent views.

In *Silverstein v. Metropolitan Life Insurance Co.*,<sup>16</sup> the insured, lifting a milk can, slipped and fell. The can struck him in the abdomen and ruptured a small ulcer. This rupture allowed the contents of the stomach to escape into the abdominal cavity, which caused peritonitis and death. Before the accident, the ulcer was unknown and was described as being the size of a pea, dormant, and not progressive. Left to itself it would have been as harmless as a pimple or a scratch. The policy explanation contained a provision that it was not to "cover accident, injury, disease, or death, or other loss caused wholly or partly by disease or bodily or mental infirmity or medical or surgical treatment."<sup>17</sup> The court, through Justice Cardozo, pointed out that an insurance policy "is not accepted with the thought that its coverage is to be restricted to an Apollo or a Hercules."<sup>18</sup> The court assumed that death would not have resulted "but for" the pea-sized ulcer and allowed recovery on the principle:<sup>19</sup>

A distinction, then, is to be drawn between a morbid or abnormal condition of such quality or degree that in its natural and probable development it may be expected to be a source of mischief in which event it may be fairly described as a disease or infirmity; and a condition abnormal or unsound when tested by a standard of perfection, yet so remote in its potential mischief that the average man would call it not disease or infirmity but at the most a *predisposing tendency*. (Emphasis added.)

This distinction, though it may not be a simple solution in all cases, provides a workable standard by which reasonably uniform decisions could be reached. Courts and juries have long been disposed to allow recovery, where possible, when disease and accident have combined.<sup>20</sup> This principle would allow recovery even though there is pre-existing disease, but deny recovery when pre-existing disease has played too large a role in causing death or injury. Accident coverage may be broadened in some cases, but it will not be wider than the average insured believes it to be. Accident insurance companies should realize that their accident policies are going to cover accidents as they are popularly conceived without undue regard to the wording used in the policy. It may be possible for insurance companies to attempt to limit their liability by the use of specifically worded exceptions, but this has not always been successful in the past.<sup>21</sup> The wording of the policy is not likely to prevent recovery when pre-existing disease of a non-serious nature and accident combine to produce death or injury.

The court rejected a literal interpretation of the policy in the *Silverstein* case because it would reduce the policy and its coverage to absurdity. Combination of two or more causes makes it impossible to point to any one cause as being efficient to the exclusion of all others. The chain of causation can not be followed from inception to conclusion as it is practically impossible to do so under a liberal interpretation of the policy. For this reason the term "proximate cause," which is employed by a large number of courts,<sup>22</sup> tends to be misleading, although it may be a convenient label for an efficient cause.

<sup>16</sup> 254 N.Y. 81, 171 N.E. 914 (1930).

<sup>17</sup> *Ibid.*

<sup>18</sup> *Id.* at 82, 171 N.E. at 915.

<sup>19</sup> *Ibid.*

<sup>20</sup> See *Stout v. Pacific Mutual Life Insurance Co.*, 130 Cal. 471, 62 Pac. 732 (1900).

<sup>21</sup> See note 16 *supra*.

<sup>22</sup> *Stokes v. Police and Firemen's Insurance Assn.*, 109 Cal.App.2d 928, 243 P.2d 144 (1952).