

STATE OF CALIFORNIA
DEPARTMENT OF INDUSTRIAL RELATIONS

DECISION ON ADMINISTRATIVE APPEAL
RE: PUBLIC WORKS CASE NO. 2002-038
KOHL'S WAREHOUSE AND DISTRIBUTION CENTER
CITY OF SAN BERNARDINO

I. INTRODUCTION AND PROCEDURAL HISTORY

The Department of Industrial Relations ("Department") received a letter dated May 28, 2002, filed on behalf of the Carpenters Contractors Cooperation Committee ("Carpenters"), requesting an opinion as to whether the construction of Kohl's Warehouse and Distribution Center ("Project") in the City of San Bernardino ("City") is a public work requiring the payment of prevailing wages pursuant to Labor Code section¹ 1720 et seq. On January 17, 2003, the Acting Director of Industrial Relations ("Director"), Chuck Cake, issued a coverage determination ("Determination"), finding that the Project is a public work subject to California's prevailing wage laws. The Director received three separate

¹ All section references are to the Labor Code unless otherwise indicated.

administrative appeals of the Determination each dated February 14, 2003, filed by Kohl's Department Stores, Inc. ("Kohl's"), Inland Valley Development Agency ("Agency") and Hillwood/San Bernardino, LLC ("Hillwood") (collectively "Appellants"). Carpenters filed its response to these administrative appeals on April 30, 2003. For the reasons stated below, the appeals are denied.

II. RELEVANT FACTS

A. Introduction

This Project involves the construction of a 650,000 square-foot regional warehouse and distribution center to be owned and operated by Kohl's, a national department store chain. The warehouse and distribution center is to be located in City and will be used to support Kohl's retail store expansion into Southern California, Nevada and Arizona. The Project is being built on a parcel of land located at the former Norton Air Force Base ("Norton"). After base closure, the Air Force began the process of transferring title in the Norton property to Agency and the San Bernardino International Airport Authority for civilian reuse and redevelopment purposes. Hillwood, a private developer, was selected by Agency to lead the redevelopment effort.

B. The Formative Agreements

1. The Disposition and Development Agreement between Agency and Hillwood

The Project was implemented through a master Disposition and Development Agreement No. 3 ("DDA"), entered into on or about August 15, 2001 between Agency and Hillwood. Under the DDA, Agency agreed to convey a 60 acre "Primary Parcel"² ("Site") to Hillwood. Hillwood agreed to redevelop the property by re-conveying it to an "Ultimate User" who would then construct upon it a manufacturing, assembly, commercial and/or warehouse building.

2. The Advance Payment Agreement and the Purchase and Sale Agreement between Hillwood and Kohl's

a. *The Advanced Payment Agreement*

On or about September 12, 2001, in anticipation of Kohl's becoming the "Ultimate User" as referred to in the DDA, Hillwood and Kohl's entered into an Advance Payment Agreement ("APA") authorizing Hillwood to initiate demolition work pursuant to two Scope of Work Plans attached to the APA, one for above-ground abatement and demolition of buildings and streets, the other for underground demolition and removal of utilities. On or about September 17, 2001, Hillwood entered into a contract with Tetra Tech, Inc.

² The DDA also provided an option to buy an additional 20 acre property, referred to as "Option Parcel." To the Department's knowledge, this option has not been exercised.

("Tetra Tech") to perform the above-described demolition work.

Under the APA, Kohl's paid Hillwood \$130,000 as a first advanced payment, which was to be applied toward the cost of the demolition work. The payment would then be credited to Kohl's against the purchase price of the Site once the parties entered into a binding purchase and sale agreement. The APA also required Kohl's to pay a second advanced payment in the amount of \$500,000, to be applied and credited in the same manner as the first advanced payment.

The APA was amended on or about November 2, 2001 ("Amended APA") to provide for a third advanced payment by Kohl's in the amount of \$870,000 and a fourth advanced payment in the amount of \$500,000. Kohl's agreed that a portion of the third and fourth advanced payments would pay for underground demolition costs, without that amount being applied as a credit against the purchase price of the Site.³

b. *Purchase and Sale Agreement*

On or about November 13, 2001, Hillwood and Kohl's entered into a Purchase and Sale Agreement ("Sale

³ Of the \$870,000 third advanced payment, \$680,000 would be applied against the purchase price, \$56,000 would be applied against a change order to the Demolition Contract pertaining to the acceleration of the demolition work schedule, and the remaining \$134,000 would be applied against a second change order to the Demolition Contract pertaining to the underground demolition work.

Of the \$500,000 fourth advanced payment, \$318,500 would be applied against the purchase price, \$98,000 would be applied against the first change order, and the remaining \$83,500 would be applied against the second change order.

Agreement"). The parties agreed, among other things, that Hillwood would pay the cost of the above-ground demolition work and Kohl's would pay the cost of the underground demolition work. The amounts already advanced by Kohl's under the APA and Amended APA for the above-ground work would be credited against the purchase price of the Site. As for the underground demolition work, Kohl's had already made some payments toward the cost of this work pursuant to the Amended APA; Kohl's agreed to pay the balance upon receipt of invoices for progress payments. In addition, Kohl's agreed to pay Hillwood an additional \$25,000 as compensation for the administration and coordination of the underground demolition work being performed by Tetra Tech.

The Sale Agreement was amended on or about November 28, 2001. The amendment extended the date for the close of escrow to December 4, 2001. It also finalized the amount of two credits against the purchase price provided for under the Sale Agreement: (1) a \$160,000 credit for the installation of a water line; (2) a \$180,000 credit for work related to the installation of a storm sewer line. Kohl's had agreed to undertake this work pursuant to a Site Development Agreement with Agency.

C. The Conveyance of the Site from Agency,
To Hillwood, and Then to Kohl's

Agency transferred fee title interest in the Site to Hillwood for \$0.75 per square foot, for a total of

\$1,939,521. Close of escrow between Agency and Hillwood was conditioned on the concurrent closing of escrow between Hillwood and Kohl's whereby Kohl's purchased the property from Hillwood in a back-to-back escrow for \$2.55 per square foot, for a total of \$6,564,371.40. The escrow holder was directed to record the deed directly from Agency to Kohl's to avoid a second deeding. Escrow closed and the quitclaim deed was recorded on December 5, 2001.

D. Project Construction

Prior to the close of escrow, Hillwood and Kohl's entered into construction contracts and initiated construction activities to prepare the Site. Because Agency still owned the Site, Hillwood and Kohl's entered into temporary licensing agreements with Agency, allowing them and their contractors to enter the Site and perform the work. The most pertinent licenses are discussed below.

1. Hillwood's Undertaking

On or about September 17, 2001, the date that Hillwood contracted with Tetra Tech for the demolition work, Hillwood, Tetra Tech and Agency entered into a License Agreement Permitting Limited Entry for Demolition of Specific Structures and Improvements Relating Thereto ("Demolition License"). The demolition work was carried out pursuant to a Demolition Plan, attached as an exhibit to the Demolition License. The Demolition Plan called for the

abatement of hazardous materials, the demolition of five buildings, and the removal of associated utility infrastructure and paved surfaces at the Site. All costs associated with this work were paid by Hillwood.

The Demolition License required both Agency and Hillwood to enter into separate contracts with Montgomery Watson Harza, Americas, Inc. ("MWH") for "oversight of demolition, abatement and removal work."

a. *Contract between Agency and MWH*

As required under the Demolition License, Agency entered into a contract with MWH on or about September 24, 2001 ("Master Services Agreement"), in which MWH agreed to perform inspection, testing and oversight services in connection with asbestos and lead abatement work undertaken by Tetra Tech at the Project Site. The Scope of Work under the Master Services Agreement describes the work to be performed by MWH during demolition as continuous third-party oversight for the lead and asbestos abatement activities, including observation of Tetra Tech's work practices and engineering controls, periodic air and wipe testing, visual clearance reviews, etc. The Demolition License required Tetra Tech to revise the Demolition Plan as reasonably required by MWH on behalf of the Agency and consistent with the Master Services Agreement.

Under the Demolition License, Hillwood agreed to pay the first \$50,000 of MWH's fee due under the Master Services Agreement, with the balance to be split evenly between Agency and Hillwood. In the end, the total amount due MWH under the Master Services Agreement was \$55,142.14, of which Hillwood paid \$52,571.07 and Agency paid \$2,571.07.

b. *Contract between Hillwood and MWH*

As required under the Demolition License, on or about October 5, 2001, Hillwood retained the services of MWH for environmental oversight work. The Scope of Work describes the work to be performed by MWH during demolition as 80 hours of site inspection, focusing on demolition and pad removals, grading, utility excavation and other activities involving soil contact. This work was paid by Hillwood.

Independent of the above-described oversight work undertaken by Agency and Hillwood pursuant to the Demolition License, Tetra Tech was also required under its demolition contract with Hillwood to engage a third party contractor for environmental monitoring and oversight.

2. Kohl's Undertaking

On or about November 9, 2001, Kohl's entered into a contract with J.D. Diffenbaugh, Inc. for the performance of site work and building construction. By letter of November 2, 2001 from Kohl's to Diffenbaugh, Kohl's issued a

Notice of Commencement requiring that the Project be substantially completed by August 1, 2002.

On or about November 30, 2001, Agency and Kohl's entered into Temporary License Agreement for the Grading of Land. The Work Plan attached as Exhibit C to the Grading License describes the work to be performed by Kohl's at the Site prior to the close of escrow. This work includes pre-watering, rough grading and commencement of utility construction. All costs associated with this work were paid by Kohl's.

Following demolition and grading, Kohl's undertook actual building construction.

E. Agency's Offer of Financial Inducements to Kohl's For Development of the Project

1. The Mayor's Letter to Kohl's

Mayor Judith Valles wrote to Kohl's on or about September 7, 2001 offering a package of financial incentives. The first element of the package pertained to permit and impact fees totaling \$577,482.78. Mayor Valles stated:

Kohl's would not be responsible for the payment of any of the deferred fees as outlined in this letter. Although the City of San Bernardino must characterize the non-payment of the following set forth fees as a 'deferral', under no circumstances will Kohl's nor the project be obligated for the payment of such fees. (September 7, 2001 Letter to Kohl's Corporation from Mayor Judith Valles, p. 1.)

As an additional financial incentive, Mayor Valles agreed to recommend to the Common Council approval of a tax increment reimbursement agreement, allowing Kohl's to be reimbursed a portion of its property taxes for ten years. The Mayor stated:

Based upon a San Bernardino project on the subject site having an assessed valuation of at least \$50,000,000, we believe that the estimated value to Kohl's of this [agreement] could be equal to approximately \$45,000 to \$50,000 per year. (September 7, 2001 Letter to Kohl's Corporation from Mayor Judith Valles, p. 3.)

2. Project Development Mitigation Credits

On or about November 30, 2001, Agency and Kohl's entered into Assignment of Primary Parcel Development Project Mitigation Credits ("Assignment"). Under the terms of the Assignment, Agency agreed to transfer to Kohl's (1) 4,282 vehicle trip credits per day and (2) 14,118 gallons per day of sanitary sewer treatment capacity rights. City accepted the assignment of these credits to Kohl's and applied them to offset a \$75,369 City traffic impact fee and a \$175,769 City sewer capacity fee. Under the express terms of the Assignment, if the City had ultimately refused to recognize the transfer of these credits, Agency would assume responsibility for paying these City impact fees on Kohl's behalf. The Mayor and Common Council convened at a joint regular meeting on or about September 17, 2001 and approved the "fee deferrals." It is noted that this meeting occurred over two months prior to the date of the Assignment.

3. Tax Increment Reimbursement Agreement

On or about November 30, 2001, Agency and Kohl's entered into Tax Increment Reimbursement Agreement ("Tax Reimbursement Agreement"). Pursuant to the terms of the Tax Reimbursement Agreement, Agency "shall reimburse the Developer for its payment of the Development Costs from the Tax Increment Revenues received by the Agency from the real property taxes paid." (Tax Reimbursement Agreement, p. 3, § 1.) The reimbursement payments "shall be equal to twenty-two percent (22%) of the real property taxes actually paid." (Tax Reimbursement Agreement, p. 3, § 1.) The reimbursement payments are referred to as "redevelopment assistance to reduce Development Costs." (Tax Reimbursement Agreement, p. 2, Recital 8.) Development Costs are defined as "off-site infrastructure costs, utility construction costs and other eligible public infrastructure costs in connection with development of the Project." (Tax Reimbursement Agreement, p. 2, Recital 7.)

The mechanics of the reimbursement are described in Section 3 of the Tax Reimbursement Agreement, which states in pertinent part that: (1) Kohl's "shall provide to the Agency within forty-five (45) days after the payment of each installment of real property taxes . . . a copy of the real property tax bill" and evidence of tax payment; (2) Agency "shall remit to the Developer on or before August 31 of each

year commencing on August 31, 2002, through and including August 31, 2012" the annual reimbursement payment. (Tax Reimbursement Agreement, p. 3, § 3.) The total amount of reimbursement payments recoverable by Kohl's over the course of the ten year term of the Tax Reimbursement Agreement is capped at \$576,890. (Tax Reimbursement Agreement, p. 4, § 3(c).)

For its part under the Tax Reimbursement Agreement, Developer agreed to operate a warehouse and distribution center at the Site, keep the Site on the property tax rolls, and provide the Agency with a list of "actual" Development Costs upon completion of construction. (Tax Reimbursement Agreement, pp. 4-5, § 5.) Thus far, Kohl's has refrained from exercising its reimbursement rights under the Tax Reimbursement Agreement.

III. DISCUSSION

A. Request for Hearing

Appellants have requested a hearing pursuant to California Code of Regulations, title 8, section 16002.5. They assert that the Determination misstates the facts and a hearing is required to resolve the factual disputes raised on appeal.

As the above-cited regulation provides, the decision whether to hold a hearing is within the sole discretion of the Director. A hearing may be needed when the material

facts of a case are in dispute and resolution of the factual disagreement cannot be determined on the basis of the record. Here, whatever factual inaccuracies exist in the Determination are corrected, in part as a result of the submission of additional information on appeal.⁴

The corrections made to the facts, however, have no bearing on the resolution of the dispositive legal issues involved here. For these reasons, a hearing is unnecessary and the Appellants' request is denied.

B. Applicable Law

Section 1771 requires, with certain exceptions, that prevailing wages be paid to all workers employed on public works. Under what is now section 1720(a) (1) (as amended by statutes of 2001, chapter 938, section 2 (Senate Bill 975)), a public works is defined as follows:

Construction, alteration, demolition or repair work done under contract and paid for in whole or in part out of public funds For purposes of this subdivision, "construction" includes work performed during the design and preconstruction phases of construction including, but not limited to, inspection and land surveying work.

⁴ The Determination misstates the correct property tax reimbursement formula. The correct formula is described herein under the section "Relevant Facts."

In addition, certain facts stated in the Determination reflect the administrative record as it existed prior to the filing of the appeals. The administrative record has since been augmented by the submission of additional information. During the administrative appeal process, the parties submitted 68 documents, several of which were duplicative, many of which were already part of the administrative record, and some of which were new. The section "Relevant Facts," by incorporation of portions of the augmented administrative record, corrects any factual inaccuracies in the Determination.

Thus there are three elements to a public works: (1) the project involves construction, alteration, demolition or repair; (2) the work is performed under contract; and (3) the work is paid for in whole or in part out of public funds.

There is no question the Project here involves construction and that the work is being performed under contract. The issue in dispute is whether it is being paid for in part with public funds. As explained below, there are at least two sources of public funds.⁵ One is the Tax Reimbursement Agreement, by which Agency is contractually obligated to reimburse Kohl's a portion (22%) of the property taxes it pays each year, up to a maximum amount of \$576,890. The other source of public funds is \$2,571.07 paid by Agency to MWH under the Master Services Agreement to perform inspection, testing and oversight services in connection with asbestos and lead abatement work undertaken by Hillwood's contractor, Tetra Tech, at the Project Site during demolition.

⁵ As stated in Footnote 2 of the Determination, because the Decision on Appeal is being decided on other grounds, it is unnecessary to reach the issue of whether the Agency sold the Site to Hillwood at less than fair market value and whether a below market transfer would constitute a payment of public funds for construction.

C. Property Tax Reimbursements Under The Tax Reimbursement Agreement Constitute A Payment Of Public Funds For Construction.

Under the Tax Reimbursement Agreement, Agency "shall" Reimburse Kohl's for its development costs from tax increment revenues received by Agency, in an amount equal to twenty-two percent of the real property taxes collected from Kohl's over the course of ten years, up to a maximum of \$576,890. The Tax Reimbursement Agreement refers to these reimbursement payments as a form of "redevelopment assistance" designed to reduce development costs, which are defined as "off-site infrastructure costs, utility costs, utility construction costs and other eligible public infrastructure costs in connection with development of the Project."

Under the Tax Reimbursement Agreement, Agency is contractually obligated to make payments to Kohl's out of the public coffers for the express purpose of reimbursing Kohl's for construction costs. As such, these reimbursement payments constitute a payment of public funds for construction. (See *Pleasant Hill Schoolyard Redevelopment Project*, PW 2002-053 (July 10, 2003) (involving in part a reimbursement scheme funded by annual net tax increments and housing set-aside revenues of redevelopment agency).)

Agency and Kohl's advance two main arguments on appeal. First, they argue that the payments contemplated under the

Tax Reimbursement Agreement are not for construction, but rather for operation of the business. Contrary to Kohl's and Agency's assertions, the Tax Reimbursement Agreement is unambiguous in its declaration of purpose. As set forth in the Tax Reimbursement Agreement itself, the purpose of these payments is to assist Kohl's in reducing Project development costs, as defined above.

Second, Kohl's and Agency assert that Agency has no obligation to make payments under the Tax Reimbursement Agreement until Kohl's has satisfied a number of "conditions precedent." Kohl's has not satisfied these "conditions precedent," so Agency has not made any payments. Therefore, Kohl's and Agency argue, there has been no expenditure of public funds for construction, an essential element for finding this Project to be a public works.

The "conditions precedent" are found in Sections 3 and 5. Section 3 sets out the conditions for payment. Simply stated, in order to receive reimbursement, Kohl's must provide Agency with a copy of the tax bill and evidence of bill payment.

Section 5 contains the representations and covenants of the parties. Under this section, Agency agrees to make reimbursement payments to Kohl's by August 31 of each year; and Kohl's agrees to pay its property taxes on time, operate

its business at the Site through June 30, 2012, and provide the Agency with a list of actual development costs incurred.

For reasons unbeknownst to the Department, Kohl's has not provided Agency with a list of actual development costs pursuant to Section 5, nor has it provided Agency with a copy of its tax bill(s) or evidence of bill payment pursuant to Section 3. Evidently, Kohl's is not at the present time choosing to exercise its rights to reimbursement under the Tax Reimbursement Agreement and, consequently, has received no payment. While that is Kohl's choice to make, that choice does not alter the character of the Tax Reimbursement Agreement. This document is an agreement to spend public funds to reimburse Kohl's for construction-related costs incurred in connection with the Project.

Over the years, the Department consistently has held that a reimbursement agreement, which contemplates future repayment of construction costs out of public coffers, satisfies the public funds element of a public works. (See, e.g., *Morro Bay Desalination Plant*, PW 91-041A (November 29, 1991); *Tustin Fire Station*, PW 93-054 (June 28, 1994); *City of Clovis Sewer Improvement Project*, PW 2001-041 (August 15, 2002).) In fact, similar arguments were raised in *Morro Bay* and were addressed as follows:

Aqua Design next contends that the Determination was premature because no public funds have been or may be paid if the conditions of the contract are not fulfilled by Aqua Design. This contention confuses the

effect of the parties' terms of contract regarding the method and timing of payment with the statutory factors governing whether a project falls within the public works statutes. Where a duly executed contract between a public entity and a private contractor clearly specifies, as in the instant case, that public funds will be paid for construction, determination whether the project is a "public works" under Labor Code section 1720(a) is not contingent on prior payment of such public funds.

Here, the "conditions precedent" are simply conditions of the type that are normally required in any bilateral contract. As to these conditions, it can safely be assumed that Kohl's is paying its taxes and continuing to operate its business at the Site, and will remedy its failure to provide Agency with a list of its actual development costs when it decides to exercise its rights to receive payment. At that time, payment by Agency will be triggered automatically upon submission by Kohl's of appropriate tax documentation.

In sum, the determination whether a project is a public works is not contingent on prior payment of public funds. What is important is that the Tax Reimbursement Agreement was a financial inducement for Kohl's to build its warehouse and distribution center in City and its purpose is to assist Kohl's in reducing its construction costs. Therefore, the funding mechanism embodied in the Tax Reimbursement Agreement satisfies the public funds element of a public works. If Kohl's were to agree to forego payments under the Tax Reimbursement Agreement, and such payments were the only

source of public funds involved, then the public funds element of a public works would be removed and prevailing wages would not be owed. Kohl's, however, has not declared any such intent and the payments under the Tax Reimbursement Agreement are not the only source of public funds involved in this Project, as discussed in the following section.

It should be underscored here that the purpose of California's prevailing wage law is to "protect and benefit employees on public works projects." *Lusardi Construction Co. v. Aubry* (1992) 1 Cal.4th 976, 985. Consistent with this purpose, prevailing wage statutes are to be construed liberally. *McIntosh v. Aubry* (1993) 14 Cal.App.4th 1576, 1589. As such, to find that no coverage determination can be made until Kohl's decides to accept the public funds due under the Tax Reimbursement Agreement would defeat the purpose of the statute. It would allow the parties to defer receipt of the public funds until the time for enforcement of prevailing wages has run, and thereby deprive workers of the prevailing wages they are owed. To effectuate the purpose of the prevailing wage laws, public works coverage determinations must necessarily be made on the basis of the funding arrangements and agreements made by the parties at the time a project is conceived.

D. Agency's Payment Of \$2571.07 Under The Master Services Agreement For Inspection, Testing And Oversight Services Performed In Connection With The Abatement Work At The Project Site Constitutes A Payment Of Public Funds For Construction.

Under the Master Service Agreement between Agency and MWH, MWH agreed to provide inspection, testing and oversight services in connection with the asbestos and lead abatement work performed by Hillwood's demolition contractor, Tetra Tech, at the Project Site. MWH was required to provide continuous oversight of these abatement activities, including observation of Tetra Tech's work practices and engineering controls, periodic air and wipe testing, and visual clearance reviews.

Under section 1720(a) (1), "construction" includes work performed during the design and preconstruction phases of construction including, but not limited to, inspection and land surveying work. The work performed by MWH at the Project Site under the Master Services Agreement fits squarely within the definition of construction. The work was performed under contract between MWH and Agency in conjunction with the Project, as required by the Demolition License. Agency's contribution of \$2,571.07⁶ toward the cost of this work is a payment of public funds for construction

⁶ Appellants have characterized this amount as "de minimus." Under the applicable law, there is no "de minimus" exception to the public funds element of a public works.

and thereby constitutes a second ground for finding this Project to be a public works.

Appellants make a variety of similar arguments on appeal, which can best be condensed into two main arguments. First, they assert the work at issue was not necessary or integral to the Project because it benefited the Agency only and was duplicative of the work performed by Tetra Tech's third-party environmental oversight contractor.

This work was necessary to the Project for at least one very obvious reason. The Demolition License *requires* that it be performed. Moreover, the Demolition License also *requires* Tetra Tech to revise its demolition activities at the request of MWH on behalf of Agency and consistent with the Master Services Agreement. The assertion that the work at issue was duplicative or of no consequence to the Project is rejected.

Second, Appellants cite *Vineyard Creek Hotel and Conference Center, Redevelopment Agency, City of Santa Rosa*, PW 2000-016 (October 16, 2000) in support of the argument that the demolition work performed by Hillwood and the subsequent grading and building construction performed by Kohl's are two separate projects. *Vineyard Creek* set forth factors to consider in determining whether a construction undertaking is one or multiple projects. These factors include organization of the construction, physical lay-out,

project oversight, financing and general interrelationship of the various parts.

Applying the factors leads to the conclusion that the undertaking here is one project, which involves both the demolition work undertaken by Hillwood and the subsequent grading and building work undertaken by Kohl's. That there was one contractor responsible for the demolition and another for the grading and building construction is of no consequence given the physically integrated nature of the entire Project. For public works purposes, the "construction" process includes everything required to erect a structure. (*Priest v. Housing Authority* (1969) 275 Cal.App.2d 751, 756; *Marina Suites Hotel and Conference Center, Suisin City Waterfront*, PW 2002-006 (September 26, 2002) (site preparation work paid for with public funds "part of and integrally connected to" the subsequent construction of the hotel and conference center.)

Also Appellants' *Vineyard Creek* argument is factually flawed. Hillwood states that "there was no interrelationship" between Hillwood's undertaking and Kohl's undertaking. (Hillwood appeal, p. 5, f. 4.) Kohl's states that Kohl's had no "interest" in the Site prior to acquisition and that Hillwood undertook demolition at its sole expense. (Kohl's appeal, p. 4, f. 5.)

Kohl's ownership interest in the Site is indistinguishable from Hillwood's ownership interest in the Site. Escrow for both sales closed on the same date. Prior to transfer of title on December 5, 2001, Kohl's and Hillwood were actively working to consummate the deal - coordinating the financing of the demolition work, engaging in Site preparation activities, and entering into binding agreements. For example, Kohl's was a party to the second amendment to the DDA with Agency, entered into on or about October 24, 2001, agreeing to construct the foundation of the Project within a certain period of time. Prior to that, on or about September 12, 2001, Kohl's entered into the APA with Hillwood, agreeing to advance funds for the demolition work. Although it is true Hillwood undertook responsibility for performing the demolition work, it was not at Hillwood's sole expense. Under the Sale Agreement, Kohl's agreed to pay for the underground demolition work, including a \$25,000 fee to Hillwood for coordinating that work. Kohl's also paid for a change order that accelerated the demolition schedule. Contrary to Kohl's assertions, and lending further support to the finding of a single project, these facts evidence a shared interest, both financial and otherwise, by Kohl's and Hillwood in the success of the Project as a whole.

In sum, there is but one project. Therefore, Agency's payment under the Master Services Agreement for inspection, testing and oversight services in connection with the asbestos and lead abatement work at the Project Site constitutes a payment of public funds for construction and thereby satisfies the public funds element of a public works.

E. Agency's Transfer Of Project Development Mitigation Credits To Kohl's Does Not Constitute A Payment Of Public Funds For Construction.

As an inducement to build its warehouse and distribution center in City, the Mayor offered Kohl's a package of financial subsidies. One such subsidy was a waiver⁷ of development impact and permit fees totaling \$577,482.78. This amount included the following two fees: \$75,369 in traffic impact fees and \$175,769 in sewer capacity fees (collectively "two City fees"). Under the Assignment, Agency agreed to transfer to Kohl's 4,282 vehicle trip credits per day and 14,118 gallons of sanitary sewer treatment capacity rights per day (collectively "Agency credits"), which would go towards offsetting the two City fees. In the event City refused to recognize the transfer of the Agency credits, Agency was obligated under the Assignment to pay the two City fees on Kohl's behalf.

⁷ As stated by the Mayor in her letter to Kohl's of September 7, 2001, City was required to characterize the waiver of fees as a deferral. Regardless of the characterization, the Mayor assured Kohl's that "under no circumstances" would it be obligated to pay these fees.

The Determination stated in Footnote 5 that if Agency became obligated to pay the two City fees on Kohl's behalf, such payment would constitute an additional basis for coverage. Kohl's submitted a Summary of the September 17, 2001 Common Council meeting, reflecting the Council's approval of the "fee deferrals." Also, according to representations made by Kohl's and Agency, City accepted the transfer of the Agency credits to Kohl's. Therefore, no payment by Agency of the two City fees was ever required.

Concluding the issue left open in Footnote 5 of the Determination, neither the waiver of City fees nor the transfer of Agency credits constitutes a payment of public funds for construction. Neither the waiver nor the transfer involves a payment of funds from public coffers. (See, *McIntosh v. Aubry* (1993) 14 Cal.App.4th 1576, 1590.)⁸

On appeal, Carpenters argues for a different conclusion. Carpenters assert that the transfer of Agency credits constitutes a payment of public funds based on three separate lines of authority.

First, Carpenters cites the Department's precedential decision in *Redding Hotel Renovation, Redding Redevelopment Agency/City of Redding*, PW 2002-008 (February 25, 2003). *Redding Hotel* involves an exemption under Senate Bill 975

⁸ It should be noted that the law has since changed. Under section 1720 as amended by Senate Bill 975, fee waivers now constitute a payment of public funds for construction. *McIntosh* still applies, however, in cases decided under pre-Senate Bill 975 law, such as this one.

amendments to section 1720 for low-income housing projects that are allocated state or federal low-income housing tax credits. (Lab. Code § 1720(d)(3).) Carpenters' reliance on this case is misplaced for two reasons. First, Senate Bill 975 amendments do not apply here. Second, even if they did, whether a project qualifies for an exemption from coverage under Senate bill 975 amendments is a separate issue from the issue what constitutes a payment of public funds for construction.

Next, Carpenters cites *13th and F Street Townhouse Development, City of Sacramento*, PW 2000-043 (January 23, 2001) and *Mitsui Fudosan v. County of Los Angeles* (1990) 219 Cal.App.3d 525. The court in *Mitsui* found that the purchase by Mitsui from adjacent landowners of unused floor area ratios, known as transferable development rights, constituted transfer of a real property interest and therefore a taxable event. Carpenters assume that the transfer of Agency credits here would be considered a taxable event under *Mitsui*, and then rely on *13th and F* for the proposition that a taxable event constitutes a payment of public funds.

In *13th and F*, a private developer received a "loan" from a redevelopment agency, which did not contemplate repayment. The determination found that the "loan" was really an outright grant of public funds and noted that this

analysis was consistent with tax law, which defines gross income as including income derived from the discharge of indebtedness.

These cases do not support Carpenters' position. *Mitsui* involved the purchase for money of a real property interest, not the transfer of project development mitigation credits. And, contrary to Carpenters' assertion, *13th and F* does not stand for the proposition that all taxable events constitute a payment of public funds for construction.

The last case cited by Carpenters is *McIntosh*. Carpenters assert that the Department has relied on *McIntosh* in finding coverage in cases involving "non-monetary assets that have a cash equivalent value" including *Town Square Project, City of King*, PW 2000-011 (December 11, 2000) and *Riverview Business Center Office Building D*, PW 99-039 (November 17, 1999). (Carpenters' appeal, p. 7.)

Carpenters assert that the Agency credits were included as consideration for the purchase of the Site and were mentioned in the appraisal report. Therefore, Carpenters allege, the Agency credits have a cash value and a transfer of Agency credits should be considered a payment of public funds. As further support, Carpenters claim that Kohl's is entitled to "liquidate" the Agency credits for cash when it sells the Site.

Carpenters' argument is rejected for the following reasons. First, the court in *McIntosh* defined "funds" as "an available pecuniary resource like cash or some readily cash-convertible asset." (*McIntosh v. Aubry, supra*, 14 Cal.App.4th 1576, 1588.) *McIntosh* involved, among other things, a forbearance of rent and a waiver of costs. The court acknowledged that such subsidies may be "valuable as a negotiating tool in securing the total project" but are not a payment of funds out of public coffers. (*McIntosh v. Aubry, supra*, 14 Cal.App.4th 1576, 1588-1590.) Carpenters' characterization of the definition of funds as "non-monetary assets that have a cash equivalent value" is not consistent with the actual definition set forth in *McIntosh*.

Second, *Town Square* and *Riverview* involve the transfer of publicly owned land to private developers. Under *McIntosh*, real property satisfies the definition of funds in that it is property of value that readily can be converted into cash. It can be bought and sold on the open market. Therefore, when a public entity gives away real property, it is as though it is giving away cash. The same cannot be said of project development mitigation credits. While the Agency credits may have been a valuable negotiating tool in consummating the Project, they are not cash and they cannot be readily converted into cash. Therefore, a transfer of

Agency credits does not constitute a payment of public funds for construction under the law applicable to this Project.

Last, Carpenters' assertion that Kohl's is free to liquidate the Agency credits upon sale of the Site is contradicted by the express terms of the Assignment itself. Section four of the Assignment requires Kohl's upon completion of the Project to execute a written release of any unused Agency credits in favor of Agency.

In sum, the transfer of Agency credits to Kohl's is not a payment of funds out of public coffers and therefore not a basis for coverage in this matter.

IV. CONCLUSION

In summary, the appeals filed by Agency, Kohl's and Hillwood are denied, their request for hearing is also denied, and the determination that the Project is a public works requiring the payment of prevailing wages is upheld. This decision constitutes final administrative action in this matter.

Dated: 10-21-03

Chuck Cake
Chuck Cake, Acting Director
Department of Industrial
Relations