STATE OF CALIFORNIA EDMUND G. BROWN JR., *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
Christine Baker, Director
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To All Interested Parties:

Re: Public Works Case No. 2011-043
Optimized Waterflood Program for West Wilmington Oil Field
City of Long Beach

By agreement to resolve this matter, the interested parties have requested the Department of Industrial Relations vacate the Coverage Determination in Public Works Case No. 2011-043, Optimized Waterflood Program for West Wilmington Oil Field, City of Long Beach. Tidelands Oil Production Company further agreed to withdraw its appeal of said Coverage Determination.

In consideration of the unique facts leading to the determination, the Department has agreed that the Coverage Determination is hereby vacated.

STATE OF CALIFORNIA EDMUND G. BROWN JR., *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
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1515 Clay Street, 17th Floor
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April 26, 2013

Donald C. Carroll, Esq.
Law Offices of Carroll & Scully, Inc.
300 Montgomery Street, Suite 735
San Francisco, CA 94104-1909

Re: Public Works Case No. 2011-043
Optimized Waterflood Program for West Wilmington Oil Field
City of Long Beach

Dear Mr. Carroll:

This constitutes the determination of the Director of Industrial Relations regarding the coverage of the above-referenced project under California's prevailing wage laws and is made pursuant to California Code of Regulations, title 8, section 16001(a). Based on my review of the facts of this case and an analysis of the applicable law, it is my determination that the recovery of oil and gas from the West Wilmington oil field (Project) is a public work subject to prevailing wage requirements.

Facts

The City of Long Beach (City) holds in trust certain state tidelands from which City has extracted oil and gas over the past several decades.[1] Among the tidelands is the West Wilmington oil field. To recover the oil and gas from the field, City previously entered a series of agreements under which Long Beach Oil Development Company (LBODC) incurred costs of construction, erection, operation, maintenance, repair and abandonment of oil wells and associated structures and equipment, subject to approval of the State Lands Commission.[2] LBODC agreed to sell all of the oil and gas produced and pay City the net profits calculated after reimbursing LBODC all expenses incurred in the performance of its obligations plus 9 percent of the profits. LBODC subcontracted with various companies for the work of constructing the facilities on the tidelands in order to extract and deliver oil and gas.

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[1] "The city's interest in the lands involved dates from 1911 when the State of California granted to the city the tidelands and submerged lands lying within the city's boundaries in trust for certain uses and purposes connected with the development of Long Beach Harbor. Stats.1911, ch. 676, pp. 1304-1305." (*City of Long Beach v. Vickers* (1961) 55 Cal.2d 153, 157 (*Vickers*).)

[2] "The State of California owns a beneficial interest under the tidelands grants to the city, but it is not required to execute the agreements. Section 6879 of the Public Resources Code provides that when approved by the State Lands Commission the agreements bind the state and all parties executing them." (*Vickers, supra*, at p. 156.)

Over the years, the agreements were revised and City's net profit share increased. In 1989, City awarded the work to Tidelands Oil Production Company (Oxy).[3] As did LBODC before it, Oxy agreed to conduct the oil and gas recovery operations, sell the oil and gas, account for expenses and revenues, and pay City the net profits determined after deducting the expenses of the operations. Whereas LBODC also was allotted 9 percent of the profits, Oxy was allocated 5 percent of the profits over and above its expenses.

Effective January 1, 2010, City and Oxy entered into an Agreement for Implementation of an Optimized Waterflood Program (Agreement) for enhanced oil recovery techniques. Under the Agreement Oxy commits a minimum of $20 million for the design and implementation of the new techniques in order to increase oil production from new wells or redrilled existing wells. Oxy will conduct the drilling and redrilling work utilizing "independent third party contractors." (Agreement, § 2.02(c) and (d).) Oxy agrees to meet its $20 million commitment no later than two years after the date when certain published prices of oil exceed $65 per barrel, subject to stated conditions. (Agreement §§ 1.02(v) and 2.02(b).) Oxy selects the subcontractors, materials and equipment, subject to City's approval. In consideration for the $20 million Oxy commits, City agrees to accept a 51 percent share of the net profits derived from the enhanced recovery techniques, calculated on a monthly basis, after reimbursing Oxy the expenses incurred in performance of the Agreement plus 49 percent of the City's net profits. Oxy is also entitled to another 3 percent share of City's base net profits, as defined. City must pay Oxy amounts for those months when the accounting reflects that the City's allocation is less than zero.[4] (Agreement, §§ 1.02(l), 2.05, and 2.08.) Oxy and City state Oxy's increased share of profits above the prior share of profits allocated to Oxy is consideration for the $20 million commitment of investment costs Oxy makes under the Agreement. Without that commitment, City would have to invest its own capital or defer the operational changes.

In the calculation of net profits, the Agreement allocates to City 51 percent of the costs related to abandonment of the new wells, removal of associated facilities, and remediation of soil and groundwater impacted by the wells, as well as certain other costs. (Agreement, §§ 1.02(i), 2.06, 2.2, and Exhibit D.) Oxy and City state that under the previous contracts, all costs related to well abandonment were allocated to City.

Discussion

Labor Code section 1771[5] generally requires the payment of prevailing wages to workers employed on public works. Section 1720, subdivision (a)(1), defines "public works" to mean "[c]onstruction, alteration, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds...." Subdivision (b) provides:

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[3] Tidelands Oil Production Company is a subsidiary of Occidental Petroleum Corporation.

[4] City and Oxy state that there are no instances where City will ever be required to make a payment to Oxy and the section of the Agreement providing for City's payment to Oxy for a month's negative balance is a "misnomer." They indicate the Agreement will be amended to clarify that no payments are to be made by City to Oxy. No amendment has been submitted to date.

[5] Subsequent statutory references are to the Labor Code and subsequent subdivision references are to section 1720 unless otherwise indicated.

(b) For purposes of this section, "paid for in whole or in part out of public funds" means all of the following:

(1) The payment of money or the equivalent of money by the state or political subdivision directly to or on behalf of the public works contractor, subcontractor, or developer.

The parties dispute whether the Project is a public work. A preliminary issue is whether the analysis is curtailed by the doctrine of stare decisis based on the decision in *International Brotherhood of Electrical Workers v. Harbor Commissioners of the City of Long Beach* (1977) 68 Cal.App.3d 556 (*International Brotherhood*). That case found the predecessor oil drilling contract with City at the tidelands was not one for public work, but for payment of royalties to the City after drilling work undertaken by LBODC at its own risk. The analysis in *International Brotherhood* has been cited by other courts. (See, e.g., *City of Long Beach v. Department of Industrial Relations* (2004) 34 Cal.4th 942, 950; *McIntosh v. Aubry* (1993) 14 Cal.App.4th 1576, 1586 (*McIntosh*).)

Courts of inferior jurisdiction must respect the doctrine of stare decisis. (*Auto Equity Sales, Inc. v. Superior Court* (1962) 57 Cal.2d 450, 454-455. Similarly, administrative agencies are bound by stare decisis in their statutory interpretations, because the ultimate interpretation of a statute is an exercise of judicial power. (*Henning v. Industrial Welfare Comn.* (1988) 46 Cal.3d 1262, 1270.) The doctrine of stare decisis, however, extends only to the *ratio decidendi* of a decision, "the principle or rule that constitutes the ground of the decision ... that has the effect of a precedent." (9 Witkin, Cal. Procedure (5th ed. 2008) Appeal, § 509, p. 572.) "To determine the precedential value of a statement in an opinion, the language of that statement must be compared with the facts of the case and the issues raised." (*Western Landscape Construction v. Bank of America National Trust and Savings Association* (1997) 58 Cal.App.4th 57, 61.)

The current circumstances are materially different from those present in *International Brotherhood*. While the general legal issue before and now is whether the projects constitute public work, *International Brotherhood* construed the former prevailing wage law (PWL), before it was amended by Senate Bill (SB) 975. (Stats. 2001, ch. 938, § 2; *International Brotherhood, supra,* 68 Cal.App.3d at p. 560.) Amendments made by SB 975 are of significance here, because when *International Brotherhood* was issued, the phrase "paid for in whole or in part out of public funds" had not been interpreted to include payment of "the equivalent of money." After SB 975 the meaning of "paid for in whole or in part out of public funds" includes payment of "the equivalent of money," a type of public subsidy asserted in this matter. (Subdivision (b)(1).)

Further, *International Brotherhood* answered neither the question whether the drilling operations involved construction, alteration or installation done under contract nor the issue whether the project was paid for with public funds. (*International Brotherhood, supra*, 68 Cal.App.3d at p. 562.) Instead, the court simply stated the contract before it did "not contemplate any of the results ... contemplated by section 1720" and "the contract was not for a 'public work'...[but was] "an oil and gas lease, calling for payment of royalties to the City." (*Ibid.*) The court did not

employ the framework that subsequent cases use for analyzing whether a project is public work under the PWL as amended by SB 975. (See, e.g., *Hensel Phelps Construction v. San Diego Unified Port Dist.* (2011) 197 Cal.App.4th 1020, 1032 (*Hensel Phelps*) ["[s]ection 1720, subdivision (a)(1) sets forth two separate statutory requirements for the Project to be considered a 'public work'"]; and *State Bldg. and Constr. Trades Council v. Duncan* (2008) 162 Cal.App.4th 289, 309 (*Trades Council*).)

Aside from the analytical process used, the facts examined in *International Brotherhood* are different than those in the Project. While the facts before and now generally involve drilling for gas and oil on the tidelands, the contractual arrangement has changed. (*International Brotherhood, id.*, at p. 562; Agreement, § 2.02.) Besides altering the division of profits to give Oxy a bigger share, the Agreement allocates to City various costs, including 51 percent of the cost of well abandonment. While City and Oxy state that under the previous contracts, all costs related to well abandonment were allocated to City, nothing in *International Brotherhood* discloses that the contract allocated costs to City. Indeed, the opinion suggests the opposite-that LBODC operated at its own risk and paid for all services, work and labor, including that for well abandonment. (*International Brotherhood, supra*, 68 Cal.App.3d at pp. 558, 565 ["The contract required Development to conduct all operations under the contract at its own expense"].) Due to the changed circumstances, the doctrine of stare decisis does not control the current public work coverage analysis.

Turning to that analysis, public work is defined to mean "construction, alteration, demolition, installation or repair work done under contract and paid for in whole or in part out of public funds...." (Subdivision (a)(1).) "Under contract" means that the work is contracted for as opposed to being performed by a public agency with its own forces. (§ 1771.) That the Agreement contemplates that Oxy will incur costs for work performed by "independent third party contractors" satisfies the "under contract" element. (Agreement, § 2.02.)

The question becomes whether the Project involves the type of work covered by subdivision (a)(1). The root of alteration, "alter," is defined as "to cause to become different in some particular characteristic (as measure, dimension, course, arrangement or inclination) without changing into something else." (Webster's Third New Internat. Dict. (2002), p. 63;[6] *Priest v. Housing Authority of City of Oxnard* (1969) 275 Cal.App.2d 751, 756 ["[t]o 'alter' is to modify without changing into something else."); see, too, PW 2008-0158, *Land Clearing Project, Selma-Kingsburg-Fowler County Sanitation District* (June 11, 2008) ["[t]hus, with regard to land, under these definitions, alteration under section 1720(a)(1) is to modify a particular characteristic of the land in question"].) The act of drilling land modifies the surface of the land by creating holes for insertion of pipelines. The facts disclose the work involves "alteration" within the meaning of subdivision (a)(1).

"Construction" is defined to include the "'act of putting parts together to form a complete integrated object.'" (*City of Long Beach, supra,* 34 Cal.4th at p. 951, quoting Webster's Third New Internat. Dict. (2002), p. 489.) Under that definition, the construction of structures, pipelines and

[6] Dictionary definitions of statutory terms can shed light on the meaning of the law. (*City of Long Beach, supra,* 34 Cal.4th at p. 951, quoting a dictionary for the plain meaning of "construction.")

associated facilities necessary to accomplish extraction of oil and gas constitutes construction within the meaning of subdivision (a)(1). (See, too, appendix to *International Brotherhood* showing the drilling operations included "the construction, erection, operation, maintenance, repair, and abandonment of Oil Wells" and various structures, equipment and facilities. [*International Brotherhood, supra,* 68 Cal.App.3d at pp. 563-564].)

"Installation" has been defined in prior public works coverage determinations as work involving the bolting, securing or mounting of fixtures to realty. (See, e.g., PW 2008-034, *Installation of Smart Classroom Technology, Fresno Unified School District* (July 27, 2009) and cases referenced therein; also see Webster's Third New Internat. Dict. (2002), p. 1171 [defining "installation" as "the setting up or placing in position for service or use"].) No party denies that at least some drilling equipment, pipelines, and facilities will need to be affixed to the realty. Hence, "installation" within the meaning of subdivision (a)(1) occurs at the Project.[7]

The next question is whether the work is paid for in whole or in part out of public funds. Subdivision (b)(1) defines "paid for in whole or in part out of public funds" to mean "the payment of money or the equivalent of money" by the state or political subdivision to or on behalf of a contractor, subcontractor, or developer. In *McIntosh,* the court turned to dictionary definitions of "pay" and "funds" to analyze the plain meaning of the phrase "paid for in whole or in part out of public funds." The definitions included "the delivery of money or its equivalent," payment "out of available pecuniary resources ordinarily including cash and negotiable paper," and "some readily cash-convertible asset." (*McIntosh, supra,* 14 Cal.App.4th at p. 1588 [internal citations and quotation marks omitted].)

While "equivalent of money" is not defined in section 1720, the plain meaning of "equivalent" is "[e]qual in value, force, amount, effect or significance; [c]orresponding in effect or function; nearly equal; virtually identical." (Black's Law Dict. (9th ed. 2009), p. 620.) The plain meaning is also "[c]orresponding or virtually identical esp. in effect or function." (Webster's Third New Internat. Dict. (2002), p. 769.) Application of the "equivalent of money" subsidy was discussed in *Trades Council, supra,* 162 Cal.App.4th at pages 307 and 311. There, the question was whether tax credits provided by the state to facilitate construction of low-income housing falls under the definition of "paid for in whole or in part out of public funds." (*Id.*, at p. 294.) Citing case law that "excludes tax credits from the category of goods and services that amount to public assets or are treated as the equivalent of money," the court noted that a tax credit "has no intrinsic value to the state [,]... is not sold by the state[,] ...[and] cannot be stolen from the state." (*Id.,* at pp. 310-311.) Because subdivision (b)(1) "speak[s] to the state or political subdivision parting with a thing possessing current value," the court found that the tax credits did not constitute the equivalent of money under that subdivision. (*Id.*, at pp. 311, 315.)

The "payment of money or the equivalent of money" appears under the facts of this case. Oxy and City indicate that for any month in which the accounting shows for City a negative balance

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[7] City and Oxy admit as much where they state that the installation, removal, and/or relocation of pipe is a necessary component of drilling for oil. Also, the well abandonment work contemplated by the Agreement constitutes "demolition" within the meaning of subdivision (a)(1) to the extent that work "involves tearing down that which has been constructed." (*Priest, supra,* 275 Cal.App.2d at p. 756.)

because costs of operations allocated to City exceed its agreed-upon share of oil and gas sales revenues, the balance is carried forward in lieu of City having to pay the amount to Oxy. That arrangement is contrary to the wording of section 2.08 of the Agreement, which requires City payments to Oxy in the amount of the negative balance for a given month. While Oxy and City expect to amend the Agreement to provide the City must make no payments to Oxy, under the Agreement as known, City payment to Oxy for the negative balance would constitute the payment of money within the meaning of subdivision (b)(1). If the Agreement is amended along the lines Oxy and City suggest, this conclusion would be revisited to the extent it is based on section 2.08 payments.

The Southern California Labor/Management Operating Engineers Contract Compliance Committee argue for a subdivision (b)(1) public subsidy on the theory that City pays for the work out of the profits that are divided with Oxy, thereby decreasing City revenues. The argument has merit. The proceeds from the sale of oil and gas constitute money. While Oxy holds the sale proceeds for the cost allocation process, thereafter paying City a share, the proceeds are "a thing possessing current value," an "available pecuniary resource," and a "readily cash-convertible asset." (*Trades Council; McIntosh.*) By agreeing to deduct from gross proceeds the cost of operations, absorbing certain costs itself, City effectively pays to Oxy a pecuniary resource, part of the proceeds from the oil and gas production. Unlike the tax credits in *Trades Council*, which "ha[d] no intrinsic value to the state," the proceeds from the sale of gas and oil produced from the tidelands do have intrinsic value to City. (*Trades Council, supra,* 162 Cal.App4th at p. 310.) Whereas "in allocating a tax credit, the state parts with nothing of any realizable monetary worth," in accepting allocation of well abandonment and other operational costs in the calculation process, City parts with something of realizable monetary worth. (*Id.*, at p. 311.) Based on the reduction of the sales proceeds in the amount equal to costs allocated to City, the Project is paid for in part out of public funds in the form of payment of money or the equivalent of money within the meaning of subdivision (b)(1).

Oxy and City deny the Project is a public work, and, instead, characterize the arrangement as a lease under which City receives royalties. A lease, however, can form the basis for a public work. (See, e.g., *Oxbow Carbon & Minerals, LLC v. Dept. of Industrial Relations* (2011) 194 Cal.App.4th 538, 543.) The arrangement may include royalties, but as seen in *Vickers*, City is not a mere royalty interest holder but a working interest owner with "rights to drill for, develop, and produce gas and oil...." (*Vickers, supra*, 55 Cal.2d at pp. 156-157.) In any event, the fact that royalties are involved does not deflect the need to follow the statute and ascertain if construction and installation work is being done under contract, paid for in whole or in part out of public funds. Nothing in the PWL specifically carves out an exception for work meeting the statutory elements on the basis of royalty payments associated with that work.

Public Resources Code section 6879 provides that grantees of tide and submerged lands of the state may enter agreements that fix "the time location and manner of drilling and operating of wells for the production of oil or gas, or providing for the return or injection of gas, water or other substances into the subsurface for the purpose of storage or the repressuring of such oil or gas field." While the statute does not mention any prevailing wage implications for such agreements, no undue significance should be attached to that omission. As stated as to the low income housing tax credit program considered in *Trades Council*, "[w]e do not think it unduly significant that the

LIHTC program does not have a similar stand-alone directive in its enabling statutes, because such an approach would strip section 1720 of much of any independent utility, and threaten it with desuetude, if not extinction." (*Trades Council, supra*, 162 Cal.App.4th at p. 319.)

For the foregoing reasons, the Project is a public work subject to the prevailing wage requirements of the Labor Code.

I hope this determination satisfactorily answers your inquiry.

Sincerely,

Christine Baker

Christine Baker
Director