

STATE OF CALIFORNIA
DEPARTMENT OF INDUSTRIAL RELATIONS

DECISION ON ADMINISTRATIVE APPEAL

PUBLIC WORKS CASE NO. 2017-002

VIRGIN HOTEL

PUBLIC WORKS CASE NO. 2017-003

KIMPTON HOTEL

PUBLIC WORKS CASE NO. 2017-004

DOWNTOWN REVITALIZATION

CITY OF PALM SPRINGS

I. INTRODUCTION

On August 13, 2018, the Director of Industrial Relations (Department) issued a public works coverage determination (Determination) finding each of the above-referenced projects to be public works subject to California prevailing wage requirements.

On September 18, 2018, Palm Springs Promenade, LLC (Developer) timely filed a notice of appeal of the Determination (Appeal) under Labor Code section 1773.5¹ and requested a hearing pursuant to California Code of Regulations, title 8, section 16002.5. All interested parties were thereafter given an opportunity to provide written legal argument and to submit any additional supporting evidence. Developer and the Center for Contract Compliance (Requester) timely submitted argument and evidence.

¹ Unless otherwise indicated, all further statutory references are to the California Labor Code and all subdivision references are to the subdivisions of section 1720.

Although the City of Palm Springs (City) was provided an opportunity to do so, the City did not submit a brief on appeal.²

On December 2, 2021, the City provided, through its City Attorney, an analysis of the applicability of one of the City's municipal ordinances in response to a request by the Department, as did Developer, which filed a separate response. The City Attorney's analysis of the City's municipal ordinances suggests the City believes the projects were not subject to prevailing wages.

The Director has sole discretion to decide whether to hold a hearing. (Cal. Code Regs., tit. 8, § 16002.5, subd. (b).) The Director reviewed Developer's substantive notice of appeal, opening brief, reply brief, and supplemental brief as well as over 1,000 pages of documents.³ Because the Director is able to ascertain the undisputed material facts from the documents submitted, the request for a hearing is denied.

All of the submissions have been reviewed in detail and given careful consideration. For the reasons set forth in the Determination, which is incorporated into this Decision on Administrative Appeal (Decision on Appeal), and for the additional reasons set forth and discussed in detail below, the Appeal is denied and the Determination is affirmed.

II. RELEVANT FACTS

Due to the detailed factual circumstances and procedural history, a recitation of the factual background is provided here for context. Any additional facts provided for the first time on appeal are also recited below.

² The City had also declined to submit a position statement in the underlying coverage determination.

³ Developer's briefing raised a concern regarding whether the Department had reviewed documents from an FTP (file transfer protocol) site that Developer had initially submitted without claiming privilege, and later refused to show to the Requester. In its February 5, 2021 supplemental brief, Developer admits that these documents can be shown to the Requester. They have now been reviewed by the Department.

A. The Charter City Ordinance

Prior to December 31, 2014, the City, which is a charter city, had a municipal ordinance which read: “Contracts for public projects, as defined in Section 1720 of the Labor Code, shall not be subject to prevailing wage law (Labor Code Section 1770 et. seq.) . . . Any notice inviting bids for such public projects shall include notification of this Subsection.” (former Palm Springs Mun. Code, § 7.06.030, subd. (1).) However, that former municipal code section did not apply to “financial participation agreements; owner participation agreements; disposition and development agreements; development agreements; real estate purchase or lease agreements; covenants, easements; encroachment agreements; memoranda of understanding; or other similar agreements,” which are not procured through the traditional bidding procedure. (Palm Springs Mun. Code, § 7.01.030, subd. (6).) After December 31, 2014, section 7.06.030 of the Palm Springs Municipal Code (currently renumbered as section 7.06.020) was amended to require the payment of prevailing wage where required by state law.⁴

B. The Direct Payments of Public Funds

On December 2, 2009, the City and the Palm Springs Redevelopment Agency approved the Museum Market Specific Plan to remove a blighted shopping mall in downtown Palm Springs and to turn the area into five city blocks of retail, housing, and hotels. (See Staff Report, July 20, 2011, at p. 4.)

On September 29, 2011, the City and Developer entered into a Project Finance Agreement (PFA) to effectuate the goals of the Museum Market Specific Plan. (PFA, Sept. 29, 2011 at p. 1.) The PFA was also motivated by the report of a third-party consultant, Keyser Marston Associates, Inc. (KMA), which had concluded that “\$40 to \$45 million dollars in public participation would be necessary to fund the project.” (*Ibid.*) Specifically, the KMA analysis “found that, as currently proposed, the project generates approximately 4.8% in return to the Developer on total development costs, compared to the average threshold rate of return in the current investment marketplace, which is in

⁴ According to an October 1, 2014 Staff Report, the City amended its ordinance in response to the Legislature’s adoption of Senate Bill 7 (2013), which prohibits a charter city from receiving or using state funding for public works projects if the city has a charter provision or ordinance that authorizes noncompliance with state prevailing wage laws for projects awarded January 1, 2015 and after. (§ 1782, subd. (f).)

the 9.5% range,” and thus, “the Project is not financially feasible without significant public assistance.” (Staff Report, July 20, 2011, at p. 33 [Attachment No. 5: Project Feasibility Analysis].) The City then agreed to pay to Developer, through the PFA, \$43 million (hereafter \$43 million City Payment). (See PFA, Sept. 29, 2011, at p. 2.) Use of the \$43 million City Payment funds was restricted to “Phase I” construction, which includes the downtown revitalization work described in the operative Museum Market Specific Plan and specifically incorporates the Kimpton Hotel, as stated in the PFA.

The \$43 million City Payment was purportedly given in exchange for “certain property and interests,” described as the “Public Assets.” (See PFA, Sept. 29, 2011, at p. 2.) The PFA defines these Public Assets as two existing parking garages, land under those garages, land for new city streets, and two vacant lots (labelled H-1 and H-2 on the project site map), as well as improvements to these properties such as actual construction of the streets, and repairs and upgrades to the garages.⁵ (*Id.* at pp. 2-3.)

In addition to the Public Assets that were given in exchange for the \$43 million City Payment, the PFA also granted the City the legal right to require Developer to complete all construction on the project, regardless of whether it was deemed “a public asset” or private. This was completed through a combination of several PFA provisions.

First, the PFA required Developer, without additional consideration, to grant the City a Performance Trust Deed “to secure performance of the Developer’s obligations under this Agreement to complete the Private Improvements” as well as the public improvements. (PFA, Sept. 24, 2011, at p. 9.) The Performance Trust Deed required

⁵ There is some dispute about the actual value of the “Public Assets.” In December 2010, the City had the entire project site, including the two existing garages, private and public lots, and land for the streets, appraised. According to a December 15, 2010 Staff Report, the entire site was appraised at \$15.7 million dollars. Developer confirms this \$15 million valuation. (Reply, Jan. 31, 2019, at p. 2.) However, that same month, the City offered to pay \$18 million dollars for the same property. In early 2011, according to the KMA study, the “Public Assets” being contemplated under the PFA were valued at \$20 million dollars by the City and \$32 million dollars by the Developer. (Staff Report, July 20, 2011, at p. 34.) On appeal, the Developer submitted an Appraisal by Michael Scarcella of Capital Realty Analysts, which concluded that the “Public Assets” contemplated by the PFA were worth \$29.9 million dollars as of March 20, 2011. (Summary Appraisal Report, Apr. 8, 2011, at p. 3 [AALRR000433].) As discussed *infra*, the actual value of the assets is irrelevant to the finding of coverage.

Developer to convey to the City title to the entire Museum Market Specific Plan property, including all property on which the Developer was to build private structures. (*Ibid.*) The City would then release title to portions of the land back to Developer once the construction, public and private, on that land had been substantially completed. (*Id.* at p. 10.) The City considered Developer's substantial completion of the private structures, including the Kimpton hotel, to be necessary to obtain release of title under the Performance Trust Deed. (See, e.g., Staff Report, Dec. 14, 2016, at pp. 3-4.) Developer clarified that the City "purchased the Assets under the condition the developer would build a project." (Opening Brief, Nov. 27, 2018, at p. 2.)

Second, to further ensure that Developer could not use funds from the \$43 million City Payment for anything other than this revitalization project, the PFA created public and private improvement escrow accounts. Developer could only take funds from those escrow accounts for qualified construction expenses on Phase I construction. (PFA, Sept. 24, 2011, at pp. 7-8.) Developer made clear that "the City wanted to ensure the project would be started and completed and did not want the developer to use the [City Payment] for personal consumption, but for costs related to Downtown." (Opening Brief, Nov. 27, 2018, at p. 8.) Moreover, according to Developer, "[t]he City insisted that all of the [City Payment] be spent by the Developer to improve adjoining property" under the PFA. (Letter brief Feb. 5, 2021, at p. 4.) As with the Performance Trust Deed, Developer did not receive additional consideration for restricting the use of the \$43 million City Payment funds in this way.

In June 2012, the City deposited the \$43 million City Payment into the public and private improvements escrow accounts pursuant to the PFA. Developer thereafter admits to having used all of the \$43 million City Payment funds for public and private Phase I construction under the PFA. Developer acknowledges using \$13 million of City Payment funds specifically for the construction of the Kimpton Hotel, which was designated as part of Phase I construction under an amendment to the PFA. (See 2nd Amended PFA, Oct. 17, 2012, at p. 3.) Developer submitted extensive documentation on the use of the escrow accounts to pay for Phase I construction.

Along with the \$43 million City Payment, the City reimbursed at least \$230,000 of Developer's "procurement costs," for preconstruction architectural and planning under a

March 31, 2011 Reimbursement Agreement. The City also paid \$3.1 million for change orders relating to the improvements on the public assets under the PFA. In total, the City's direct cash payments stemming from the PFA exceeded \$46 million. With over \$46 million in public funding, Developer separately raised \$68 million in loans and spent an additional \$75 million of its own funds for a total project cost of \$189 million for the Phase I development under the PFA. (See Opening Brief, Nov. 27, 2018, at p. 11.)

C. The Transient Occupancy Tax Covenants

Aside from the payment of public funds as described above, the City entered into two operations covenants with Developer regarding the Kimpton and Virgin Hotels. For the Kimpton Hotel, the covenant provided that the City would continue to collect the transient occupancy tax (TOT)⁶ from Developer, the owner of the hotel property, but would remit to Developer, within 30 days, a payment of public funds in an amount equal to 75 percent of the TOT collected, up to a maximum of \$50 million or 30 years, whichever comes first. (Operations Covenant, Dec. 17, 2014 [Kimpton Hotel], at p.2.) In a resolution adopting the covenant, the City Council found that the "the Hotel Operations Covenant is a method of financing in part the hotel." (City Res. 23706, Nov. 19, 2014, at p. 2.)

For the Virgin Hotel, rather than enter into an original operations covenant, the City transferred to the Virgin Hotel an old operations covenant originally intended for a Marriott Hotel on a different lot. (See City Council Staff report, May 4, 2016, at p. 1.) The terms of the Virgin Hotel Operations Covenant are identical to those of the Marriott and Kimpton Hotels, and the covenant itself appears to be a form agreement. (See *id.* at pp. 6-16.) The Staff Report discussing the transfer of the Marriot Operations Covenant to the Virgin Hotel explains that the purpose of this TOT rebate program is "to help close the gap in financing new hotels" and that "the stream of additional revenue is intended to help fill the financing gap for new hotel projects." (*Id.* at pp. 2-3.) Because the agreements are identical, the same TOT payment-and-rebate arrangement and \$50-million or 30-year cap apply to the Virgin Hotel Operations Covenant. (*Id.* at p. 7.)

⁶ A transient occupancy tax is a tax imposed by a city "on visitors for the privilege of occupancy in hotels located within the city." (*In re Transient Occupancy Tax Cases* (2016) 2 Cal.5th 131, 133.)

Developer reports that it has been receiving payments from the City under these agreements since 2017 and that the City is now requiring prevailing wages for the Virgin Hotel project. (Opening Brief, Nov. 27, 2018, at p. 11; Reply, Jan. 31, 2019, at p. 4.) According to Developer, approximately \$30 million, which represents only a portion of the TOT money received, was returned to the City in a settlement following the indictment of the former Mayor and Developer for bribery related to the procurement of the funds for this overall development.⁷

III. CONTENTIONS ON APPEAL

On appeal, Developer essentially challenges the entirety of the Determination as incorrect and wrongly decided. It is difficult to parse the exact formulation of Developer's arguments and ascriptions of error because Developer's briefs, prepared by its attorney, mix multiple divergent arguments within the same heading, often within the same paragraph, and in no discernible order. Although requested to do so, Developer's briefs do not contain a fact section or any consistent citation to the record.⁸ Many of the arguments invoke Developer's request for a face-to-face ex parte meeting with the

⁷ The trial court later dismissed the indictment against Developer only, but the Court of Appeal recently reversed the trial court's order of dismissal reinstating the indictment. The Supreme Court is currently considering a petition to review the Court of Appeal's decision. (See *People v. Wessman* (Cal. Ct. App., Mar. 4, 2022, No. E076327) 2022 WL 632170, at *5, [nonpub. opn.], review filed (Apr. 12, 2022).) Developer raised the issues of these indictments as support for its argument that the TOT money did not pay for construction because Developer paid the TOT money back to the City after the indictments. The indictments are otherwise irrelevant to this case.

⁸ Developer's briefs also appear to contain wholly irrelevant arguments regarding PW Case No. 2017-014 *Nut Tree – Proposed Sale of Land Within Boundaries of Westrust Nut Tree Project* (Jan. 15, 2018) and *City of El Centro v. Lanier* (2016) 245 Cal.App.4th 1494, decisions that were neither relied upon nor cited in the underlying coverage determination. Developer also discusses the retroactivity of Labor Code section 1782, a statute also not cited or relied upon in the coverage determination. Further, Developer, through its attorney, cites to statements allegedly made at oral argument in appellate cases, but not incorporated into the decision, without citation to a transcript, and cites to statutes by bill number only without any designation of the legislative session or year of publication, all of which further complicate the project of parsing Developer's substantive arguments.

Department or a hearing, for which the Director has sole discretion and has denied based on the strength of the written record as discussed *supra*. (See Cal. Code Regs., tit. 8, § 16002.5, subd. (b).) At several points, Developer raises factual concerns, which, to the extent they were relevant, have been addressed by the summary of facts above and citations have been provided to the source of challenged factual findings in the record.

Putting Developer's arguments in their best light, Developer asserts the following: the project is wholly exempt from state prevailing wage law due to the charter city's home rule authority discussed in *State Building & Construction Trades Council of California v. City of Vista* (2012) 54 Cal.4th 547 (*City of Vista*). If not wholly exempt due to the home rule doctrine, the project is not public works under the exceptions in Labor Code section 1720, subdivisions (c)(2) and (c)(3). If not subject to a statutory exception, the project is not public works because the City did not contribute public funds or contract for construction. The City simply bought assets at arms-length at fair market value, and in fact Developer lost money on the deal. Finally, the TOT Covenants do not constitute public funding because the funds are contingent upon operation of the hotel, are not due until construction is complete, and the City clawed back the TOT payments in settlement following the indictment of the former Mayor and Developer for bribery related to the funding of these projects. The Department considers each of these arguments in the order presented above.

IV. DISCUSSION

A. The City's Home Rule Authority Does Not Apply to the Projects.

1. Application of the City's home rule authority requires a four-part test.

Under the "home rule" doctrine, cities operating under home rule charters have supreme authority as to "municipal affairs," as charter cities have been "specifically authorized by our state Constitution to govern themselves, free of state legislative intrusion, as to those matters deemed municipal affairs." (*City of Vista, supra*, 54 Cal.4th at p. 555; Cal. Const., art. XI, § 5, subd. (a).) This is often referred to as a charter city's "home rule authority." However, this autonomy is not unlimited. Charter cities remain

subject to and controlled by general state laws regardless of the conflicting provisions of their charters where the matters are of “statewide concern.” (*Pacific Tel. & Tel. Co. v. City & Cnty. of San Francisco* (1959) 51 Cal.2d 766, 769 [citations omitted].)

The California Supreme Court in *City of Vista* applied a four-part test for resolving whether a matter falls within the “home rule authority” for charter cities. First, the city ordinance at issue must regulate an activity that can be characterized as a “municipal affair.” Second, there must be an actual conflict between the city ordinance and state law. Third, the state law must address a matter of “statewide concern.” Finally, a court must determine whether the state law is reasonably related to the resolution of that statewide concern and whether it is “narrowly tailored” to “avoid unnecessary interference in local governance.” (*City of Vista, supra*, 54 Cal.4th at p. 556.) If the state law satisfies those criteria, “then the conflicting charter city measure ceases to be a ‘municipal affair.’” (*Ibid.*) Applying the test here, the City’s home rule authority does not apply because the projects do not involve a matter of purely municipal concern.⁹

2. Redevelopment through the PFA was not a purely municipal affair.

In *City of Vista*, the court concluded the fire stations in that case were *purely* municipal affairs because they consisted of: “facilities operated by the city for the benefit of the city’s inhabitants, and . . . [entirely] financed from the city’s own funds.” (*Id.* at p. 559.) The Supreme Court was directly concerned with increased cost to the city, which had the obligation to fund all the expenses due to the direct procurement of the construction. (*Id.* at pp. 561-562 [“the question presented is whether the state can require a charter city to exercise its purchasing power in the construction market . . . while increasing the charter city’s costs.”].) In light of the above, the *City of Vista* court found “no statewide concern has been presented” to overcome the conflict with the local ordinance. (*Id.* at p. 566.)

“Statewide” refers to “all matters of more than local concern and thus includes matters the impact of which is primarily regional rather than truly statewide.” (*Committee of Seven Thousand v. Superior Court* (1988) 45 Cal.3d 491, 505 (COST).) In determining whether a matter implicates statewide concerns, “the rule to be applied is

⁹ In addition, the local ordinance at issue here and the state prevailing wage law do not appear to actually conflict, as discussed below.

not entirely a geographical one. Under certain circumstances, an act relating to property within a city may be of such general concern that local regulation concerning municipal affairs is inapplicable.” (*In re Means* (1939) 14 Cal.2d 254, 259.) Generally speaking, “municipal action which affects persons outside of the municipality becomes to that extent a matter which the state is empowered to prohibit or regulate.” (*COST, supra*, 45 Cal.3d at p. 505.) In addition, “ordinances governing municipal affairs supersede general laws insofar as the latter conflict with the ordinance unless the state has preempted the field.” (*Bellus v. City of Eureka* (1968) 69 Cal.2d 336, 346, but see *Professional Fire Fighters, Inc. v. City of Los Angeles* (1963) 60 Cal.2d 276, 292 [doctrine of state preemption is distinct from, but overlaps with, home rule doctrine].) Even projects that may appear to be municipal affairs cease to be municipal affairs if they “affect matters which are acknowledged to be of statewide concern.” (*City of Santa Clara v. Von Raesfeld* (1970) 3 Cal.3d 239, 246.)

Here, a bona fide issue of statewide concern exists with respect to redevelopment. The City and the Palm Springs Redevelopment Agency approved the Museum Market Specific Plan to remove a blighted shopping mall in downtown Palm Springs and redevelop the area into five city blocks of retail, housing, and hotels. Redevelopment has been held to be an issue of statewide concern. (*Redevelopment Agency v. City of Berkeley* (1978) 80 Cal.App.3d 158, 169.) “A legislative intent to preempt the field of community redevelopment is apparent. The redevelopment of blighted areas was declared to be a governmental function of state concern.” (*Ibid.*) The State’s declared policy is that the “redevelopment of blighted areas . . . are governmental functions of state concern” (Health & Saf. Code, § 33037, subd. (c)) and such redevelopment is “in the interest of the health, safety, and general welfare” of the people of the State. (Health & Saf. Code, §§ 33030, 33035.) The removal of the blighted Desert Fashion Plaza Mall from the downtown area motivated the City to enter into the PFA. (See Staff Report, July 20, 2011, at p.4.)

Moreover, while a statewide concern relating to redevelopment exists here, none of the municipal concerns expressed in the *City of Vista* decision are present. The Phase I project does not provide a basic city service like a fire station, but was initiated to remove blight and to compete with other cities for the tourist trade. (See Staff Report,

July 20, 2011, at p. 4.) To achieve those goals and revitalize downtown, the City invested funds, which would not increase with labor costs, and which were intended to increase the projected rate of return for the private Developer. (PFA, Sept. 29, 2011, at p.1-2; Staff Report, July 20, 2011, at p. 33.) These motivations for redevelopment, as opposed to traditional procurement, are outward-looking and provide an immediate private benefit; they would not have been covered by the statute in *City of Vista*, which exempted non-municipal affairs. And these motivations certainly would not have been supported by the balancing of local and statewide concerns at issue in that case. (*City of Vista, supra*, 54 Cal.4th at pp. 559-560.) The Kimpton Hotel and Phase I projects are simply not equivalent in purpose, scale, or function to the fire station project at issue in *City of Vista*.

Since the Kimpton Hotel and the rest of Phase I received public funding through the PFA for otherwise private development, they would not be considered municipal affairs, and the City's home rule authority does not apply.¹⁰

3. No actual conflict exists between the local ordinance and state law.

The City's home rule authority does not apply in this case for the additional reason that the local anti-prevailing wage ordinance does not appear to conflict with state law. Former Palm Springs Municipal Code section 7.06.030, the source of the anti-prevailing wage ordinance, was contained in Title 7: Procurement and Contracting. That title contains a "Chapter of General Provisions," which includes a section on "Exemptions to provisions of this title." (Palm Springs Mun. Code, § 7.01.030.) Section 7.01.030 plainly states the provisions of Title 7, which the anti-prevailing wage ordinance is a part of, are inapplicable to a whole assortment of public contracts, including "financial participation agreements," "disposition and development

¹⁰ As explained in the Determination, a prior coverage determination reasoned that a project is not a municipal affair where the developer obtains public funds to construct private structures, but the public entity is not a party to the construction contract. (PW 2002-021, *City Place Project – City of Long Beach* at p. 3 n. 4 (Nov. 5, 2002).) The reasoning appeared to be that the public entity is essentially only providing funds and its interest and control over the otherwise private project is fairly circumscribed, such that the public entity is not a party to the construction contract and has few, if any, contractual rights to influence the project. In such a circumstance, finding the construction a "municipal affair" is inappropriate.

agreements,” “development agreements,” “real estate purchase or lease agreements,” and “covenants.” (*Id.*, subd. (6).) The PFA and other agreements between the City and Developer appear to fall into the category agreements to which the anti-prevailing wage ordinance is inapplicable. Similarly, the “Operations Covenants,” which enact the TOT Rebate for the Virgin and Kimpton Hotels are covenants and therefore also specifically exempted from the anti-prevailing wage ordinance at former section 7.06.030. (*Ibid.*)

The City Attorney contends, however, that during the relevant time period, the anti-prevailing wage ordinance “applied to any contract that provided for public funding to private projects” and, “assuming arguendo that the City provided public funding, the funding contracts are therefore subject to [the anti-prevailing wage ordinance] and the projects are not subject to prevailing wages.” The City Attorney insists that the anti-prevailing wage ordinance at former section 7.06.030 “exempts” from the state prevailing wage law any “public projects,” as defined under Labor Code section 1720. If, as the Determination concluded, the projects here fall within section 1720, the City Attorney contends that anti-prevailing wage ordinance *automatically* takes them out of the ambit of the state prevailing wage law, *regardless* of what other local provisions say. This argument goes too far. The exemptions provision in section 7.01.030 would be meaningless if the City Attorney’s interpretation were adopted – section 7.01.030, by its own terms, clearly state that provisions of Title 7, of which former section 7.06.030 is clearly a part, do not apply.

The City Attorney more emphatically argues that the City’s “charter operates not as a grant of power, but as an instrument of limitation and restriction on the exercise of power over all municipal affairs which the city is assumed to possess.” (*City of Grass Valley v. Walkinshaw* (1949) 34 Cal.2d 595, 598–599.) The City’s charter expressly declares that the City’s charter is supreme over all municipal affairs. The City claims that “unless a home rule provision subjects a category of contracts to prevailing wages, the prevailing wage law does not apply to municipal affairs” and concludes that “[b]ecause the City did not, at the time of the subject projects, expressly subject itself to the prevailing wage law, its contracts are not subject to prevailing wages.” This argument, while superficially appealing, presupposes that the projects at issue are municipal affairs. But as discussed above, Phase I and the Virgin Hotel projects are *not*

municipal affairs. Moreover, the interplay between the exemption provision at section 7.01.030 and the anti-prevailing wage ordinance at former section 7.06.030 suggests that the exempted category of contracts is exempt precisely because those types of contracts, when used to fund publicly-funded private development, tend to fall outside the ambit of municipal affairs. And since the projects are not municipal affairs, they are not subject to home rule authority. It is therefore reasonable for the City, through enacting section 7.01.030, to exempt those projects and other non-municipal affairs from the anti-prevailing wage ordinance. Whatever plenary power the City may exercise over municipal affairs clearly does not extend to non-municipal affairs, like the projects at issue here.

Alternatively, the City Attorney further claims that because former section 7.06.030 is a more “specific enactment” it should “govern over section 7.01.030.” The rule of statutory construction the City Attorney appears to be advancing applies only when two statutes are irreconcilable. (*Lopez v. Sony Electronics, Inc.* (2018) 5 Cal.5th 627, 637.) But as discussed above, the two ordinances can reasonably be read together: one provides the rule, the other provides exceptions. Furthermore, it cannot be said which of the two ordinances is the more specific one.

In sum, the local ordinance does not conflict with the state prevailing wage law, and therefore the City’s home rule authority does not apply to the Kimpton Hotel and the rest of the Phase I construction. (See *City of Vista, supra*, 54 Cal.4th at pp. 547, 560.)

4. The effective date of the Virgin Hotel TOT Covenant is May 4, 2016.

While the City’s home rule authority does not apply mostly due to the projects not being municipal affairs, the Virgin Hotel is not subject to the City’s home rule authority for an additional, separate reason: the effective date of the Virgin Hotel TOT Covenant postdates the City’s amendment to repeal its anti-prevailing wage ordinance.

Section 6.1 of the Virgin Hotel TOT Covenant provides that the covenant is to run with the land. (Staff Report, May 4, 2016, at p. 11.) A covenant which runs with the land is attached to, and passes with, that specific piece of land. (See *Monterey/Santa Cruz etc. Trades Council v. Cypress Marina Heights LP* (2011) 191 Cal.App.4th 1500, 1519-1520.) The TOT Covenant allegedly “transferred” to the Virgin Hotel property (Block B-1) was originally attached to an entirely different property for the Marriott Hotel (Block

F). (Staff Report, May 4, 2016, at pp. 1-2.) The “transferred” TOT Covenant is merely a form agreement, and is identical to the Kimpton TOT Covenant.

Rather than being a “transfer” of rights under a covenant attached to Block F (Marriott Hotel), it is more appropriate to describe the transaction as an agreement between the City and Developer to simultaneously end the covenant running with Block F and enter into a new covenant running with Block B-1 on the same terms.¹¹ That would give the Virgin Hotel Covenant an effective date of May 4, 2016. As a result, even had the local anti-prevailing wage ordinance applied to covenants before December 2014, no home rule authority applies to the Virgin Hotel.

B. None of the Cited Statutory Exceptions to Public Works Apply.

Developer contends that the exception under section 1720, subdivision (c)(2) (hereafter section 1720(c)(2)) for otherwise private development projects and the so-called de minimis exception under section 1720, subdivision (c)(3) (hereafter section 1720(c)(3)) apply here. For the reasons explained below, neither exception applies.

1. Section 1720, subdivision (c)(2) does not apply.

Section 1720(c)(2)’s exception “applies if four requirements are met: (1) the public improvement work is required as a condition of regulatory approval; (2) the project is an otherwise private development; (3) the public entity must not contribute more money, or the equivalent of money, to the overall project than is required to construct the public improvement work; and (4) the public entity must not maintain any proprietary interest in the overall project.” (*Azusa Land Partners v. Department of Industrial Relations* (2010) 191 Cal.App.4th 1, 29 (*Azusa Land Partners*).)

For the Phase I construction, in addition to the \$11 million agreed cost of public improvements, the City contributed \$32 million for title to the public assets, and also

¹¹ This is also in keeping with the Department’s benchmark date decisions. (See, e.g., PW Case No. 2018-027, *Former Naval Training Center Development Hotel Project – City of San Diego* (Nov. 25, 2019) [“One recognized exception to the use of the DDA date as the benchmark date in RDA cases is where the modification to an existing agreement changes the project’s character as a public work, such as by introducing or removing the payment of public funds.”] [internal quotations omitted].) Here, the Virgin Hotel site, which was not part of the Phase I construction and had not received any of the City Payment under the PFA, first received public funding through the TOT Covenant on May 4, 2016.

obtained the Performance Trust Deed and escrow guarantees. (See PFA, Sept. 29, 2011.) Without analyzing the other elements, section 1720(c)(2) cannot apply because the third element is not satisfied: the City paid significantly more money than was required for the public improvements.

Application of the section 1720(c)(2) exception likewise fails for the Virgin Hotel project. The City did not require any specific public improvements as a condition of regulatory approval, and Developer made no showing of the relationship of any alleged public improvement costs to the \$50 million TOT Covenant subsidy received.

2. Section 1720, subdivision (c)(3) does not apply.

The relevant version of section 1720(c)(3), which contains the so-called minimis exception, reads as follows:

If the state or a political subdivision reimburses a private developer for costs that would normally be borne by the public, or provides directly or indirectly a public subsidy to a private development project that is *de minimis* in the context of the project, an otherwise private development shall not thereby become subject to this chapter.

(former § 1720, subd (c)(3), italics added.)¹² While no fixed amount was set by statute at the time of these projects, past determinations held public subsidies to be *de minimis* when “the amount of public funds is proportionately small enough in relation to the overall cost of the Project, such that availability of the subsidy does not significantly affect the economic viability of this Project.” (PW 2011-033, *Blue Diamond Agricultural Processing Facility – City of Turlock* (May 9, 2012) (*Blue Diamond*)). The subsidy at issue in *Blue Diamond* was 1.75 percent of the overall project cost.

Using simple arithmetic, the \$43 million City Payment alone would constitute 22.75 percent of Phase I’s overall project cost of approximately \$189 million, well in excess of the 1.75 percent public subsidy found to be *de minimis* in *Blue Diamond*. On the Virgin Hotel project, there has been no showing of overall project costs, but taking the 1.75 percent threshold in *Blue Diamond* as an example, the \$50 million TOT

¹² During the pendency of this request, the Legislature passed Assembly Bill No. 2231 (stats. 2020, ch. 346, § 1) to define when a public subsidy is *de minimis*. The statutory amendment expressly states that it is not applicable to projects advertised for bid or awarded before July 1, 2021 and therefore does not affect this Decision on Appeal.

Covenant subsidy would be de minimis only in relation to a \$2.8 billion hotel project, far exceeding the reasonable cost to develop a Virgin hotel in Palm Springs. In sum, these substantial contributions of public funds “significantly affect the economic viability” of these projects such that they would not be built without the public subsidies.

C. The Phase I Construction Meets the Definition of Public Works in Labor Code Section 1720, Subdivision (a)(1).

Labor Code section 1720, subdivision (a)(1) (hereafter section 1720(a)(1)) defines public works as “construction . . . done under contract and paid for in whole or in part out of public funds.” Payment of public funds includes “the payment of money or the equivalent of money by the state or a political subdivision directly to or on behalf of the public works contractor, subcontractor, or developer.” (§ 1720, subd. (b)(1).) In the present case, the City paid \$43 million plus additional pre-construction costs and change orders to Developer. Those funds came from City coffers and constitute the payment of public funds. (*Ibid.*) Developer admits these funds were in fact used for Phase I construction and provided extensive escrow records demonstrating as much.

In spite of this, Developer repeatedly asserts that these public funds were not for construction, but solely for the purchase of the public assets under the PFA for fair market value. Developer’s “inaccurate and overly simplistic” characterization of the contract was disposed of by the Court of Appeal in *Hensel Phelps Construction Co. v. San Diego Unified Port Dist.* (2011) 197 Cal.App.4th 1020, 1033 (*Hensel Phelps*).¹³ In *Hensel Phelps*, the document signed by the parties was called a “lease,” and the contractor had argued it therefore could not be a contract for construction. (*Ibid.*) The court found that the document “plainly requires construction,” the payments in the

¹³ Developer’s counsel asserts that *Hensel Phelps* is “not binding interpretative precedent on its face” because “the case was settled and not presented to the Supreme Court for review. As a consequence neither regulators nor litigators can as precedent claim [sic] its analysis as controlling.” (Developer’s Reply, Jan. 31, 2019, at p. 2.) This argument borders on the frivolous and must be flatly rejected. According to basic principles of *stare decisis*, published appellate decisions in California bind all lower courts and tribunals, including regulatory and enforcing agencies. (See, e.g., *Auto Equity Sales, Inc. v. Superior Court* (1962) 57 Cal. 2d 450, 455 [“Decisions of every division of the District Courts of Appeal are binding upon all the justice and municipal courts and upon all the superior courts of this state”].)

contract subsidize construction, and therefore meet the requirements of section 1720(a)(1) for “construction . . . done under contract.” (*Id.* at pp. 1033-1034.) Similarly here, although the PFA purports in one section that the \$43 million City Payment is just to acquire title to some public assets and pay for improvements to those assets, the existence of the extensive Performance Trust Deed documentation requiring completion of all private and public work on the project before the City will cede title back to Developer, as well as the escrow requirements dedicating the City Payment funds to construction of the private and public improvements, all for no consideration other than the City Payment, make clear that the PFA “plainly requires construction” and the City Payment funds are intended to subsidize that construction. (See *Id.*; see PFA Sept. 29, 2011.) This conclusion is supported not just by the PFA, but by the KMA analysis and the Staff Reports analyzing the PFA. (See Staff Reports Dec. 15, 2010, July 20, 2011, and attachments.)

Finally, Developer asserts that it must actually turn a profit from public participation in order to be covered by the prevailing wage law. (See Appeal, Sept. 18, 2018 at p. 5 [“Servicing of debt and loan payback will ultimately determine if there will be profit to developer” to show public funding]; Reply Jan. 31, 2019, at p. 3 [Developer argues that the public improvements were not publicly funded because they actually cost \$12.5 million instead of the \$11 million from the City Payment]; Opening Brief at p. 11 [same public improvements alleged to have cost \$13 million].) But the statute simply looks at whether the “three basic elements to a ‘public work’ under section 1720(a)(1)” are satisfied, namely, whether there was “(1) ‘construction, alteration, demolition, installation, or repair work’; (2) that is done under contract; and (3) is paid for in whole or in part out of public funds.” (*Busker v. Wabtec Corporation* (2021) 11 Cal.5th 1147, 1157.) If public funds were contributed, the whole project is covered, unless an exception applies. (See *Azusa Land Partners, supra*, 191 Cal.App.4th at p. 29 [rejecting the developer’s argument that only those portions actually paid for with public funds are covered and holding that “[o]nce the determination is made that the Project is a public work under section 1720, subdivision (a)(1), the entire project is subject to the PWL [prevailing wage law].”]) Developer does not even have to actually show receipt of the funds so long as there is a reasonable inference that it will receive them. (See *Cinema*

West v. Baker (2017) 13 Cal.App.5th 194, 215-216 (*Cinema West*.) As a result, Developer need not walk away with a net profit from public investment for the project to be public works; receipt of public funds for any portion of project construction is sufficient to trigger the application of the statute.

Here, Developer received at least \$46 million dollars that was intended to, and did, finance the cost of public and private Phase I construction. That renders all of Phase I construction covered work within the meaning of the prevailing wage law.

D. The TOT Rebates Are Also Public Funding Within the Meaning of Labor Code Section 1720, Subdivision (b).

The TOT Covenants require the hotel to remit the TOT tax to the City and then obligate the City to provide a rebate to the hotel from funds held in public coffers. (See Operations Covenant, Dec. 17, 2014 [Kimpton Hotel], at p.2; Staff Report, May 4, 2016, [Virgin Covenant] at p. 7.) This type of tax revenue sharing arrangement has been previously determined to constitute a payment of public funds under section 1720, subdivision (b)(1). (See PW Case No. 2018-034, *Great Wolf Lodge – City of Manteca* (Oct. 10, 2019) (*Great Wolf Lodge*.) Because TOT tax revenue sharing requires the hotel to collect the TOT tax from visitors and remit that tax to the public entity, and then obligates the public entity to issue a rebate of a portion of the TOT tax from public coffers back to the hotel, the tax rebates are a form of public funds. (See *Great Wolf Lodge, supra*, at p. 4, citing *Azusa Land Partners, supra*, 191 Cal.App.4th at pp. 23-24.) This is exactly how the TOT Covenants operate in this case.

Further, where the rebate of public funds is meant to subsidize the construction of the project and “serves to reduce a developer’s project costs” overall, it constitutes public funding for the construction on the project. (*Hensel Phelps, supra*, 197 Cal.App.4th at p. 1034.) Payment is not required at the time of construction so long as the effective promise of the funds exists. (See *Cinema West, supra*, 13 Cal.App.5th at p. 216 [finding of public works coverage can be based on facts supporting an inference a developer “will receive the promised amounts” of public funds in future.])

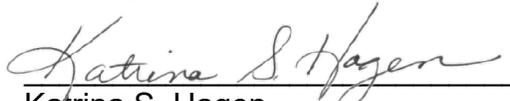
That a portion of TOT tax rebates was clawed back following the indictment of the former Mayor and Developer for bribery related to this project is likewise irrelevant to the coverage analysis. (See Supplemental brief, Feb. 5, 2021, at p. 6.) Developer has

received these funds since 2017 and should have been paying prevailing wage and abiding by the prevailing wage law since the covenants were signed in 2014 and 2016. Allowing a developer to “avoid paying prevailing wages and statutory penalties by repaying or disclaiming the public subsidy” would seriously undermine the prevailing wage law, “discourage voluntary compliance and place undue burdens on the Department's limited enforcement personnel. This cannot have been the Legislature's intent.” (*Cinema West, supra*, 13 Cal.App.5th at p. 216.)

V. CONCLUSION

In summary, for the reasons set forth in the Determination, as supplemented by this Decision on Appeal, the Appeal is denied and the Determination is affirmed. This Decision on Appeal constitutes the final administrative action in this matter.

Dated: 05/23/2022



Katrina S. Hagen
Director of Industrial Relations