

**Office of
The City Attorney
City of San Diego**

**MEMORANDUM
MS 59**

(619) 236-6220

DATE: September 23, 2015

TO: Honorable Mayor and City Councilmembers

FROM: City Attorney

SUBJECT: Applicability of Prevailing Wage Requirements to Third Party Contracts for Construction or Maintenance Work in Business Improvement Districts

INTRODUCTION

The City Council (Council) annually designates a nonprofit business association (Nonprofit) for each business improvement district (BID) to advise the Council on the district budget, assessments, and activities and improvements, and to implement the district under an agreement with the City. On May 13, 2013, the Council approved agreements with each Nonprofit for a five-year term, from July 1, 2013 until June 30, 2018 (Management Agreements). On May 19, 2015, the Council approved a First Amendment to each Management Agreement (First Amendments) in order to improve the efficiency of BID administration, address changes in the San Diego Municipal Code (Municipal Code or SDMC) for contracting and procurement, and address other circumstances pertaining to management of the BIDs.

On June 15, 2015, San Diegans for Open Government (SDOG) filed a complaint setting forth three causes of action against the City and Nonprofits related to the City's BIDs. The third cause of action alleges that the City is in violation of prevailing wage laws because its contractual relationship with the Nonprofits does not include prevailing wage requirements.¹ This Office

¹ In the first cause of action, SDOG challenges the legitimacy of the Fiscal Year 2016 BID assessments under Proposition 26 on the grounds that the levies authorized by the BID resolutions constitute either an illegal "tax" within the meaning of article XIII C, section 1(e) of the California Constitution or an illegal "special tax" within the meaning of San Diego Charter (Charter) section 76.1. The first cause of action is virtually identical to a cause of action that SDOG has initiated against the City in previous complaints filed with respect to BID assessments in earlier fiscal years. In the second cause of action, SDOG alleges that the Nonprofits had an illegal financial interest in the Management Agreements in violation of California Government Code section 1090 and Charter section 94 because each Nonprofit, while acting in the capacity as an advisory board to the City, recommended that the City enter into contracts with the Nonprofit to fund its operations and activities related to the BIDs. The first and second causes of action are outside the scope of this memorandum.

evaluated SDOG's third cause of action and, as discussed further below, concluded that the City is under no legal obligation to include such requirements in the Management Agreements or the First Amendments, and thus its contractual relationship with the Nonprofits does not violate prevailing wage laws. Nonetheless, SDOG's complaint triggers the question of whether the Nonprofits managing the City's BIDs must include prevailing wage requirements in their third party contracts for construction or maintenance work² paid for with BID funds.

QUESTION PRESENTED

Are Nonprofits managing the City's BIDs required to include prevailing wage requirements in their third party contracts for construction or maintenance work paid for with BID funds?

SHORT ANSWER

Yes. Based on existing legal authority, the most reasonable conclusion is that Nonprofits managing the City's BIDs are required to include prevailing wage requirements in their third party contracts for construction or maintenance work paid for with BID funds if the contemplated work will exceed the minimum monetary thresholds in the City's prevailing wage ordinance. Therefore, this Office recommends that the City direct the Nonprofits to comply with prevailing wage laws through either a subsequent amendment to the Management Agreements or a directive issued under the provisions of the Management Agreements. Alternatively, the Council could amend its existing prevailing wage ordinance to waive prevailing wage requirements for the Nonprofits, but this approach could subject the City to the potential loss of substantial State funding on construction projects and subject the City and the Nonprofits to significant liability and penalties.

BACKGROUND

A. State and Local Prevailing Wage Laws

Charter cities, such as San Diego, are not required to pay prevailing wages. *State Bldg. & Constr. Trades Council of Cal., AFL-CIO v. City of Vista*, 54 Cal. 4th 547, 556 (2012). The policy decision whether to pay prevailing wages to workers on locally funded public works projects is a municipal affair and not a matter of statewide concern; thus, charter cities are exempt from State prevailing wage laws. *Id.* at 565-66.

Nevertheless, on October 13, 2013, Governor Brown signed California Senate Bill 7 (SB 7) into law adding section 1782 to the California Labor Code. Under SB 7, charter cities are prohibited from receiving or using state funding or financial assistance on construction projects if the charter city has awarded, within the prior two years, a public works project without requiring

² This memorandum uses the phrase "construction or maintenance work" to characterize the type of work governed by the City's prevailing wage ordinance. For purposes of this memorandum, this phrase refers to work meeting the definition of a "public works" as defined in California Labor Code sections 1720-1743, including construction, alteration, demolition and repair work, and maintenance work, such as tree trimming, brush clearing, and habitat restoration. See City Att'y MOL No. 2013-18 (Nov. 19, 2013) for additional guidance on work governed by the City's prevailing wage ordinance.

compliance with all of the prevailing wage provisions of California Labor Code sections 1770-1784.³ Cal. Lab. Code § 1782(b). California Labor Code sections 1770-1784 impose various obligations⁴ and potential liabilities⁵ upon awarding bodies and hiring parties directly contracting with a contractor for a public works project.

SB 7 exempts from its requirements any contracts for projects of \$25,000 or less for construction work, or projects of \$15,000 or less for alteration, demolition, repair, or maintenance work. *Id.* § 1782(d)(1). SB 7 applies to contracts entered into by charter cities on or after January 1, 2015.

In September 2013, prior to the enactment of SB 7, the Council adopted a prevailing wage ordinance. San Diego Ordinance O-20299 (Sept. 26, 2013); SDMC § 22.3019. The City's prevailing wage ordinance applies to "public works" as defined in California Labor Code sections 1720-1743 and to maintenance contracts. The ordinance states that the City must require compliance with State prevailing wage laws with respect to "contracts and *task orders* awarded, entered into, or extended on or after January 1, 2014 . . . for construction work over \$25,000 and for alteration, demolition, repair or *maintenance* work over \$15,000." *Id.* § 22.3019(a), (c). For purposes of the ordinance, the "City" includes "all boards, agencies, or districts created pursuant to ordinance or resolution of the City Council." *Id.* § 22.3019(b).

B. The City's BIDs and Management Agreements

A BID is a mechanism by which business owners can elect to have assessments levied against their businesses for the purpose of improving business conditions in designated geographic districts. BIDs in the City are districts that are authorized by the Parking and Business Improvement Area Law of 1989, contained in California Streets and Highways Code sections 36500-36551 (BID Act), to promote economic revitalization of older commercial areas and improve the scenic, recreational, and cultural attraction of those areas. Cal. Sts. & High. Code § 36501. The BID Act authorizes BID assessment revenues to be used for physical improvements and activities that benefit the businesses within the district. *Id.* §§ 36510, 36513.⁶

³ This Office has previously opined that SB 7 is probably unconstitutional. City Att'y MOL No. 2013-10 (June 17, 2013). However, the constitutionality of SB 7 is still being litigated.

⁴ These sections in the California Labor Code require an awarding body to: (i) provide electronic notice of the award of a public works project, referred to as a "PWC-100 Form," to the Department of Industrial Relations (DIR) within five days of award (Cal Lab. Code § 1773.3(a)(1)), (ii) require all contractors and subcontractors who bid or work on a public works project to register with the DIR and pay an annual fee (Cal. Lab. Code § 1725.5), (iii) require all contractors and subcontractors to submit certified payrolls directly to the DIR (Cal. Lab. Code § 1771.4(c)(2)(B)), and (iv) include required prevailing wage language in all calls for bids, contracts, and purchase orders for public works projects (Cal. Code of Regs. Title 8 §§ 16421(a)(1) and 16433(b)).

⁵ These sections in the California Labor Code provide that both the awarding body and the hiring party directly contracting with a contractor may be liable for attorneys' fees, penalties, and wage underpayment on projects that are inaccurately designated. Cal. Lab. Code §§ 1726(c)(1), 1784. Moreover, City representatives who willfully violate the California Labor Code may be guilty of a misdemeanor. Cal. Lab. Code § 1777.

⁶ An "improvement" means the acquisition, construction, installation, or maintenance of any tangible property with an estimated useful life of five years or more including, but not limited to, parking facilities, benches, trash receptacles, street lighting, decorations, parks, and fountains. Cal. Sts. & High. Code § 36510. "Activities" mean, but are not limited to, promotion of public events which benefit businesses in the area and which take place on or in public places within the area, furnishing of music in any public place in the area, promotion of tourism within the area, and activities which benefit businesses located and operating in the area. *Id.* § 36513.

In accordance with the BID Act, the Council designates a Nonprofit for each of the City's 18 BIDs.⁷ Annually, as required by the BID Act, the process to approve budget reports and authorize the levy and collection of assessments occurs over two Council meetings. At the first meeting, the BID budget reports are submitted to the Council for approval, along with a resolution of intention to levy and collect the annual assessments and to notice the required public hearing. At the second meeting, the Council holds a public hearing and may confirm the budget reports by adopting a resolution which constitutes the levy of assessments for the fiscal year and authorizes the City's appropriation, expenditure, and transfer of BID funds.

The Management Agreements set forth the terms and conditions related to the management of the BIDs by the Nonprofits.⁸ The First Amendments made minor administrative changes to the Management Agreements.⁹ However, the First Amendments did not expand the scope of work, increase the compensation, or extend the term of the Management Agreements.¹⁰

Based on this Office's preliminary review of the annual budget reports approved by the Council for Fiscal Years 2015 and 2016, it is possible that, during these fiscal years, some of the Nonprofits have performed, or will perform, work funded with BID revenue that exceeds the minimum monetary thresholds in the City's prevailing wage ordinance.

⁷ A total of 17 Nonprofits manage the City's 18 BIDs. The El Cajon Boulevard Business Improvement Association manages both the El Cajon Boulevard Gateway BID and the El Cajon Boulevard Central BID.

⁸ Among other things, the Management Agreements require the Nonprofits to: (i) perform services necessary for the management of the BIDs; (ii) prepare annual budget reports for proposed improvements and activities with estimated costs; (iii) prepare annual reports with goals, accomplishments and expenditures; (iv) comply with all applicable laws, ordinances, regulations, and policies of the federal, state, and local governments; and (v) comply immediately with all directives issued by the City or its authorized representatives under authority of any laws, statutes, ordinances, rules, or regulations. Management Agreements §§ 4.1, 4.2, 15.1.

⁹ Each First Amendment makes the following changes to the Management Agreement: (i) deletes a provision requiring Nonprofits to attend monthly meetings of the San Diego Business Improvement District Council; (ii) modifies Nonprofits' responsibilities regarding monthly and annual reports and posting documents on its website; (iii) modifies provisions regarding the Small Business Enhancement Program; (iv) clarifies that Nonprofits are not required to comply with all provisions of the Management Agreement when using non-public funds; (v) revises Exhibits B1 and B2 to modify monthly reporting requirements and reimbursement procedures; and (vi) revises Exhibit C (the conflict of interest and procurement policy) to clarify that it only applies to BID-associated funds, to require written quotes and pricing, and to require a longer public notice period for bidding projects in excess of \$50,000.

¹⁰ This Office has concluded that the Council's approval of the First Amendments did not trigger a requirement for the City to include prevailing wage requirements in the Management Agreements because the City's prevailing wage ordinance only applies to contracts and task orders "awarded, entered into, or extended on or after January 1, 2014." SDMC § 22.3019(c). The City awarded the Management Agreements in May 2013, over seven months before the City's prevailing wage ordinance became effective. Given that the First Amendments only made minor administrative changes regarding the management of the BIDs and did not extend the duration or increase compensation, they do not constitute contracts "awarded, entered into, or extended on or after January 1, 2014." *Id.* Moreover, even if the First Amendments were subject to this requirement, the Management Agreements comply with the City's prevailing wage ordinance because they require the Nonprofits to comply with all applicable laws, ordinances, regulations, and policies of the federal, state, and local governments, and the Nonprofits are the entities awarding the third party contracts for construction and maintenance work in the BIDs.

ANALYSIS

I. THE NONPROFITS ARE SUBJECT TO THE SAME REQUIREMENTS AS THE CITY UNDER THE CITY'S PREVAILING WAGE ORDINANCE

This Office concludes that the Nonprofits, acting in their management capacity on behalf of the BIDs, fall within the definition of "City" under the City's prevailing wage ordinance. This conclusion is based on both the most reasonable interpretation of SDMC section 22.3019(b) and several practical considerations, as discussed in detail below.

SDMC section 22.3019(b) states that the "City" includes, among other entities, boards or districts created by Council resolution or ordinance. Technically, the Nonprofits are private California nonprofit corporations, not districts created by Council action. However, the respective BIDs managed by the Nonprofits were created by ordinances adopted by the Council.¹¹ Moreover, as part of the annual budget process, the Council adopts a resolution appointing the Nonprofits as the advisory boards for the respective BIDs for the fiscal year. *See* San Diego Resolution R-309669 (Apr. 29, 2015). Given that the Council created the BIDs as assessment districts by ordinance and appointed the Nonprofits as advisory boards for the BIDs by resolution, it is reasonable to conclude that the Nonprofits fall within the definition of "City" in SDMC section 22.3019(b) and are subject to the same requirements as the City under the prevailing wage ordinance.

This conclusion is supported by several practical considerations. First, SB 7 applies not only to charter cities but also to agents and entities controlled by charter cities, presumably to prevent charter cities from avoiding compliance by awarding public works contracts through affiliated entities. Cal. Lab. Code § 1782(d)(2). The Council adopted the City's prevailing wage ordinance to apply in conjunction with SB 7. Thus, for purposes of evaluating compliance with prevailing wage requirements, the Nonprofits could reasonably be considered the City's agents in administering the City's BIDs. Second, State prevailing wage law requires compliance based on the source of funding, not the identity of the person responsible for the work. *See Azusa Land Partners v. Dept. of Industrial Relations*, 191 Cal. App. 4th 1 (2010) (private developer using funds from a community facilities district required to pay prevailing wages). The source of funding for the BIDs is assessments imposed and collected by the City. In light of this City funding source, *Azusa* dictates that the Nonprofits should be subject to the same requirements as the City in entering into new construction or maintenance contracts on or after January 1, 2014. Third, to conclude that the Nonprofits do not meet the definition of "City" would undermine sound public policy because it would allow the City to circumvent its own prevailing wage requirements by using private entities to procure construction or maintenance work exceeding the monetary thresholds in the City's prevailing wage ordinance. This conclusion is also consistent with previous guidance from this Office describing the implications of SB 7 and

¹¹ *See* San Diego Ordinances O-16479 (Jul. 29, 1985), O-16918 (Aug. 3, 1987), O-18263 (Feb. 20, 1996), O-18262 (Feb. 20, 1996), O-10450 (Dec. 1, 1970), O-19881 (Jul. 22, 2009), O-16919 (Aug. 3, 1987), O-16480 (Jul. 29, 1985), O-15647 (Jan. 4, 1982), O-16230 (Jun. 25, 1984), O-17458 (Apr. 16, 1990), O-18374 (Jan. 13, 1997), O-17229 (Jan. 30, 1989), O-16481 (Jul. 29, 1985), O-17248 (Feb. 21, 1989), O-18208 (Sep. 11, 1995), O-18373 (Jan. 13, 1997), O-18612 (Jan. 11, 1999).

opining that the City's prevailing wage ordinance applies to entities responsible for City infrastructure, like BIDs and maintenance assessment districts. 2013 City Att'y MOL 142, 144 (2013-18; Nov. 19, 2013).

The Nonprofits could argue that they do not meet the definition of "City" under a plain reading of the City's prevailing wage ordinance for two reasons. First, the BIDs, not the Nonprofits, were created by ordinance. Second, the Nonprofits are not boards created by resolution. These arguments, however, would not be persuasive. A more reasonable interpretation is that the Nonprofits either constitute a board or a district created by resolution or ordinance or are nonetheless acting as the City's agent in managing the BIDs.

II. THE NONPROFITS ARE REQUIRED TO INCLUDE PREVAILING WAGE REQUIREMENTS IN THIRD PARTY CONTRACTS FOR CONSTRUCTION OR MAINTENANCE WORK AWARDED, ENTERED INTO, OR EXTENDED ON OR AFTER JANUARY 1, 2014

As described above, the Nonprofits fall within the definition of "City" in the City's prevailing wage ordinance and must comply with that ordinance. The ordinance provides that "[f]or contracts and *task orders* awarded, entered into, or extended on or after January 1, 2014, the City shall require compliance with California Labor Code sections 1770-1781 for construction work over \$25,000 and for alteration, demolition, repair or *maintenance* work over \$15,000." SDMC § 22.3019(c). California Labor Code sections 1770-1781 require an awarding body to, among other things, include specified language in its contract documents and bid specifications for any public works project. *See* Cal. Lab. Code § 1771.4.

California Labor Code section 1722 defines an "awarding body" to mean a "department, board, authority, officer *or agent awarding a contract for public work.*" (Emphasis added.) Title 8, section 16000 of the California Code of Regulations defines an "awarding body" to mean "[a]ny state or local government agency, department, board, commission, bureau, district, office, authority, political subdivision, regional district officer, employee, *or agent awarding/letting a contract/purchase order for public works.*" (Emphasis added.)

The Management Agreements provide for the Nonprofits, not the City, to contract with third parties for activities and improvements. As such, the Nonprofits are "awarding" or "letting" contracts, which could include contracts for construction or maintenance. This means that the Nonprofit is the "awarding body" and, effective January 1, 2014, must include specified language in its contract documents and bid specifications for construction or maintenance work that may exceed the monetary thresholds in the City's prevailing wage ordinance.

The Nonprofits could argue that because the Management Agreement does not contain any prevailing wage requirements, the City cannot now require prevailing wages for its third party contracts for construction or maintenance work paid for with BID funds. The crux of this argument would be based on the concept that requiring compliance with prevailing wage requirements that were not expressly stated in the Management Agreement or the First Amendment would constitute an impermissible amendment, by unilaterally imposing new obligations on each Nonprofit. The California Supreme Court has rejected similar arguments in

the prevailing wage context, holding that statutory prevailing wage obligations apply independent of contract provisions and may not be contracted away. *Lusardi Constr. Co. v. Aubry*, 1 Cal. 4th 976, 987-88 (1992). The Court in *Lusardi* reasoned that a contrary conclusion “would encourage awarding bodies and contractors to legally circumvent the law, resulting in payment of less than the prevailing wage to workers on construction projects that would otherwise be deemed public works.” *Id.* at 987-88.

In this instance, prevailing wages do not apply as the result of a negotiated condition agreed to between the parties in the Management Agreement. Instead, prevailing wages apply because the City, in its governmental capacity, enacted a public ordinance making prevailing wage requirements the law locally (*see* Ordinance O-20299; SDMC § 22.3019) in light of the potential penalties under SB 7 (*see* Cal. Lab. Code § 1782). It is a tenet of public contract law that “rights under a so-called ‘public’ contract are subject to further exercise of the power to which they owe their existence.” *Caminetti v. Pac. Mut. Life Ins. Co. of Cal.*, 22 Cal. 2d 344, 362 (1943). When parties enter into contracts with the government, “[i]t is . . . presumed that parties contract in contemplation of the inherent right of the state to exercise unhampered the police power that the sovereign always reserves to itself.” *Delucchi v. Cnty. of Santa Cruz*, 179 Cal. App. 3d 814, 823 (1986). Any argument that prevailing wage requirements must be expressly set forth in the Management Agreement ignores these principles of law, as well as the origin of the City’s prevailing wage requirements.

In any event, a reasonable interpretation of the Management Agreements dictates that the Nonprofits are contractually bound to fulfill the City’s prevailing wage requirements. The Management Agreements require the Nonprofits to comply with “all [applicable] laws, ordinances, regulations, and policies of the federal, state, and local governments” in contracting for activities and improvements. Management Agreement § 15.1. The City’s prevailing wage requirements, even to the extent enacted after execution of the Management Agreements, are binding on the Nonprofits under the Management Agreements because the requirements result from applicable law, statute, and ordinance. Moreover, the Municipal Code and California Labor Code are public laws of general applicability, and the Management Agreement has been and always will be subject to the general laws enacted by the City and the State.

CONCLUSION

The Nonprofits fall within the definition of “City” under the City’s prevailing wage ordinance and, therefore, must include prevailing wage requirements in third party contracts for construction or maintenance work exceeding the monetary thresholds in the City’s prevailing wage ordinance that are awarded, entered into, or extended on or after January 1, 2014. This Office recommends that the City direct the Nonprofits to comply with prevailing wage laws through either a subsequent amendment to the Management Agreements or a directive issued under the provisions of the Management Agreements. Alternatively, the Council could amend its

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prevailing wage ordinance to waive prevailing wage requirements for the Nonprofits, but this approach could subject the City to the potential loss of substantial State funding on construction projects and subject the City and the Nonprofits to significant liability and penalties.

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By /s/ Michael T. Reid

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