

DEPARTMENT OF INDUSTRIAL RELATIONS

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May 27, 2005

Dennis Cook, Esq.
COOK BROWN, LLP
555 Capitol Mall, Suite 425
Sacramento, CA 95814

Re: Public Works Case No. 2004-049
Silverado Creek Family Apartments
Sacramento, California

Dear Mr. Cook:

This constitutes the determination of the Director of Industrial Relations regarding coverage of the above-referenced project under California's prevailing wage laws and is made pursuant to title 8, California Code of Regulations, 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 Silverado Creek Family Apartments Project ("Silverado" or "Project") is not a public work, and therefore is not subject to prevailing wage requirements.

Facts

Silverado Creek Family Apartments, LP ("Developer" is a California limited partnership comprised of USA Properties as its administrative general partner and Riverside Charitable Corporation, a nonprofit public benefit corporation, as the managing general partner. Developer proposes to construct the 168-unit Silverado Creek Family Apartments ("Project"), to consist of 72 very low-income units, 62 low-income units, and 34 market-rate units. As a condition of regulatory agreement between Developer and the Sacramento Housing and Development Agency ("SHRA"), eighty percent (80%) of the units will be restricted for a period of 55 years to individuals or families earning sixty percent (60%) or less of the area median income.

The total cost of construction and permanent financing is estimated to be \$25,564,250. Financing is to come from several sources. First, tax-exempt bonds will be allocated by the California Debt Limit Allocation Committee ("CDLAC" and issued by SHRA in an amount up to \$15,500,000. U.S. Bank has committed to directly purchase these bonds as a private placement transaction and to loan the proceeds to Developer. There will be two series of bonds with a total bond issuance of \$14,270,000, which is below

the maximum of the requested allocation. The Series A-1 Permanent Bonds will be in the amount of \$13,100,000, and will fund a 30-year first mortgage in that amount, at an estimated effective annual rate of 5.3 percent. The Series A-2 Construction Bonds will be in the amount of \$1,270,000, and will be redeemed at permanent loan closing.¹

Second, the SHRA has committed to provide a \$2,200,000 loan from the City Housing Trust Funds for the purpose of financing the development and permanent financing of the Project. The loan will bear an interest rate of 4% per annum, and the unpaid balance will be due and payable 360 months from the date of the note. Principal and interest payments will be deferred for the first 168 months and interest-only payments are required for the next 12 months. Thereafter, unpaid principal and interest will be fully amortized and repaid over the remaining 180 months of the term. All contracts, subcontracts, contractors and subcontractors are subject to SHRA's approval prior to the loan. SHRA also reserves the right to require performance and material bonds or letters of credit, and to review and approve financial statements and other credit information and references prior to closing. The source of the loan funds is an occupancy tax on all apartment units in the City of Sacramento and the County of Sacramento.

Third, the Federal Home Loan Bank of San Francisco will provide an Affordable Housing Program grant of \$456,693. The Federal Home Loan Banks ("Banks") were established pursuant to the Federal Home Loan Bank Act of 1932, 12 U.S.C section 1421 et seq. They are federally chartered but privately owned.² Their mission is to promote the availability of housing financing through more than 8,000 member institutions. They are cooperatives whose stock may be owned only by member institutions such as insured banks, thrifts, credit unions and insurance companies engaged in housing finance.³ The Banks fund themselves principally by issuing consolidated obligations, which are the primary obligation of a sponsoring Bank or Banks, backed by a guarantee of joint-and-several liability of all Banks.

Fourth, Developer will provide a note in the amount of \$1,400,000.

Finally, a limited partner, WNC & Associates, will make an equity contribution of \$8,407,557. This partner will own 99.9% of the Project and will invest its funds in exchange for federal tax

¹ This amount will be repaid out of the equity contribution discussed below, and accordingly is not included in the total cost estimate.

² Letter Of August 31, 1999, from United States General Accounting Office to Rep. Richard H. Baker and Rep. Paul E. Kanjorski.

³ Prepared testimony of John T. Korsmo, Chairman, Federal Housing Finance Board, Before the Subcommittee on Financial Institutions, Senate Committee on Banking, Housing, and Urban Affairs, September 9, 2003.

credits to be allocated by the California Tax Credit Allocation Committee ("CTCAC") in an amount equal to its equity contribution.⁴

Discussion

Labor Code section 1771⁵ generally requires the payment of prevailing wages to workers employed on public works. Section 1720(a)(1) defines public works to include: "Construction, alternation, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds"

The phrase "paid for in whole or in part out of public funds" is defined in detail in section 1720(b), with certain exceptions and exclusions set forth in subdivisions (c) and (d). Section 1720(b)(1) provides that "payment of money or the equivalent of money by the state or political subdivision" constitutes payment out of public funds. Section 1720(b)(4) defines "payment out of public funds" to include:

Fees, costs, rents, insurance or bond premiums, loans, interest rates, or other obligations that would normally be required in the execution of the contract, that are paid, reduced, charged at less than fair market value, waived, or forgiven by the state or political subdivision.

Here, the Project involves construction done under contract. The funding sources that appear to require scrutiny for possible status as payment of public funds include the tax-exempt bonds, the federal tax credits, the SHRA loan, and the grant from the Federal Home Loan Bank.⁶

Tax-exempt bond financing such as that involved here is widely used for multifamily housing projects. There are two basic structures for multifamily housing revenue bonds: Publicly-offered and privately-placed.⁷ A private placement, such as the one at issue here, is in substance a real-estate loan by the

⁴ Additionally, the City of Sacramento and the Sacramento Regional County Sanitation District have committed to waive approximately \$500,000 in development fees and sewer fees related to this project. If DIR determines that the Project is not covered, Owner will decline these waivers. Owner will accept the waivers only if the Project is determined to be covered.

⁵ Subsequent statutory references are to the Labor Code unless otherwise indicated.

⁶ There should be no question that Developer's note and the equity contribution of the limited partner are private funds.

⁷ J. Cooper, *Multifamily Rental Housing: Financing with Tax-Exempt Bonds* (Orrick, Herrington & Sutcliffe LLP, 2003) at 13. Publicly-offered "conduit" bond financing was addressed in PW Case No. 2004-016, Rancho Santa Fe Village Senior Affordable Housing Project (Feb. 25, 2005).

bondholder, here U.S. Bank: "The Borrower/Developer essentially borrows money from a bank or other lender, just as it would if no bonds were issued, but the debt takes the form of a bond transaction in which the lender holds the bonds."⁸ The Bonds are issued by a governmental Issuer (here SHRA), and the proceeds are loaned by the bondholder to the Borrower/Developer.⁹ The Borrower/Developer repays the bondholder pursuant to a loan document.

In such a private placement, the Issuer never has possession of either the bond proceeds or the loan repayments that are made by the borrower to the bondholder.¹⁰ This Department has previously determined that money collected for, or in the coffers of, a public entity is "public funds" within the meaning of section 1720. PW 93-054, Tustin Fire Station (June 28, 1994). Here neither the bond revenues nor the loan repayments ever enter the coffers of a public entity, nor are they collected for the public entity. Since none of the money flows into or out of public coffers, the bond financing is not "the payment of money or the equivalent of money by the state or political subdivision" within the meaning of section 1720(b)(1).¹¹

The Federal tax credits do not, under Section 1720(b)(4), entail any action by the state or a political subdivision. While the tax credits may reduce the Developer's federal income tax obligations, these are not "obligations that would normally be required in the execution of the contract." The execution of the contract entails expenditures by, not income to, the Developer. The tax credits therefore would reduce tax obligations, if any, on income derived from activities other than construction of the housing.¹²

As discussed above, section 1720(b)(1) provides that "payment of money or the equivalent of money by the state or political subdivision" constitutes payment out of public funds. Here the federal tax credits do not entail any payment to the Developer by either the state or a political subdivision. Moreover, a tax credit "involves no expenditure of public moneys received or held ... but merely reduces the taxpayer's liability for total tax due." *Center for Public Interest Law v. Fair Political Practices Commission* (1989) 210 Cal.App.3d 1476. Accordingly, the

⁸ Cooper, *supra* note 7, at 21.

⁹ *Id.* at 22.

¹⁰ *Id.* In PW Case No. 2004-016, *supra* note 7, the same conclusion was reached with respect to publicly-offered "conduit" bonds. While there are structural differences in the two types of bond issues, they are essentially similar insofar as the public entity has no involvement in the cash flow.

¹¹ If bond proceeds in the coffers of a public entity were used to finance construction, such financing would likely fall within the quoted statutory language.

¹² PW Case No. 2-4-016, *supra* note 7

allocation of federal tax credits is not a payment of money or the equivalent of money within the meaning of section 1720(b)(1). As no other provision of section 1720(b) is applicable, the federal tax credits do not constitute payment in whole or in part out of public funds.¹³

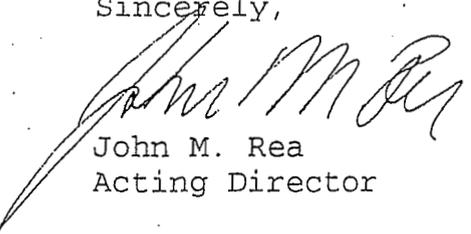
It need not be determined here whether the SHRA loan entails an interest rate "charged at less than fair market value" such that it constitutes payment of public funds within the meaning of section 1720(b)(4). Section 1720(c)(6)(E) provides an exemption for such a loan for a "project in which occupancy of at least 40 percent of the units is restricted for at least 20 years, by deed or regulatory agreement, to individuals or families earning no more than 80 percent of the area median income. Here, by regulatory agreement, occupancy of 80 percent of the units will be restricted for a period of 55 years to tenants earning no more than 60 percent of the area median income. Because these restrictions exceed the requirements of section 1720(c)(6)(E), the exemption set forth therein applies.¹⁴

Finally, as referenced above, the Federal Home Loan Banks are private entities financed by private capital. Accordingly, a grant from such a Bank would not be payment out of public funds within the meaning of section 1720.

Conclusion

For the foregoing reasons, construction of the Project is not paid for in whole or in part out of public funds within the meaning of section 1720, and accordingly is not subject to prevailing wage requirements.

Sincerely,



John M. Rea
Acting Director

¹³ *Id.*

¹⁴ *Id.* Although, as dismissed above, the tax-exempt bond financing does not meet the criteria of section 1720(b), even if it did, section 1720(c)(6)(E) would exempt such financing.