

DEPARTMENT OF INDUSTRIAL RELATIONS

OFFICE OF THE DIRECTOR
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July 19, 2002

Charles M. Taylor
Northern California Carpenters
Regional Council
448 Hegenberger Road
Oakland, CA 94621-1418

Re: Public Works Case No. 2001-043
Capitol Park Homes
City of Sacramento Redevelopment Agency

Dear Mr. Taylor:

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 construction of Capitol Park Homes ("Project") is a public work subject to the payment of prevailing wages.

This Project involves the construction of 64 single-family townhouses in the City of Sacramento, and was initiated by the Redevelopment Agency of the City of Sacramento ("Agency"). The Project is part of the Agency's effort to provide affordable housing in central Sacramento. The developer is the Shasta/Downtown Sacramento Venture Single Family Development LLC ("Developer").

An Agency Staff Report dated September 10, 1998 analyzed the proposed Project and recommended that the Agency assist the Developer by providing a forgivable loan of \$2 million. The Staff Report notes "the entire principal amount of the \$2 million must be forgiven in order to make this project feasible. If home sales escalate to the maximum allowable prices (110 percent of median) then the Agency will receive \$266,519 as repayment on the loan, with the balance being forgiven." Acting upon this recommendation, the Agency adopted a resolution authorizing the transfer of \$2 million to the Developer pursuant to Owner Participation Agreement ("OPA") "to ensure proper repayment and/or forgiveness of Agency funds."

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On October 23, 1998, Developer and Agency entered into an OPA. In Section 3 of the OPA, the Agency and the Developer recite that:

[C]onstruction of the Project on the Site is a private work of improvement, no federal funds are being used and the Project shall not be subject to any state or federal prevailing wage laws and regulations.

Exhibit "2" to the OPA sets forth the costs and sources of funding for the Project. Total costs, from land acquisition to sales, are calculated at \$12,024,820.¹ Exhibit "8" to the OPA sets forth projected unit prices for the housing to be constructed. The total sales revenue from the sale of all 64 units of the Project is projected to be \$9,952,000.

The Agency "loan" was made to Developer pursuant to a promissory note secured by a deed of trust ("Note").² Of this amount, "a sum not to exceed \$200,000 shall be available for pre-construction costs, and the balance shall be for construction." OPA, Paragraph C, Recitals, October 23, 1998. Other sources of funding included a private construction loan of for \$8,595,84 and Developer equity of \$1,428,976.

The OPA provides:

In the event that the gross sale price for any unit sold by Developer within the Project exceeds the sale price shown for that type of unit in the Projected Unit Prices, Developer shall make payments to the Agency as provided in Section 2 of the Note.

Section 2 of the Note provides that net proceeds from the sale of the housing units will be distributed to the Developer to repay

¹ The real property underlying the Project was sold to the Developer by the Capitol Area Development Authority ("CADA") for \$800,000 pursuant to a Disposition and Development Agreement ("DDA") and a Promissory Note. The financial instruments between the Agency and the Developer with respect to the "loan" described in this determination letter are subordinated to the DDA and the CADA note governing the Developer's purchase of the property.

² The initial Promissory Note, executed October 23, 1998, is superseded by a "First Amended and Restated Promissory Note secured by Deed of Trust", dated May 16, 2000. It is the terms of this latter note that are discussed herein.

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the construction loan and cover the Developer's own investment in the Project. Any remaining proceeds are to be distributed among the Developer, CADA and the Agency, with 45 percent of the residual amount, if any, going to the Agency in partial repayment of the loan. (It is the application of this distribution formula that led Agency staff to estimate that the Agency would ultimately be repaid only \$266,519 when the Project was completed.)

Paragraph 2.6 of the Note provides:

[T]he balance of the Principal Amount not repaid to Agency...shall be forgivable upon Borrower's compliance with the terms and conditions of the OPA, and Lender shall forgive the Principal Amount at the rate of 1/64 upon each sale of a residential unit in compliance with the OPA.³

Under what is now Labor Code section 1720(a)(1) (as amended by Statutes 2001, chapter 938, section 2), public works are generally defined as: "Construction, alteration, demolition or repair work done under contract and paid for in whole or in part out of public funds." The Project is construction performed under contract. The issue presented is whether the Project is paid for in whole or in part out of public funds in the form of the \$2 million in financing provided by Agency.

Under title 8, California Code of Regulations, Section 16000, money loaned to a private entity for construction work to be performed under private contract and where no portion of the work is supervised, owned, utilized or managed by an awarding body, is excluded from the definition of public funds.

Implicit in the legal construct of a loan, however, is the obligation to repay. Civil Code, section 1912 defines a loan of money as "a contract by which one delivers a sum of money to another, and the latter agrees to return at a future time a sum equivalent to that which he borrowed." Thus, where a private entity obtains a loan of public monies for a construction project and repays the loan in its entirety, the project is not paid for in whole or in part out of public funds. A "loan" that does not

³ As used in the Note, the term "borrower" refers to the Developer, and the term "lender" refers to the Agency.

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contemplate repayment, however, cannot be considered a bona fide loan.

The loan forgiveness feature of this transaction is a certain outcome of the sale of the housing units in this Project. Although the repayment mechanism of Section 2 of the Note is described in the OPA as a contingency, to be triggered only "in the event" that the gross sales prices exceed the projected unit prices, there is no alternate repayment scheme if this purported contingency fails to occur.⁴ Both the OPA and the Note contemplate forgiveness of the purported loan as the only realistic result of this arrangement.⁵

This holding is consistent with another recent case involving the Sacramento Redevelopment Agency. In Precedential Public Works Coverage Determination Case No. 2000-43, 13th and F Street Townhouse Development, City of Sacramento (December 4, 2001), the construction of a low and moderate-income housing project was funded by Agency "loans" that were forgiven upon the sale of each of the housing units. Because repayment was not contemplated, the determination found that the loan was in the nature of a payment and not exempt from the definition of public funds under the regulation cited above. As such, the loan forgiveness constituted the payment of public funds under Labor Code section 1720(a), and that project was a public work.

In this case the transaction is also in the nature of a payment of public funds. Under the facts of this case, the Agency provided \$2 million to Developer for construction of the Project. The parties entered into a promissory note, which would normally memorialize a loan agreement. However, the OPA and Note together do not contemplate repayment of any more than a tiny fraction of

⁴ The artificially low aggregate projected sales figure of \$9,952,000 is highlighted by the fact that, at the same time this projection was made, the entire cost of the Project was estimated to exceed \$12,000,000. The Developer currently estimates that sales revenue from all 64 units will total \$15,461,00. If this estimate turns out to be correct, gross sales derived from this Project will exceed the projected unit prices by \$5,509,000. Even if the Developer's costs have increased since the Note was signed, it is clear that actual sales will easily exceed the projected sales price in the OPA.

⁵ The entire principal amount of the Note becomes due and payable only if Developer is in default of its obligations under the OPA included documents. As of May 15, 2002, the Developer has already closed on 15 units in the Project. With construction of the Project well underway, and not having been informed of any default, the Department assumes Developer is in compliance.

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the principal amount. Both the OPA and the Note reflect the parties' intent to make a loan that will ultimately be forgiven upon the sale of the housing units involved. For this reason, the \$2 million from Agency to Developer is a payment of public funds.

Because it is funded with public funds, the Project is a public work within the meaning of Labor Code section 1720(a)(1), making it subject to prevailing wage requirements.

I hope this determination satisfactorily answers your inquiry.

Sincerely,

A handwritten signature in cursive script that reads "Stephen J. Smith".

Stephen J. Smith
Director