

STATE OF CALIFORNIA

Arnold Schwarzenegger, Governor

DEPARTMENT OF INDUSTRIAL RELATIONS
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December 5, 2005

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Re: Public Works Case No. 2004-035
Santa Ana Transit Village
City of Santa Ana

Dear Mr. Goetz:

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 California Code of Regulations, title 8, section 16001(a). Based on my review of the facts of this case and an analysis of the applicable law, it is my determination that the construction of the Santa Ana Transit Village ("Project") is a public work subject to the payment of prevailing wages.

The Project involves the construction of 108 attached live-work units within the City of Santa Ana ("City") pursuant to City's Transit Village Plan ("Plan").¹ The Project is being undertaken by Santa Ana Transit Village, LLC ("Developer") under a Disposition and Development Agreement ("DDA") entered into with the Santa Ana Redevelopment Agency ("Agency") on April 19, 2004. The DDA provides that once the 108 units are constructed, the units will be sold at market rates with covenants requiring that a title holder live in each unit and operate a small entrepreneurial or artistic enterprise, consistent with the specific transit village plan for the area.

The Project is being built on five contiguous parcels of land. Developer is purchasing three of the parcels through private sales for \$1,830,000 ("private parcels").² City owned the other two parcels but sold them to Agency for \$2,084,700 to assist the Agency in land assembly for the Project ("public parcels"). One of the public parcels is a vacant parking lot located at 927 Santa Ana Boulevard ("Parcel 927"), and the other is a building of offices and small shops located at 901 Santa Ana Boulevard, which

¹ Government Code sections 65460 et seq., which require cities to develop area-specific transit village plans, set forth the necessary components of a transit village and the funding advantages to a city's public transportation system made possible by construction of such a village.

² Developer represents that the average cost per square-foot of the three separately-sold and differently-priced private parcels is \$16.33.

is currently occupied by Rancho Santiago Community College, whose rent is \$1 per year ("Parcel 901").

Under the DDA, Agency agreed to sell the public parcels to Developer. Prior to the sale, City, Agency and Developer obtained both a fair market value appraisal for each of the public parcels considered separately and a fair reuse value analysis for the two public parcels considered as one, as set forth below.

Fair market value is the value of the land at its highest and best use as determined by a bona fide appraisal. The appraisal determined the highest and best use of Parcel 927 to be its proposed use as live-work units; its fair market value at that use is \$25 per square-foot or \$1,300,000. The highest and best use of Parcel 901, when occupied, was determined to be an "office/shop building," its pre-existing, non-conforming use; its fair market value at that use is \$1,739,800. The highest and best use of Parcel 901, when vacant, was determined to be its proposed use as live-work units; its fair market value at that use is \$35 per square-foot or \$1,708,000.

By contrast, fair reuse value is the value of the land in relation to the covenants and conditions that control its development under the DDA, as determined by a calculation of the development's projected costs, income and profitability. Beatty, *Redevelopment in California* (2004), p. 151. The fair reuse value analysis estimated the projected proceeds from the sale of the 108 units. From that amount, the estimated cost of construction, the expected profit to Developer and the cost of acquiring the private parcels were subtracted. The remainder, \$1,620,000, was deemed to be the fair reuse value of the public parcels, with no differentiation between the two parcels.

As required by Health and Safety Code section 33433, Agency prepared a Report ("33433 Report") describing the disposition and development plan. In the Report, Agency represented the fair market value of the two public parcels to be \$25 per square-foot or \$2,520,000,³ and the fair reuse value of said public parcels to be \$1,620,000.

In the DDA, Agency and Developer set the total purchase price for the public parcels at \$1,620,000. The DDA set the price for

³ The Report does not explain either of the following: (1) Agency's adoption of \$25 per square-foot from the appraisal of Parcel 927, rather than \$35 per square-foot from the appraisal of Parcel 901, as the measure of fair market value of the two public parcels; or (2) Agency's calculation of \$2,500,000 as the fair market value of the public parcels rather than what which was determined by the appraisal - \$3,039,800 (\$1,300,000 for Parcel 927 plus \$1,739,800 for Parcel 901 if occupied) or \$3,008,000 (\$1,300,000 for Parcel 927 plus \$1,739,800 for Parcel 901 if vacant).

Parcel 927 at \$1,300,000, its fair market value. In setting the purchase price for Parcel 901 at \$320,000, Agency and Developer appear to have subtracted the fair market value of Parcel 927 (\$1,300,000) from the fair reuse value of the public parcels (\$1,620,000). The \$320,000 purchase price for Parcel 901 is not based on any methodological measurement of that parcel's value; it does not derive from either the fair market value appraisal or the fair reuse value analysis. Clearly, the parties agreed to a total purchase price equal to the fair reuse value of both parcels and worked backwards from there.

Labor Code section 1720(a)(1) defines a public work in pertinent part as "Construction, alteration, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds"

Labor Code section 1720(b)(3) defines "public funds" to include a "Transfer by the state or political subdivision of an asset of value for less than fair market price." In cases involving the transfer of real property, as here, "we deem 'fair market price' to be synonymous with fair market value." PW 2003-040, *Sierra Business Park/City of Fontana* (January 23, 2004), p. 3.

The Project is construction done under contract. The issue is whether it is being paid for out of public funds. Developer specifically asks whether the proposed sale of the public parcels at \$1,620,000 is a transfer "for less than fair market price" within the meaning of Labor Code section 1720(b)(3). Apart from the transfer of the public parcels to Developer, there are no other potential sources of public funds involved here.

The Director in *Sierra Business Park* left open the question whether fair reuse value is equivalent to fair market price where, for example, "a public agency places restrictions on the use of property that diminish its value to the purchaser." *Sierra Business Park*, *supra*, fn. 6. Because the facts in *Sierra Business Park* did not involve a transfer of property at its fair reuse value, there was no need to answer the question whether such a transfer might constitute a payment of public funds under Labor Code section 1720(b). That question is answered here.

Developer contends that fair market price must necessarily include fair reuse value. According to Developer, the Legislature intended "fair market price" to have a different meaning from "fair market value" and expressed its intention by using these two different phrases in adjacent subsections of Labor Code section 1720(b). Compare Lab. Code, §§ 1720(b)(3) and 1720(b)(4). Developer argues that, had the Legislature intended the payment of public funds to include transfers of property below its fair

market value, it would have used the phrase "fair market value" in Labor Code section 1720(b)(3) and not "fair market price."

The opposite position is advanced by the State Building and Construction Trades Council ("Council").⁴ Council contends that there is no material difference between "fair market value" and "fair market price," and the use of "price" in section 1720(b)(3) is stylistic, not substantive. In support of its position, Council cites to numerous reported decisions, which use the two phrases, "fair market price" and "fair market value" interchangeably.⁵

The legislative history of Labor Code section 1720(b)(3) provides no direct support for either Developer's or Council's view of what the Legislature meant by the phrase "fair market price." Generally, however, Senate Bills 975 and 972, which amended Labor Code section 1720 to expand the definition of public funds, were intended in part to capture the universe of public subsidies given by redevelopment agencies to private developers for their construction projects. A common way in which redevelopment agencies subsidize these projects is through the sale of publicly-owned property, sometimes acquired through the agency's power of eminent domain, to the developer at less than the property's fair market value. *Beatty, supra*, at p. 169. To provide balance in the statutory scheme, in addition to expanding the definition of public funds, the Legislature created several statutory exceptions to the definition of public funds for projects undertaken by private developers (Labor Code section 1720(c)) and numerous exemptions from California prevailing wage law for affordable housing projects (Labor Code section 1720(d)). None of the exceptions or exemptions applies here, and Developer does not argue to the contrary.

Under basic rules of statutory construction, the words of a statute should be given their plain meaning. *Moyer v. Workers' Compensation Appeals Board* (1973) 10 Cal.3d 222, 230. "Fair market value" is a term of art in the appraisal community and generally performed in accordance with the Uniform Standards of Professional Appraisal Standards established by the Appraisal

⁴ Because of the significant issues involved, the Director invited and received comments from interested parties including, among others, the California Redevelopment Association and the State Building and Construction Trades Council.

⁵ It should be noted that, by contrast, there are no reported decisions that use the phrases "fair market price" and "fair reuse value" interchangeably or, for that matter, rely on "fair reuse value" as an accepted concept in land valuation methodology and appraisals.

Institute.⁶ A fair market valuation reflects a property's value "on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available." Code Civ. Proc., § 1263.320; see also, Health & Saf. Code, § 25395.73. The fair market value assumes the purchaser will use the property for its highest and best use consistent with state and local law. For redevelopment projects, highest and best use contemplates a use consistent with the redevelopment plan. See, Health & Saf. Code, § 33433(b)(1). In public works coverage determinations involving the issue of fair market value, the Director will accept a bona fide appraisal performed by an independent and certified appraiser as determinative of fair market value unless credible evidence to the contrary is presented. *Sierra Business Park, supra*, p. 4.

"Fair reuse value" is a term unique to redevelopment projects. It assumes the proposed restrictions in the disposition and development agreement on the use of the property, and thereby distorts the property's value such that a market-based appraisal is not possible; that is, there is no "market" value. Fair reuse valuation is not a generally accepted appraisal method, and the Appraisal Institute does not recognize it as a means of determining market value. The fair reuse value is a speculative figure because it is based entirely on a set of assumptions as to the projected income, costs and profit of the proposed development. A change in one assumption will result in a dramatically different result. In the context of public works coverage determinations, in no section of the Labor Code is the phrase "fair reuse value" anywhere mentioned.

Health and Safety Code section 33433 permits redevelopment agencies to transfer property to private developers for less than the fair market value so long as the transfer is for at least the fair reuse value of the property.⁷ Developer argues that so long as redevelopment agencies comply with Health and Safety Code

⁶ The Appraisal Institute is the appraisal industry's standard-setting professional organization. The Appraisal Institute certifies its most highly trained appraisers with a Masters of Appraisal Institute ("MAI").

⁷ In part, Health and Safety Code section 33433 requires the local redevelopment agency to issue a resolution that contains one of the following findings:

"(1) The consideration is not less than the fair market value at its highest and best use in accordance with the plan.

(2) The consideration is not less than the fair reuse value at the use and with the covenants and conditions and development costs authorized by the sale or lease."

section 33433, a transfer of property by a redevelopment agency to a private developer constitutes a transfer for fair market price within the meaning of Labor Code section 1720(b)(3).⁸ The California Redevelopment Association essentially concedes that under Developer's view no sale of property by a redevelopment agency to a private developer would ever constitute a payment of public funds under California prevailing wage law.

Redevelopment agencies are the exception to the rule that prohibits public entities from selling public property for less than its fair market value; such a transfer would involve an unconstitutional gift of public funds. Cal. Const., art. XVI, § 6. If Developer's arguments under Health and Safety Code section 33433 were accepted, Labor Code section 1720(b)(3) would be rendered a nullity. Basic rules of statutory construction, however, would not countenance such a result. *California Teachers Assn. v. Governing Bd. of Rialto Unified School Dist.* (1997) 14 Cal.4th 627.

In light of the core differences in meaning between "fair market value" and "fair reuse value" and the legislative purpose of Senate Bills 975 and 972 as described above, Developer's interpretation of Labor Code section 1720(b)(3) is untenable. Developer's position would have the Director ignore the word "market" in "fair market price" and accept "fair reuse value" in its place even though the calculation of fair reuse value bears no relationship whatsoever to the market. To read into the concept of "market" a calculation that is subject to mathematical manipulation is not the Director's role. Thus, the resolution of this issue rests on the word "market" in the phrase "fair market price." In order for a transfer to be considered at fair market price within the meaning of Labor Code section 1720(b)(3), there must be evidence that the purchase price is determined by competitive forces in the "market." Here, the purchase price was set below the market value in a private negotiation between the Developer and Agency, not in a competitive market environment.

At the same time, contrary to Council's position, there is a difference between fair market "value" and fair market "price." As mentioned above, fair market value at a property's highest and

⁸ Developer also argues that the average cost per square-foot of the private parcels was \$16.33, only \$.30 per square foot more than the proposed purchase price of the public parcels, which Developer claims is \$16.03 per square-foot. Developer argues that the price to be paid for the public parcels is for all intents and purposes the same as the price paid on the open market for the private parcels and therefore the price for the public parcels is the market price. One of the problems with Developer's argument is that the \$.30 per square foot difference is evidence that the transfer of the public parcels is on its face at a price less than the price of the private parcels and therefore below Developer's own view of the market price.

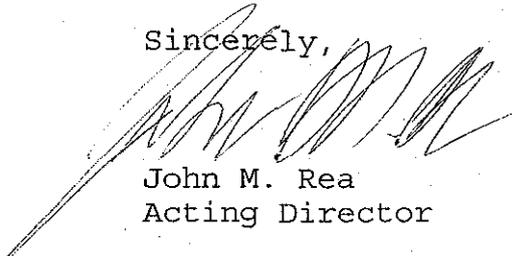
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best use is established by an appraisal. Redevelopment agencies can also examine the market in connection with the sale of a property with additional verifiable use restrictions for purposes of establishing a fair market price. See, Allardice, *When is "Fair Market Price" The Same As "Fair Reuse Value,"* Redevelopment Journal, February 2003, pp. 9, 14. If a 33433 Report demonstrates that the purchase price has been determined based on competitive forces in the market, such as when a restricted property is offered for sale either on the open market or through a request for proposals that results in competitive bidding, such a price may be "fair market price" within the meaning of Labor Code section 1720(b)(3). The facts of this case, however, do not demonstrate that the purchase price of the public parcels was based on any competition in the market. Moreover, the fact that the DDA permits the Developer to develop the property at its highest and best use as live-work units supports the conclusion reached herein that the conditions imposed under the DDA do not diminish the value of the property as determined by the fair market value appraisal and, therefore, under the facts of this case the fair market value, not the fair reuse value, establishes the "fair market price" for purposes of Labor Code section 1720(b)(3).

Accordingly, because the transfer of the public parcels is for less than their fair market price, the transfer constitutes a payment of public funds under Labor Code section 1720(b)(3). As such, the Project is a public work subject to the payment of prevailing wages.

I hope this determination satisfactorily answers your inquiry.

Sincerely,



John M. Rea
Acting Director