STATE OF CALIFORNIA Arnold Schwarzenegger, *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
OFFICE OF THE DIRECTOR
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September 14, 2007

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Re: Public Works Case No. 2006-018
Crossings at Madera Apartments
City of Madera

Dear Mr. Elitzur:

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 Crossings at Madera Apartments ("Project") is not subject to the prevailing wage requirements of the California Labor Code.

Facts

Project consists of four two-story apartment buildings with adjacent recreational and parking facilities. It will include 40 two-bedroom units and 24 three-bedroom units. Pursuant to regulatory agreements, for a period of 55 years, 100 percent of the units (with the exception of the manager's unit) will be rented to residents whose income is equal to or less than 60 percent of the area median gross income.

Project is to be owned by UHC Madera, L.P., a California limited partnership ("Owner"). The partners in this entity are Heritage Community Housing, Inc., a California nonprofit public benefit corporation ("Managing General Partner"); AMTAX Holdings 551 LLC, an Ohio limited liability company ("Investor Limited Partner"); and several other limited partners. Project is to be developed by UHC Madera Development LLC, a California limited liability company ("Developer").

Financing for Project is from a combination of sources. These include (1) a construction and permanent loan ("Bond Loan") funded from the proceeds of tax-exempt low-income housing revenue bonds allocated by the California Debt Limit Allocation Committee ("CDLAC") and issued by the California Statewide Communities Development Authority ("CSCDA") in the aggregate principal amount of $5.75 million; (2) a loan from the Joe Serna, Jr. Farmworker Housing Grant Program of the Department of Housing and Community Development, in the amount of approximately $3 million, with an interest rate of three percent ("Serna Loan"); (3) a loan in the maximum amount of $240,000 with an interest rate of three percent, from the Madera

Redevelopment Agency ("RDA Loan"); and (4) equity investment from Investor Limited Partner, which will be eligible to receive federal Low-Income Housing Tax Credits ("LIHTCs") of $459,541 annually for each of 10 years, pursuant to a reservation by the California Tax Credit Allocation Committee ("CTCAC").

Discussion

Labor Code section 1771[1] generally requires the payment of prevailing wages to workers employed on public works. Section 1720(a)(1) defines public works to include: "Construction, alteration, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds … ." Project clearly will entail construction work done under contract. At issue here is whether Project is "paid for in whole or in part out of public funds" and, if so, whether Project nonetheless enjoys a statutory exemption from prevailing wage requirements. Section 1720(b) provides in pertinent part:

> (b) For purposes of this section, "paid for in whole or in part out of public funds" means all of the following:
> (1) The payment of money or the equivalent of money by the state or political subdivision directly to or on behalf of the public works contractor, subcontractor, or developer.
> (2) Performance of construction work by the state or political subdivision in execution of the project.
> (3) Transfer by the state or political subdivision of an asset of value for less than fair market price.
> (4) 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.
> (5) Money loaned by the state or political subdivision that is to be repaid on a contingent basis.
> (6) Credits that are applied by the state or political subdivision against repayment obligations to the state or political subdivision.

However, section 1720(c) provides that:

> (c) Notwithstanding subdivision (b):
>
> . . .
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> (6) Unless otherwise required by a public funding program, the construction or rehabilitation of privately owned residential projects is not subject to the requirements of this chapter if one or more of the following conditions are met:
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> . . .
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> (E) The public participation in the project that would otherwise meet the criteria of subdivision (b) is public funding in the form of below-market interest rate loans

[1] Subsequent statutory references are to the Labor Code unless otherwise indicated.

> 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.

Regarding the Bond Loan, there are two basic structures for tax-exempt low-income housing revenue bonds: publicly-offered and privately-placed.[2] In the case of publicly-offered bonds such as those involved here, a conduit issuer ("Issuer") issues and sells bonds and, simultaneously with their issuance, assigns all of its rights to the bond proceeds to a private trustee for the bondholders. The bond trustee advances the proceeds to a developer or other private party ("Borrower") to assist in financing the project. The Borrower is contractually bound to make payments to the bond trustee from revenues generated by the project on payment terms that exactly match the terms of repayment of the bonds. Because it assigns all of its rights to a bond trustee, the Issuer never has possession of either the bond proceeds or the loan repayments that are made by the Borrower directly to the bond trustee.

The issue regarding the Bond Loan is whether it involves a payment of public funds. Money collected for, or in the coffers of, a public entity is "public funds."[3] Here neither the conduit bond revenues nor the loan repayments ever enter the coffers of a public entity, nor are they collected for the public entity. As none of the money flows into or out of public coffers, the conduit bond financing is not a payment of public funds within the meaning of section 1720(b).[4]

Additionally, the fact that the Bond Loan is funded by tax-exempt bond proceeds does not mean that a public entity is making a loan at a below-market interest rate for purposes of section 1720(b)(4). Even if the Bond Loan were deemed to be a below-market interest rate loan by a public entity, it would not trigger prevailing wage requirements, where, as here, regulatory agreements meet the requirements for the section 1720(c)(6)(E) exemption.[5]

In contrast, the Serna Loan is being made by the state, and its three percent interest rate is clearly below-market within the meaning of section 1720(b)(4). Due to the restrictions set forth in the regulatory agreements, however, the Serna loan falls within the safe harbor of the exemption set forth in section 1720(c)(6)(E).[6]

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[2] J. Cooper, *Multifamily Rental Housing: Financing with Tax-Exempt Bonds* (Orrick, Herrington & Sutcliffe LLP, 2003) at p. 13.

[3] This is consistent with longstanding Department interpretation. See, e.g., PW 93-054, *Tustin Fire Station* (June 28, 1994).

[4] The analysis in PW 2004-016, *Rancho Santa Fe Village Senior Affordable Housing Project* (February 25, 2005) (*Rancho Santa Fe),* is consistent with the above analysis.

[5] *Rancho Santa Fe, supra*, is also consistent with this conclusion.

[6] Owner points out that the loan principal and accrued interest will be paid out of residual receipts, will come due at the end of its stated term, and is expected to be repaid in full prior to maturity. Therefore, the Serna Loan is not to be repaid on a contingent basis within the meaning of section 1720(b)(5).

The RDA Loan closely resembles the Serna Loan, in that its interest rate is three percent, it is to be repaid out of residual receipts, with full repayment due no later than July 1, 2062, and it is subject to regulatory agreements meeting the requirements of section 1720(c)(6)(E). Accordingly, the RDA Loan also falls within the safe harbor of that exemption.

Regarding the federal LIHTCs, 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 LIHTCs 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 allocation of federal LIHTCs is not a payment of money or the equivalent of money within the meaning of section 1720(b)(1). Additionally, the federal LIHTCs do not entail any action by the state or a political subdivision under section 1720(b)(4). While they 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.[7] As no provision of section 1720(b) is applicable, the federal LIHTCs do not constitute payment in whole or in part out of public funds.

In sum, the Bond Loan and federal LIHTCs do not involve a payment of public funds. Although the Project is paid for in part out of public funds within the meaning of section 1720(b)(4) in the form of the Serna and RDA Loans, these loans are below-market interest rate loans that fall within the safe harbor of section 1720(c)(6)(E). The regulatory agreements impose earnings and occupancy restrictions well in excess of the requirements of section 1720(c)(6)(E) and the exemption set forth therein applies.

For the foregoing reasons, Project is exempt from prevailing wage requirements of the California Labor Code.

I hope this letter satisfactorily responds to your inquiry.

Sincerely,

John C. Duncan

John C. Duncan
Director

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[7] *Rancho Santa Fe, supra,* is consistent with this conclusion.