STATE OF CALIFORNIA EDMUND G. BROWN JR., *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
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To All Interested Parties:

Re: Public Works Case No. 2005-038
Rosedale Project – City of Azusa

The Decision on Administrative Appeal, dated July 2, 2008, in PW 2005-038, *Rosedale Project, City of Azusa*, was affirmed in a published Second District Court of Appeal opinion dated December 21, 2010. See *Azusa Land Partners v. Department of Industrial Relations* (2010) 191 Cal.App.4th 1.

STATE OF CALIFORNIA

DEPARTMENT OF INDUSTRIAL RELATIONS

DECISION ON ADMINISTRATIVE APPEAL

RE: PUBLIC WORKS CASE NO. 2005-038

ROSEDALE PROJECT

CITY OF AZUSA

I. INTRODUCTION

On October 25, 2007, the Director of the Department of Industrial Relations ("Department") issued a public works coverage determination ("Determination") finding that the Rosedale Project ("Rosedale Project" or "Project") is subject to the exemption in Labor Code[1] section 1720(c)(2), which limits the application of prevailing wage requirements to the construction of the public facilities and infrastructure improvements that were required as a condition of regulatory approval of this mixed-use master-planned community development (referred to collectively as "Public Facilities").

Pursuant to California Code of Regulations, title 8, section 16002.5, administrative appeals of the Determination were filed by Azusa Land Partners, LLC ("Developer") on November 21, 2007 and by Southern California Labor/Management Operating Engineers Contract Compliance Committee ("Operating Engineers") on November 26, 2007.

All of the submissions have been considered carefully. Except as noted below, they raise no new issues not already addressed in the Determination. For the reasons set

[1] All statutory references herein are to the Labor Code, unless otherwise specified.

forth in the Determination, which is incorporated herein, and for the additional reasons stated below, the appeals are denied and the Determination is affirmed.

II. CONTENTIONS ON APPEAL

Developer contends that Mello-Roos bond funds are not public funds and therefore the Rosedale Project is not paid for in whole or in part out of public funds under the definition of "public works" in section 1720(a)(1).

Operating Engineers contends that the section 1720(c)(2) exemption does not apply. Characterizing all projects initiated under the Development Agreement Statute, Government Code section 65864, as "public private partnerships," Operating Engineers argues that the Rosedale Project cannot by law be deemed an "otherwise private development project" for purposes of applying the exemption. Purportedly relying on prior public works coverage determinations, Operating Engineers asserts that both the Public Facilities and the "otherwise private" residential and commercial undertakings constitute a single, interdependent and integrated project such that prevailing wage requirements apply to the entire Project, not just the Public Facilities.

Developer also makes an argument under section 1720(c)(2). Developer contends that the Director incorrectly applied the exemption in finding that the Public Facilities as a whole are subject to prevailing wage requirements. Because the Mello-Roos bond funds were insufficient to pay for all of the public facilities and infrastructure improvements required as a condition of regulatory approval of the Project, Developer contends that prevailing wage requirements apply only to those individual facilities and improvements to which Developer allocated the limited funds.

III. DISCUSSION

1. The Payment To Developer Of Mello-Roos Bond Funds Constitutes The Payment Of Public Funds Within The Meaning Of Section 1720(b)(1).

Section 1720(b)(1) defines "paid for in whole or in part out of public funds" as "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." Community Facilities District No. 2005-1 - Rosedale ("CFD") is a political subdivision of the state.[2] It was established as a funding source for the Public Facilities pursuant to the Mello-Roos Community Facilities Act of 1982, Government Code section 53311 et seq. (the "Mello-Roos Act"). The Mello-Roos Act is referred to throughout the statutory scheme as a public financing mechanism. (See, e.g., Gov. Code §§ 53311.5 & 53313.5.) Orrick Herrington's publication, *An Introduction to California Mello-Roos Community Facilities Districts,* summarizes the Mello-Roos funding process as follows:

> Mello-Roos can perhaps best be thought of as a three-part process. Part One involves *defining* a package of proposed governmental powers. Part Two involves *conferring* those powers upon a local legislative body. Part Three involves *exercising* the powers by financing new facilities and/or services.
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> The powers the Act can confer through the formation of a community facilities district ("CFD") are, at the most basic level, the legal authority to levy and collect a special tax, to use that revenue to finance specified facilities and services, and to borrow money (by issuing bonds or incurring other debt) to assist with financing the facilities.

(Bort, *An Introduction to California Mello-Roos Community Facilities Districts* (2006) Orrick, Herrington and Sutcliffe, LLP, p. 3, http://www.orrick.com/fileupload/1180.pdf *(as of June 12, 2008).*)

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[2] Community facilities districts are "defined as 'a legally constituted governmental entity established for the purpose of carrying on specific activities within definitely defined boundaries' (Stats. 1982, ch. 1439, § 1, pp. 5486-5499) empowered to impose special taxes to pay for specified services and facilities within the district." (*Friends of the Library of Monterey Park v. City of Monterey Park* (1989) 211 Cal.App.3d 358, 376.)

Here, the City Manager and Finance Director for the City of Azusa ("City"), acting on behalf of CFD, are authorized to approve payment of Mello-Roos bond funds to Developer in the approximate amount of $71 million[3] for construction of the Public Facilities.[4] Thereafter, the County of Los Angeles ("County") will collect special taxes from property owners within CFD to pay off the bonds. Under the plain meaning of section 1720(b)(1), the payment of Mello-Roos bond funds by CFD to Developer satisfies section 1720(a)(1)'s "paid for in whole or in part out of public funds" requirement.

Contrary to Developer's argument that bond financing is like a regular loan, CFD did not loan money to Developer that Developer was then obligated to repay. Pursuant to the Funding and Acquisition Agreement ("FAA") for the Project, City, on behalf of CFD, agreed to purchase with Mello-Roos bond funds the completed Public Facilities from Developer for the cost of construction. Developer intends to sell the developed parcels to individual property owners who will be required to pay special taxes to County. This tax revenue will be used to pay off the bonds. The bond indebtedness is not being assigned to or assumed by Developer. The obligation for repayment flows with the land. That the bond financing mechanism creates a form of indebtedness does not mean that the payment of Mello-Roos bond funds can be characterized as a loan to Developer.

Developer also compares Mello-Roos bonds to conduit bonds, which were found not to be a payment out of public funds in PW 2004-016, *Rancho Santa Fe Village Senior*

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[3] The Determination stated that the Mello-Roos bond funds totaled $57 million. Developer's subsequent submissions indicate the amount to be approximately $71 million.

[4] City Manager has the right to approve all Developer's costs and expenses to be paid or reimbursed from the Mello-Roos bond funds. City Manager's approval authority includes the right to inspect the Public Facilities in order to ensure compliance with City-approved plans.

Affordable Housing Project (February 25, 2005) ("*Rancho Santa Fe*"). As discussed in *Rancho Santa Fe*, the conduit bond issuer assigns all of its rights to a private bond trustee. Public entities never have possession of either the bond funds or the bond repayments. The bond trustee advances the bond funds to the developer or other private party, referred to as the borrower, who is contractually obligated to make repayments to the bond trustee from revenues generated by the project. The conduit issuer is referred to as such because it is not the true obligor on the bonds. The indebtedness is with the developer. By contrast, here, CFD controls issuance of the Mello-Roos bonds and the indebtedness is paid off with special tax revenue collected by County. As such, Mello-Roos bonds are distinguishable from conduit bonds both in substance and form.

Unlike conduit bonds or a regular loan, Mello-Roos bond financing entails a payment of money by a political subdivision to a developer within the meaning of section 1720(b)(1). Therefore, the Project is a public work under section 1720(a)(1).[5]

2. The Exemption In Section 1720(c)(2) Applies.

Section 1720(c)(2), sets forth the following exemption:

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[5] Because the Project meets the definition of public works under section 1720(a)(1) as construction done under contract and paid for in part out of public funds in the form of Mello-Roos bond funds, it is unnecessary to address Developer's contention that the Project is not paid for out of public funds, but the individual infrastructure improvements and public facilities that were in fact financed with Mello-Roos bonds are subject to prevailing wages under the other definitions of public works in sections 1720(a)(2) and/or (a)(3). It should be noted, however, that the result reached herein would be the same if the facts were analyzed under sections 1720(a)(2) and/or (a)(3). Under section 1720(a)(2), "public works" includes work done for an improvement district. Construction of the Public Facilities as a whole would appear to fall under section 1720(a)(2) because the FAA specifically states that "[a]ny Public Facilities paid by the Developer may be eligible for reimbursement from the proceeds of the Bonds," which are issued by CFD, an improvement district. Under section 1720(a)(3), "public works" includes improvement work done under the direction and supervision or by the authority of a public entity. Construction of the Public Facilities as a whole would appear to fall under section 172)(a)(3) because such construction is required as conditions of approval of the Project pursuant to the Development Agreement, FAA, Mitigation Agreements and Joint Community Facilities Agreements ("JCFA"). In addition, prior to transfer of the Public Facilities from Developer to the controlling public entity, the public entity will make inspections to assure Developer's compliance with its approved plans and specifications.

(c) Notwithstanding subdivision (b): ....

(2) If the state or a political subdivision requires a private developer to perform construction, alteration, demolition, installation, or repair work on a public work of improvement as a condition of regulatory approval of an otherwise private development project, and the state or political subdivision contributes no more money, or the equivalent of money, to the overall project than is required to perform this public improvement work, and the state or political subdivision maintains no proprietary interest in the overall project, then only the public improvement work shall thereby become subject to this chapter.

Operating Engineers' contention that prevailing wages are required for the entire Project is incorrect because it fails to take into account changes to the statutory scheme brought about by passage of Senate Bill 975 (Stats.2001, c. 938, § 2) ("SB 975"), namely the section 1720(c)(2) exemption.[6] Where the elements of the exemption are satisfied, as they are here, only the public work of improvement component of the Project is subject to prevailing wage requirements.

Operating Engineers argues that the "otherwise private development project" element of the section 1720(c)(2) exemption is not satisfied,[7] relying on an offhand reference to the word "partnership" in *Santa Margarita Area Residents Together v. San Luis Obispo County* (2000) 84 Cal.App.4th 221 ("*Santa Margarita*"). That reference is contained in the following passage:

> [I]t is true that local government may not surrender its regulatory power through ad hoc commitments. It may, however, act in partnership with private enterprise, as authorized by the development agreement statute and the Agreement.

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[6] "This bill would provide that certain private residential housing projects and development projects built on private property are not subject to the prevailing wage, hour and discrimination laws that govern employment on public works projects." (Legis. Counsel's Dig., Sen. Bill No. 975, Ch. 938 (2001-2002 Reg. Sess.).)

[7] Operating Engineers does not dispute that the other elements of the exemption are satisfied.

(Id. at p. 233.)

In *Santa Margarita*, a residential neighborhood association challenged the constitutionality of a development agreement between a county and a private developer under which zoning requirements were subject to a freeze during the development process. The court found that a local government may work together with private enterprise as authorized by the Development Agreement Statute, Government Code section 65864, without surrendering its police powers including its ability to regulate land use. That the relationship between the parties in *Santa Margarita* was described as a partnership does not negate the applicability of the section 1720(c)(2) exemption here. As discussed in the Determination, there are no facts to support Operating Engineers' view that the Rosedale Project is anything but an otherwise private development project.

Operating Engineers' reliance on prior coverage determinations such as PW 2000-016, *Vineyard Creek Hotel & Conference Center* (October 16, 2000) ("*Vineyard Creek*") and PW 2004-019, *Strand Redevelopment Project, Redevelopment Agency of the City of Huntington Beach* (June 20, 2005) ("*Strand*") is also misplaced. The issue in this case is not whether there is one project or multiple projects, as it was in those two pre-SB 975 matters. The issue is whether the Public Facilities component of the Rosedale Project is the only work subject to prevailing wage requirements under the section 1720(c)(2) exemption.

Because *Vineyard Creek* and *Strand* arose in a pre-SB 975 setting, the exemption was not a factor in the statutory analysis. In *Strand*, however, the exemption was discussed hypothetically because a party had argued that the post-SB 975 version of section 1720 applied. The exemption was found not to apply. The public improvements

in *Strand* were not required as a condition of regulatory approval. Here, the public improvements were required as a condition of regulatory approval. Also, in *Strand*, the public agency shared in the profits and therefore maintained a proprietary interest in the private commercial development. Here, City has no proprietary interest in the private development. Finally, *Strand* involved the construction of essentially one vertical structure with a subterranean public parking garage acting as the foundation for the private development. Under those facts, the project was considered not to be an "otherwise private development project" within the meaning of section 1720(c)(2).

Strand stated that section 1720(c)(2) "is meant to refer to severable requirements such as the building or improvement of streets or the extension of sewer lines that a public entity might impose on a developer of an otherwise private project ... ." In so stating, *Strand* recognized that section 1720(c)(2) would likely apply to a project such as the Rosedale Project.

Contrary to Operating Engineers' argument, *Strand* is not inconsistent with the result reached here. Under the specific facts of this case, the section 1720(c)(2) exemption applies, and only the Public Facilities component of the Rosedale Project is subject to prevailing wage requirements.

3. The Public Facilities As A Whole Are Subject To Prevailing Wage Requirements.

Developer contends that the section 1720(c)(2) exemption, if applicable, only requires that the individual infrastructure improvements and public facilities actually paid for with Mello-Roos bond funds are subject to prevailing wage requirements. Principles of statutory construction require adherence to the plain meaning of the words in the statute. (See *McIntosh v. Aubry* (1993) 14 Cal.App.4th 1576, 1588 ["To determine the

intent of legislation, we first consult the words themselves, giving them their usual and ordinary meaning."].) The plain meaning of section 1720(c)(2) does not support Developer's contention.

Section 1720(c)(2) applies to public improvement work required as a condition of regulatory approval of a project. The statute requires an analysis of the "money, or the equivalent of money, to the overall project," not to each individual work of improvement. The amount of money or its equivalent contributed to the overall project must not be more than that which "is required to perform this public improvement work." It is undisputed that the Public Facilities were required as a condition of regulatory approval of the Project. It is also undisputed that payment to Developer of approximately $71 million in Mello-Roos bond funds for construction of the Public Facilities is no more than that which is required to do the work. As such, under the plain meaning of section 1720(c)(2), the Public Facilities as a whole are subject to prevailing wage requirements.[8]

Developer's argument that section 1720(c)(2) requires that each public work of improvement required by City be analyzed separately is not supported by any legal authority. Section 1720(c)(2) is intended to immunize the private development, not the public improvement work, from prevailing wage requirements.[9] That the cost of the public improvement work exceeds the amount of the bond issuance is not a mitigating factor in the analysis.

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[8] This analysis is consistent with Civil Code section 3106, which defines "work of improvement" as "... the entire structure or scheme of improvement as a whole."

[9] SB 975 "specifies that projects that require public mitigation such as streetlights or public parks is [sic] not covered, only the public mitigation." (Senate Floor Statement, Sen. Bill No. 975, Concurrence, Prevailing Wages and Public Works (2001-2002 Reg. Sess.) and Sen. Alarcon, sponsor of Sen. Bill No. 975 (2001-2002 Reg. Sess.), letter to Governor, September 7, 2001.)

Developer also argues that the Determination will lead to the absurd result of prevailing wages being triggered on a project in which there has been no payment of public funds because a contribution of zero dollars is "no more money, or the equivalent of money." Developer's concern is unfounded because a payment of nothing by a public entity would never trigger prevailing wages under section 1720(a)(1) in the first instance.

IV. CONCLUSION

In summary, for the reasons set forth in the Determination, as supplemented by this Decision on Administrative Appeal, the appeals are denied and the determination that the Mello-Roos bond financing mechanism entails a payment of public funds; that the Project is an "otherwise private development project" for purposes of applying the section 1720(c)(2) exemption; and that the Public Facilities as a whole are subject to prevailing wage requirements is affirmed. This Decision constitutes final administrative action in this matter.

Dated: 7/2/08

John C. Duncan, Director