STATE OF CALIFORNIA Arnold Schwarzenegger, *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
OFFICE OF THE DIRECTOR
455 Golden Gate Avenue, Tenth Floor
San Francisco, CA 94102
(415) 703-5050

November 5, 2009

Mark Kaiser, Housing Division Manager
City of Fairfield
Community Resources Department
1000 Webster Street
Fairfield, CA 94533-4883

Re: Public Works Case No. 2009-027
Rehabilitation of Single-Family Homes
Neighborhood Stabilization Acquisition/Rehabilitation Program
City of Fairfield

Dear Mr. Kaiser:

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 rehabilitation of single-family homes (the "Project") funded by the federal Neighborhood Stabilization Program (the "NSP") through the City of Fairfield ("City") under the specific facts of this case is not subject to the prevailing wage requirements of the California Labor Code.

Facts

The NSP is authorized under Title III of Division B of the Housing and Economic Recovery Act of 2008 ("HERA"). (Pub.L. No. 110-289 (July 30, 2008) 122 Stat. 2654.) Under the NSP, Congress appropriated $3.92 billion in emergency assistance for the redevelopment of abandoned and foreclosed residential properties. These funds are being awarded to state and/or municipal governments in Community Development Block Grants ("CDBG").

On June 2, 2009, City applied to the California Department of Housing and Community Development ("DHCD") for $2,371,355 from the NSP funds awarded to the state by the federal government. City proposed to use these funds to implement its Neighborhood Stabilization Acquisition/Rehabilitation Program (the "Program"). According to the Request for Developer Proposals dated June 15, 2009, the Project to be undertaken under the Program entails the rehabilitation of foreclosed and vacant single-family homes in substandard condition located throughout targeted neighborhoods[1] within City (the "NSP Property" or "NSP Properties"). The

[1]The NSP Properties must be located within the four CDBG-eligible census tracts numbered 2526.05, 2526.06, 2526.08 and 2526.09. City may expand the Program area to include four additional CDBG-eligible census tracts numbered 2524.02, 2525.01, 2525.02 and 2526.07 if necessary to meet City's goal of stabilizing property values and home ownership rates in neighborhoods impacted by the recent foreclosure crisis.

funds requested by City[2] are to be allocated as follows: 1) $1,852,768 to assist unidentified private developers ("Developer") in the acquisition, rehabilitation and resale of the NSP Properties; and 2) $400,000 to assist approximately eight-to-ten "qualified households"[3] in the purchase of the NSP Properties once rehabilitated. On October 21, 2009, DHCD and City entered into Standard Agreement Number 09-NSP1-6109 in which City was awarded the funds it requested to implement the Program.

From the $1,852,768 allocated to assist in the acquisition, rehabilitation and resale of the NSP Properties, each Developer is to receive up to $350,000 per property in the form of a non-interest bearing loan (the "Acquisition and Rehabilitation Loan").[4] The acquisition price must be discounted by a minimum of one percent[5] from its "current market appraised value"[6]. After the NSP Property has been acquired and rehabilitated by Developer with the proceeds from the Acquisition and Rehabilitation Loan, the rehabilitated NSP Property is then sold to a qualified household. The sales price of the rehabilitated NSP Property is set by City in coordination with Developer based in part on a determination of what the qualified household can afford to pay (the "Affordable Sales Price"). The Affordable Sales Price must be at or below the lesser of the Acquisition and Rehabilitation Loan or the market value.[7]

After sale of the rehabilitated NSP Property to the qualified household, Developer is to repay the Acquisition and Rehabilitation Loan to City. In instances where the Affordable Sales Price is less than the Acquisition and Rehabilitation Loan, City will forgive the difference. Forgiveness allows City to factor affordability into pricing while ensuring that Developer's costs are covered.[8]

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[2]Under the NSP, City is permitted to retain five percent of the NSP funds awarded to cover eligible administrative costs.

[3]City defines "qualified households" as low, moderate or middle income households whose incomes do not exceed 120 percent of the Solano County Median Household Income adjusted for family size, as determined by DHCD. These households are required to receive a minimum of eight hours of homebuyer education from a housing counseling agency certified by the United States Department of Housing and Urban Development ("HUD").

[4]Pursuant to HUD's regulations, Developer may retain a fee not to exceed 10 percent of the Acquisition and Rehabilitation Loan.

[5]HUD initially required that the NSP Property be acquired at a minimum five percent discount. It subsequently changed that amount to one percent. (74 Fed.Reg. 29225 (June 19, 2009).)

[6]HUD defines the term "current market appraised value" to mean "the value of a foreclosed upon home or residential property that is established through an appraisal made in conformity with the appraisal requirements of the URA at 49 CFR 24.103 and completed within 60 days prior to an offer made for the property … ." (74 Fed.Reg. 29226 (June 19, 2009).)

[7]Section 2301, subdivision (d)(3) of HERA states, "SALE OF HOMES. If an abandoned or foreclosed upon home or residential property is purchased, redeveloped, or otherwise sold to an individual as a primary residence, then such sale shall be in an amount equal to or less than the cost to acquire and redevelop or rehabilitate such home or property up to a decent, safe, and habitable condition."

[8]Because there are no other public or private funds involved here, "Developer's costs" is comprised solely of the NSP-funded Acquisition and Rehabilitation Loan.

The $400,000 allocated to assist in the purchase of the rehabilitated NSP Properties is to be used to fund the equivalent of a silent second loan for each qualified household wherein City will carry back the note (the "Affordability Loan").[9] The Affordability Loan bridges the financing gap between the first mortgage obtained by a qualified household from a private lender and the total amount needed to close escrow. City expects the Affordability Loan to range in amount from approximately $15,000 to $40,000. The Affordability Loan bears no interest and is recorded in a way that restricts the NSP Property from being transferred during the "affordability period"[10] except to other qualified households.[11] So long as the qualified household occupies the NSP Property as their primary residence, no payment on the Affordability Loan by the qualified household is required and, at the conclusion of the affordability period, the Affordability Loan will be forgiven in its entirety and the transfer restriction will be lifted.[12]

Discussion

Labor Code section 1771[13] generally requires the payment of prevailing wages to workers employed on public works. Section 1720, subdivision (a)(1)[14] 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 … ." Subdivision (b)(4) defines "paid for in whole or in part out of public funds" to mean "loans … that are paid, reduced, charged at less than fair market value, waived, or forgiven by the state or political subdivision." California Code of Regulations, title 8, section 16001(b) provides: "The application of state prevailing wage rates when higher is required whenever federally funded or assisted projects are controlled or carried out by California awarding bodies of any sort."

Subdivision (c)(6)(C), however, provides an exemption from prevailing wages for projects meeting the following criteria:

> (c) Notwithstanding subdivision (b):
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> …

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[9]The term "silent second" is used here to describe a transaction in which a government or non-profit agency assists home buyers purchasing houses that they could not otherwise afford. The "silence" refers to the absence of a payment burden imposed by the second mortgage. http://www. mtgprofessor.com/silent_second_mortgates.htm.

[10]The affordability period for the Affordability Loan of less than $15,000 is five years; for the Affordability Loan ranging from $15,000 to $40,000, the affordability period is 10 years; and for the Affordability Loan of more than $40,000, the affordability period is 15 years.

[11]Where the NSP Property is sold to another qualified household during the affordability period, the newly qualified household is permitted to assume the Affordability Loan.

[12]On the other hand, full payment of the Affordability Loan would be required if prior to the expiration of the affordability period the NSP Property is no longer used as the principal residence of the qualified household or is sold to a non-qualified household.

[13]All further statutory references are to the California Labor Code unless otherwise indicated.

[14]All further subdivision references are to section 1720.

> (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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> (C) Assistance is provided to a household as either mortgage assistance, downpayment assistance, or for the rehabilitation of a single-family home.

The Project meets the elements of a public work under the above statutory provisions. The NSP Property must be in substandard condition and in need of rehabilitation in order to be eligible for inclusion in the Program. The Project therefore entails construction, alteration, demolition, installation or repair work that is to be performed under contract. City is providing Developer with the Acquisition and Rehabilitation Loan, and the qualified household with the Affordability Loan. Neither the Acquisition and Rehabilitation Loan nor the Affordability Loan bears interest. These below-market interest rate loans are therefore "charged at less than fair market value" within the meaning of subdivision (b)(4) defining "paid for in whole or in part out of public funds."[15] The source of funding is a federal grant. Under the regulation cited above governing federally funded or assisted projects, absent an applicable exemption, California's prevailing wages would apply because the Project is controlled or carried out by City, a California awarding body.

The central issue is whether the Project, which satisfies the elements of a public work as demonstrated above, is nonetheless subject to the statutory exemption set forth in subdivision (c)(6)(C). Because the Project entails the rehabilitation of single-family homes after acquisition of ownership by Developer, the threshold criterion under subdivision (c)(6) is met in that Developer is engaged in the rehabilitation of privately owned residential projects.

The question is whether under the specific statutory exemption in subdivision (c)(6)(C) City is providing assistance "to a household as either mortgage assistance, downpayment assistance, or for the rehabilitation of a single-family home." The Affordability Loan will be provided to a qualified household for the purchase of the rehabilitated NSP Property. Proceeds from the loan make up a portion of the funds necessary to close escrow. Accordingly, the Affordability Loan qualifies as "mortgage assistance" or "downpayment assistance" within the plain meaning of the statutory exemption.

Regarding the Acquisition and Rehabilitation Loan, while provided to Developer, this loan will be used for the acquisition and rehabilitation of the NSP Property. This financing mechanism confers additional assistance to qualified households downstream by ensuring affordability through cost and price controls. Developer must acquire the NSP Property at below "current market appraised value." As confirmed by City, the upfront discount realized at the time of acquisition by Developer is passed on to the qualified household because Developer must sell the rehabilitated NSP Property at a price that does not exceed Developer's costs, including the acquisition cost, which incorporates the value of the discount. Additionally, City intends to forgive that portion of the Acquisition and Rehabilitation Loan that exceeds the Affordable Sales Price to ensure that the

[15]To the extent the conditions for loan forgiveness materialize in any given case, such forgiveness provides a secondary basis for finding that the Project is "paid for in whole or in part out of public funds." (Subd. (b)(4) ["loans … that are … forgiven by the state or political subdivision."].)

Affordable Sales Price is not based entirely on market value or Developer's costs, but instead reflects the financial means of the qualified household. As such, the Affordability Loan and the Acquisition and Rehabilitation Loan are each part of a single scheme of assistance to rehabilitate foreclosed and substandard homes for the ultimate benefit of the qualified household. Accordingly, assistance provided by City in the Acquisition and Rehabilitation Loan and the Affordability Loan constitutes assistance "to a household as either mortgage, downpayment assistance, or for the rehabilitation of a single-family home" within the meaning of subdivision (c)(6)(C).

For the foregoing reasons, based on the specific facts of this case, the Project[16] is exempt from California's prevailing wage requirements under the statutory exemption set forth in subdivision (c)(6)(C).

I hope this determination satisfactorily answers your inquiry.

Sincerely,

John C. Duncan
Director

[16]The Acquisition and Rehabilitation Loan used in combination with the Affordability Loan comprises only one component of the Program. The NSP funds also may be given directly to a household for rehabilitation of their own single-family home, or for mortgage/down payment assistance where no rehabilitation is needed. These other components will be paid for by the reuse of the NSP funds that become available when the Acquisition and Rehabilitation Loans are repaid. City has great flexibility in deciding how to spend this money, but expects to benefit 33 households in total from the original funds and the subsequent reuse of the funds. While City has limited its inquiry to one component of the Program involving the Acquisition and Rehabilitation Loan used in combination with the Affordability Loan, it should be noted that assistance given directly to a household for rehabilitation would likely fall within the exemption in subdivision (c)(6)(C) and assistance given for mortgage/down payment where no construction is contemplated would not be considered a public work.