STATE OF CALIFORNIA Arnold Schwarzenegger, *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
OFFICE OF THE DIRECTOR
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March 10, 2010

Bill Quisenberry, Field Agent
Painters & Allied Trades Compliance Administrative Trust
2333 N. Lake Avenue, Unit 1
Altadena, CA 91001

Re: Public Works Case No. 2009-039
Regency Tower Office Building - Tenant Improvements
County of Riverside District Attorney's Office

Dear Mr. Quisenberry:

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 Regency Tower Office Building (the "Project") is not a public work, with the exception of the tenant improvements. Only the tenant improvement work is subject to the prevailing wage requirements of the California Labor Code.

Facts

The Project entails the construction of a Class A, 10-story, 260,000 square foot office building, including a subterranean parking structure. In January 2007, MS-Regency LLC ("Developer") acquired from the City of Riverside Redevelopment Agency a parcel of land located on Orange Street between 9th and 10th Streets (the "Property") in the City of Riverside ("City"). The Property was purchased at fair market value, as determined by an independent appraiser, pursuant to the Disposition and Development Agreement (the "DDA").

In October 2007, Developer and Snyder Langston LP ("Contractor") entered into the Construction Contract for the Project. Under the terms of the Construction Contract, the basis of payment to Contractor from Developer was the cost of the work plus a fee, with a guaranteed maximum rate.

In January 2008, Contractor commenced construction of the building core and shell. Developer planned to lease office space to private tenants upon completion of the Project. Over the course of the year, however, the weakening economy resulted in reduced demand for office space in the private sector.

In October 2008, during the course of the construction, the County of Riverside ("County") entered into a Purchase and Sale and Joint Escrow Instructions (the "Purchase Agreement") with Developer. Under the terms of the Purchase Agreement, County agreed to purchase the building,

together with easements, appurtenances, improvements and fixtures.[1] The parties further agreed that if County failed to consummate the purchase, County would enter into a 10-year lease of the entire building.

As part of the Purchase Agreement, Developer was required to construct tenant improvements per County specifications. Paragraph 8.1 of the Purchase Agreement states in part: "As part of the purchase price the intent of the parties is to convey a building in turn-key condition, ready for Buyer's occupancy at the close of escrow. ... The Seller will determine the contractor for the Tenant Improvements." Paragraph 8.2 provides:

> As part of the Purchase Price, Seller shall complete and pay all costs associated with the Buyer's approved and required tenant improvements as per the approved plans and specifications which shall be completed and attached hereto as Exhibit D – Tenant Improvement Plans and Specifications. Seller will work with Buyer's Department of Facilities Management to develop construction documents and Buyer will plan check these documents to verify the specifications. ... Seller acknowledges that the purchase price is for a fully completed and finished turn-key building inclusive of the land, building shell, core, tenant improvements, parking and soft costs.

Under the terms of the Purchase Agreement, County made an initial deposit of $10 million. The deposit was placed in escrow. The deposit was fully refundable to County if Developer failed to meet its obligations and the Purchase Agreement was cancelled, or if County failed to consummate the purchase and the parties entered into a lease.

In February 2009, Developer and California Bank & Trust with East West Bank and the Biltmore Bank of Arizona entered into a construction loan agreement (the "Loan Agreement"). Under the terms of the Loan Agreement, Developer agreed to repay the loan proceeds and all associated fees. Moshe and Andrea Silagi, individually and as co-trustees of the Silagi Family Trust, provided a guaranty for repayment of the loan.

In March 2009, Developer and Contractor entered into a separate agreement for construction of tenant improvements. Although the tenant improvements were constructed for the occupancy of the building by County, payment to Contractor was made entirely from the loan proceeds.

On October 16, 2009, City issued a Certificate of Occupancy for the Project. Escrow closed on November 5, 2009. In accordance with the terms of the Purchase Agreement, the parties did not enter into a lease because County consummated the purchase.

County funded the acquisition with tobacco securitization funds. These funds derived from a Master Settlement Agreement (the "MSA") entered into in 1998 between a number of states, including California, and four major tobacco companies. The settlement resolved approximately 40 lawsuits initiated by various states to recover costs associated with medical services for smoking-

[1]The Purchase Agreement also provided for County to purchase 400 condominium parking stalls in a nearby existing parking structure. As these parking stalls did not entail any construction, they are not relevant to this Determination.

related diseases. Under the MSA, the tobacco companies are to provide the settling states with $246 billion over a 25-year period. A number of government entities in California, like those in other settling states, have securitized their share of the settlement proceeds by using the proceeds to service bond debt.[2] The funds used by County to pay the cost of acquisition came from proceeds of bonds issued by the Inland Empire Tobacco Securitization Authority, a joint powers authority.

Discussion

Labor Code section 1771[3] generally requires the payment of prevailing wages to workers employed on public works. There are two potential bases of coverage in this matter. The first basis is under section 1720, subdivision (a)(1), which 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 ... ." Section 1720, subdivision (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.

The second potential basis of coverage is under section 1720.2, which provides that:

> For the limited purposes of Article 2 (commencing with Section 1770) of this chapter, "public works" also means any construction work done under private contract when all of the following conditions exist:
> (a) The construction contract is between private persons.
> (b) The property subject to the construction contract is privately owned, but upon completion of the construction work, more than 50 percent of the assignable square feet of the property is leased to the state or a political subdivision for its use.
> (c) Either of the following conditions exist:

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[2]California Debt and Investment Advisory Commission, *Tobacco Securitization Bond Issuance in California* (June 2009), available at http://www.treasurer.ca.gov/cdiac/reports/tobacco.pdf.

[3]Subsequent section references are to the California Labor Code unless otherwise indicated.

> (1) The lease agreement between the lessor and the state or political subdivision, as lessee, was entered into prior to the construction contract.
>
> (2) The construction work is performed according to plans, specifications, or criteria furnished by the state or political subdivision, and the lease agreement between the lessor and the state or political subdivision, as lessee, is entered into during, or upon completion of, the construction work.

Painters & Allied Trades Compliance Administrative Trust contends that section 1720.2 applies. The first element of that section, a construction contract between private persons, is satisfied, as Developer and Contractor are both private persons. The second element is that the property is privately owned, but upon completion of construction, more than 50 percent of the assignable square feet is leased to a public entity. Here, this element is not satisfied, because the Property is no longer privately owned. Also, County entered into the Purchase Agreement, which is not a lease agreement. As the Property is neither privately owned nor leased to a public entity, section 1720.2 does not apply.

Thus, the Project's public works status turns on the applicability of section 1720, subdivision (a)(1). The Project clearly entails construction done under contract, so the issue is whether construction is "paid for in whole or in part out of public funds" as defined by section 1720, subdivision (b). The only definition that potentially applies is: "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." (§ 1720, subd. (b)(1).)

Citing *State Bldg. and Construction Trades Council of California v. Duncan* (2008) 162 Cal.App.4th 289, 311, Developer contends that a payment out of public funds is signified by the delivery or transfer of money or its equivalent, and that the construction must involve payment of public funds out of a public entity's coffers or otherwise a diminution of the public entity's resources. Developer argues that the construction here did not entail any such payment because initially Developer used its own private funds to fund the construction and, subsequently, the loan proceeds. Developer emphasizes that repayment of the loan was guaranteed by private parties, and not by County; and, even if County had provided a guaranty, a guaranty neither entails a payment by County nor a diminution of County's resources. Thus, concludes Developer, the construction was not paid for out of public funds.

Developer's analysis is essentially correct with regard to the construction of the building core and shell pursuant to the Construction Contract. At the time of the DDA and the Construction Contract, it was contemplated that the Project would be an entirely private development not paid for directly or indirectly out of public funds. The fact that County subsequently entered into the Purchase Agreement does not retroactively convert the construction of the building core and shell into a public work. Accordingly, that work is not subject to prevailing wage requirements.

This reasoning, however, does not extend to the construction of the tenant improvements separately contracted for pursuant to the Purchase Agreement. The plans and specifications for the tenant improvements are attached as an exhibit to the Purchase Agreement, and thus are effectively incorporated into it. The Purchase Agreement contemplates a separate construction contract for the tenant improvements, and expressly states that Developer's costs "associated with the construction

of the Buyer's approved and required tenant improvements" are "part of the Purchase Price." The Purchase Price thus includes consideration for the construction of the tenant improvements required by the Purchase Agreement.

The Purchase Price was paid out of County coffers from tobacco securitization funds, and thus was paid out of public funds. The fact that Contractor was paid by Developer from the construction loan proceeds is immaterial, as the Purchase Price included reimbursement for such costs. The language of section 1720, subdivision (b)(1) defining "paid for in whole or in part out of public funds" to include the "payment of money ... by the state or political subdivision directly to or on behalf of the public works contractor, subcontractor, or developer" is sufficiently broad to include the payment arrangements involved here. Indeed, money was paid by County directly to Developer. Thus, construction of the tenant improvements was paid for out of public funds and is a public work.

For the foregoing reasons, construction of the tenant improvements is a public work subject to prevailing wage requirements. The remainder of the Project is not a public work. I hope this letter satisfactorily responds to your inquiry.

Sincerely,

John C. Duncan
Director