

## DEPARTMENT OF INDUSTRIAL RELATIONS

OFFICE OF THE DIRECTOR

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May 9, 2012

Ofer Elitzur, Esq.  
Cox, Castle & Nicholson  
555 California St., 10<sup>th</sup> Floor  
San Francisco, CA 94104-1513

Re: Public Works Case No. 2011-035  
Residences at Creekside Family Apartments  
Redevelopment Agency of the City of San Marcos

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 Residences at Creekside Family Apartments (Project) is not subject to the prevailing wage requirements of the Labor Code.

### Facts

The Project is an affordable housing development that will be located in San Marcos, California (City). On June 28, 2011, the Redevelopment Agency of the City of San Marcos (Agency) and Southern California Housing Resource & Development, LLC (Developer)<sup>1</sup> executed a Disposition and Development Agreement (DDA) that governs the Project. The Project, a mixed-use complex to be constructed on a 12.43 acre site within the City's central business core, will have two components. One component will be a 98-unit rental apartment complex restricted to occupancy by households at low- and very low-income levels for a period of at least 55 years.<sup>2</sup> The other component will consist of approximately 26,000 square feet of retail space. The Prospective Owner asserts that inclusion of the commercial component of the Project is required by the City's zoning requirements, including the requirement that newly-constructed apartment buildings must provide retail space on the ground floor.

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<sup>1</sup> The Developer has formed a limited partnership, Residences at Creekside Housing Partners, LP (Prospective Owner) as the entity that will assume Developer's contractual obligations in the DDA and take title to the property upon closing. According to the DDA, "closing" refers to the close of escrow for the Developer's acquisition of the site from the Agency, as well as the closing of the Developer's construction financing.

<sup>2</sup> Regulatory agreements to be recorded in the Project's chain of title specify that 10 units will be rented to residents with income no more than 30 percent of area median gross income, 15 units will be rented to residents with no more than 35 percent of area median gross income, 59 units will be rented to those with income no more than 55 percent of area median gross income and 13 units will be occupied by residents with income no more than 60 percent of the area median gross income. One unregulated unit is set aside for a manager.

Four parcels of land comprising the Project site were acquired by the Agency between 2002 and 2010 for a total purchase price of \$11,900,000. The Developer obtained an appraisal concluding that the fair market value of useable acreage within the Project site was \$7.5 million as of May 3, 2011.<sup>3</sup>

Financing for the project comes from the following sources. According to the Prospective Owner, Bank of America will extend to the Developer a conventional construction loan in the amount of \$13,164,741 with an interest rate measured by one month LIBOR plus 2.5 percent.<sup>4</sup> Another source is the Agency's Low and Moderate Income Housing Fund. The Agency will draw up to \$28 million from this fund to make a predevelopment acquisition and construction loan to the Developer (Agency Loan). Of this sum, \$7.5 million is designated the "purchase price tranche" and will carry an interest rate of .25 percent. The remainder of the Agency Loan, up to \$20.5 million, is called the "construction tranche" and will be loaned at an interest rate of 3 percent. The DDA specifies that the "construction tranche" of the Agency Loan must be allocated solely to the costs of constructing the affordable housing component of the Project. The third source of financing consists of Federal low income housing tax credits under section 42 of the Internal Revenue Code of 1986. It is anticipated that tax credit equity will be worth \$3,420,815.

The principal balance of the Agency Loan will be reduced by \$4,539,000 when the Agency purchases the commercial component of the Project per the terms of the DDA. The remaining amount of the Agency Loan will be repaid at a rate derived from a calculation based on cash flow from the Project and will be due and payable in full after 55 years.

### Discussion

Labor Code section 1771<sup>5</sup> generally requires the payment of prevailing wages to workers employed on public works. Section 1720, subdivision (a)(1)<sup>6</sup> 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) provides in relevant part that "paid for in whole or in part out of public funds" means all of the following:

...

(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.

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<sup>3</sup> The appraisal stated that the usable acreage within the Project site is limited to 6.81 acres.

<sup>4</sup> LIBOR is the acronym for London Interbank Offered Rate, generally defined as a benchmark for short-term interest rates reflecting the interest rates charged by banks lending to other banks on the London market.

<sup>5</sup> Subsequent statutory references are to the Labor Code unless otherwise indicated.

<sup>6</sup> Subsequent statutory subdivision references are to section 1720.

...

Subdivision (c), however, provides that:

(c) Notwithstanding subdivision (b):

...

(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:

...

(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 loans 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.

The Project meets the elements of a public work in that the Project involves construction work to be done under contract. As to the funding element, the construction loan from the Bank of America constitutes private rather than public funding. The availability of Federal low income housing tax credits does not constitute "public funds" as the term is used in section 1720. See *State Building and Construction Trades Council v. Duncan* (2008) 162 Cal.App.4<sup>th</sup> 289 (holding that the provision of state low income housing tax credits to the developer of a low-income housing development does not entail the payment of public funds triggering the application of the prevailing wage law.) As to the Agency Loan, the Prospective Owner concedes that this form of financing for the Project is in the form of a below-market interest rate loan. Consequently, the Agency Loan constitutes the payment of public funds under subdivision (b)(4) as a loan "charged at less than fair market value."

Because the Project involves construction work done under contract and the Project is partly paid for with public funds, the payment of prevailing wages ordinarily would be required. The question presented, however, is whether the exemption in subdivision (c)(6)(E) applies. The Prospective Owner argues that the Project qualifies for this exemption.<sup>7</sup>

Subdivision (c)(6) pertains generally to "the construction . . . of privately owned residential projects." Although the Project here will include a commercial component in addition to the residential component, both the Agency and the Prospective Owner assert that the proceeds of the Agency Loan would be allocated only to the construction of the residential component. This assertion is consistent with the provisions of the Health and Safety Code section 33334.3, limiting

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<sup>7</sup> Because it is determined herein that the Project meets the criteria for the exemption from the prevailing wage law provided in subdivision (c)(6)(E), it is not necessary to address the Prospective Owner's other argument that the Project also enjoys the exemption set forth in subdivision (c)(4).

the use of low and moderate income housing funds to the purposes specified therein.<sup>8</sup> In addition, while the commercial component will be owned by the Agency, the residential component of the Project will remain in private hands.<sup>9</sup>

Subdivision (c)(6)(E) goes on to describe an exemption from the prevailing wage law for certain affordable housing projects where the public participation that would otherwise meet the criteria of subdivision (b) is "public funding in the form of below-market interest rate loans." The duration of the regulatory agreements and the income restrictions on future residents of the Project meet the earnings and occupancy criteria of this statutory exemption.<sup>10</sup> The financing for the Project also meets the requirements of this statutory exemption, since there is no public funding for the Project other than the Agency Loan.<sup>11</sup>

For the foregoing reasons, the exemption in subdivision (c)(6)(E) applies, and the Project is not subject to the prevailing wage requirements of the Labor Code.

I hope this determination satisfactorily answers your inquiry.

Sincerely,



Christine Baker  
Director

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<sup>8</sup> For example, see Health and Safety Code section 33334.3 subdivision (a), requiring that such funds "be used for the purposes of increasing and improving the community's supply of low- and moderate-income housing", as well as subdivision (c), requiring that such funds "shall be used to increase, improve, and preserve the supply of low- and moderate-income housing."

<sup>9</sup> This analysis is consistent with PW 2006-002, *Affordable Senior Housing Project, City of Montebello* (March 22, 2006), where it was determined that the exemption set forth in subdivision (c)(4) applied to a mixed-use project involving a commercial component in addition to affordable housing.

<sup>10</sup> The affordability restrictions specified in the Project's regulatory agreements also exceed the requirements set forth in Health and Safety Code sections 33334.2(e)(2) and 33334.3(c) and (f)(1)(A).

<sup>11</sup> The "purchase price tranche" of the Agency Loan is allocated to the Developer's acquisition costs for the Project site. This reflects the fair market value of the land as determined by the Agency pursuant to an appraisal. Absent a contrary credible appraisal, this valuation is presumed to be correct. The Developer's acquisition of the property from the Agency for \$7.5 million, therefore, is not for "less than fair market price" within the meaning of subdivision (b)(3).