STATE OF CALIFORNIA GAVIN NEWSOM, *Governor*

DEPARTMENT OF INDUSTRIAL RELATIONS
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December 30, 2020

Philip C. Monrad,
Leonard Carder, LLP
1999 Harrison Street, Suite 2700
Oakland, California 94612

Re: Public Works Case No. 2020-001
Bentley Estates Housing Project
Housing Authority of Stanislaus County

Dear Mr. Monrad:

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 Labor Code section 1773.5[1] and California Code of Regulations, title 8, section 16001, subdivision (a). Based on my review of the facts of this case and an analysis of the applicable law, it is my determination that the Bentley Estates Housing Project in the City of Waterford is a public work subject to prevailing wage requirements

Facts

The Bentley Estates Housing Project (the Project) is an affordable housing development located at 13601 Bentley Street in the City of Waterford consisting of thirteen single-family homes. The Project is being directly carried out by Great Valley Housing Development Corporation (GVHDC), a California nonprofit corporation, which incorporated in 1999. In June 2015, GVHDC became an "affiliated nonprofit" of the Housing Authority of the County of Stanislaus (Housing Authority), a public entity. Affiliated nonprofit status has resulted in GVHDC and the Housing Authority sharing an address, an administrative staff, and a chief administrator. Based on the responses received by the Department related to this request, the two entities also share legal counsel. Moreover, at least two members of the GVHDC's nine-member board are Housing Authority officers.

On July 7, 2016, the Housing Authority approved a $250,000 loan to GVHDC for the purchase of the land for the Project. The Housing Authority Staff Report discussing this loan describes it as intended for the acquisition of land for an affordable housing development, which will have contingencies that ensure GVHDC will complete the

[1] Unless otherwise indicated, all further statutory references are to the Labor Code.

affordable housing development; otherwise the funding will be due and payable back to the Housing Authority.

The promissory note for the $250,000 land purchase loan, executed by GVHDC's President on August 10, 2016, provides for an annual interest rate of 4 percent over prime, calculated annually. The loan has a repayment period of 30 years with a mandatory 25-year extension if the parties comply with its terms. No interest accrues, nor is any payment due on this loan until 12 months after 50 percent or more of the units in the Project are occupied. Payment thereafter is to be made annually.

The Project has not yet begun construction. By its terms, no interest has yet accrued on the August 10, 2016 loan, nor has GVHDC been required to make any payments in the past four years.

GVHDC's annual payment of 4 percent over prime under the promissory note is contingent upon its "Net Annual Cash Flow," which is defined in the promissory note as all GVHDC's income from the property, minus a credit for all of GVHDC's annual costs in administering, staffing, and maintaining the property, including any property taxes it pays. Further, the total annual payment under the loan is capped at the percentage of the Net Annual Cash Flow, which the $250,000 loan represents in the total amount of other, more junior, private debt assumed by GVHDC for the construction (e.g. if GVHDC takes $1 million in private construction loans, GVHDC must pay a maximum of 25 percent of its net annual cash flow towards the Housing Authority loan in a given year). At the end of the extended term, (a total of 55 years from issuance), the loan is forgiven entirely.

The integrity of the above system of calculations and reductions is assured in the promissory note by granting the Housing Authority the right to approve a certified public accountant to review the annual budget of GVHDC for the property and to review GVHDC's calculation for its annual payment.

The August 9, 2016, Loan Agreement, executed by both GVHDC and the Housing Authority, which accompanies and incorporates the Promissory note, requires GVHDC to use the loan solely for the property, to purchase multiple forms of insurance in the Housing Authority's name for the property, to permit the Housing Authority to inspect the property throughout construction and thereafter, and to provide at least 80 percent of the units to individuals at or below 120 percent of area median income. The Loan Agreement also gives the Housing Authority the right of first refusal on the purchase of the completed project, and entitles the Housing Authority to a $250,000 credit against the proceeds of any sale of the property.

Based on the Development Report from the September 26, 2017, meeting of the Housing Authority Board of Commissioners, a public document, Housing Authority staff performed some preconstruction cleaning on the property shortly after purchase. According to the July 27, 2017, Housing Authority Development Report, Housing Authority staff met with California Affordable Housing Association and the City of Waterford in their official capacity to negotiate the development of the Project.

Positions of the Parties

Northern California Electrical Construction Industry Labor-Management Cooperating Committee (NCECI), which requested the coverage determination, alleges that GVHDC and the Housing Authority are in fact the same entity. Since GVHDC and the Housing Authority share administrative resources, staff, and board members, NCECI alleges that the Housing Authority is in fact the direct developer of the Project and therefore the Project is automatically public works. Further, NCECI alleges that the $250,000 loan is not an arms-length, fair market value loan, but in fact a contingent loan under section 1720, subdivision (b)(5) and therefore public funding. Finally, NCECI alleges that the administrative support and architecture services provided by the Housing Authority to GVHDC constitute either the payment of the equivalent of money or the performance of construction work on the Project resulting in public funding under subdivisions (b)(1) and (b)(2) of section 1720.

GVHDC alleges that the $250,000 loan was in fact an arms-length, market value loan at 4 percent interest per annum, and that it has no plans to request further funding from the Housing Authority. GVHDC further alleges that it used its own architect, HMR Architects, Inc. for the work on this Project. Finally, GVHDC alleges that, since the Housing Authority has not directly paid for any construction or related activity under section 1720, subdivision (a)(1) on the Project, the Project is not paid for with public funds. GVHDC raised no exceptions in response to the Department's request for a position statement.

The Housing Authority similarly alleged that the $250,000 loan was in fact an arms-length, market value loan at 4 percent interest per annum. The Housing Authority also alleges that it has a management agreement with GVHDC to provide business management services for GVHDC on a fee for services and cost incurred basis, but that GVHDC reimburses the Housing Authority for all such services and costs. The Housing Authority provided no documentary evidence to support this alleged reimbursement arrangement. The Housing Authority also raised no exceptions in response to the Department's request for a position statement.

Discussion

All workers employed on public works projects must be paid at least the prevailing wage rates applicable to their work. (§ 1771.) Section 1720, subdivision (a)(1), defines "public works" to mean: construction, alteration, demolition, installation, or repair work done under contract and paid for in whole or in part out of public funds.

The Project is indisputably construction, which will be carried out under contract. The issue for this case under section 1720, subdivision (a)(1) is whether the work is "paid for in whole or in part out of public funds" within the meaning of the prevailing wage law.

A loan from a public entity "that is to be repaid on a contingent basis," such as a forgivable loan, constitutes public funding. (§ 1720, subd. (b)(5); see also *Cinema West, LLC v. Baker* (2017) 13 Cal.App.5th 194, 216.) In the present case, the loan is forgivable on its face; if after 55 years GVHDC is unable to fully repay the principal and accrued interest, the loan is forgiven. This alone makes this loan a contingent repayment obligation and renders the $250,000 loan public funds under section 1720, subdivision (b)(5). The Staff Report accompanying the loan appears correct: this is a contingent repayment obligation where GVHDC must either construct the Project or repay the loan, but it is not expected to fully repay the loan if it completes the Project.

Furthermore, if this were a simple 30-year mortgage for $250,000 at 4 percent over prime, the annual payment would begin right away. However, rather than spell out a repayment schedule of any kind, this promissory note provides that annual repayment does not begin until the buildings on the site reach 50 percent occupancy. This 50 percent occupancy requirement also operates as a contingency to GVHDC's obligation to repay the loan, potentially providing years of ownership without making a payment or incurring any interest. Currently, GVHDC has owned the property for four years payment- and interest-free.

A further contingency in the terms of the loan requires that, even were the homes to appear and be fully occupied today, GVHDC would have to turn a profit to have any obligation to make repayment. This is a dubious proposition given that GVHDC is putatively a nonprofit corporation and its tenants will all be low-income county residents. However, assuming GVHDC does make some profit, repayment of the loan can only come from its "Net Annual Cash Flow," which allows GVHDC to subtract its entire cost of operations for the site, including property taxes, payroll, maintenance, utilities, and the premiums for the multiple forms of required insurance. In essence, the Housing Authority will be annually subsidizing all of these costs, not in full, but certainly at a nonzero level.

Additionally, the loan caps annual repayment at the percentage of the "Net Annual Cash Flow" reflected by comparing the $250,000 to the total loans involved in the Project. This is a further contingency, and allows GVHDC to significantly reduce its annual payment to the Housing Authority based on the amount of additional financing it takes to develop the site. Consequently, if, after subtracting all their operating expenses, GVHDC has anything left over from the rent it has collected from its low-income tenants, the Housing Authority would only be entitled to a small percentage of that amount.[2]

All of these contingencies applied to the loan make it operate more like a grant, where if the Project is performed to specifications and operated for a certain number of years, the funds need not be returned. As a result, this loan is not a traditional arms-length mortgage at a fair market rate, but a contingent repayment obligation, which constitutes public funds. (§ 1720, subd. (b)(5).)

In light of the finding that the $250,000 land purchase loan from the Housing Authority to GVHDC constitutes public funding sufficient to render the Project covered by the prevailing wage law, it is not necessary to discuss NCECI's other arguments.

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[2] The promissory note also leaves vague whether payments for other loans can be deducted as operating expenses for the site, which would result in a cascading effect, further reducing the payment obligation.

Conclusion

For the foregoing reasons, the Bentley Estates Housing Project in the City of Waterford is public work subject to prevailing wage requirements.

I hope this determination satisfactorily answers your inquiry.

Sincerely,

Katrina S. Hagen
Director of Industrial Relations