

STATE OF CALIFORNIA
DEPARTMENT OF INDUSTRIAL RELATIONS

DECISION ON ADMINISTRATIVE APPEAL

RE: PUBLIC WORKS CASE NO. 2004-035

SANTA ANA TRANSIT VILLAGE

CITY OF SANTA ANA

I. INTRODUCTION

On January 5, 2006, the California Building Industry Association ("CBIA") and the Building Industry Legal Defense Foundation ("BILD") (collectively "Appellants") filed a notice of appeal ("Notice") of a public works coverage determination dated December 5, 2005 ("Determination"). The Determination found that the Santa Ana Transit Village ("Project") is a public work subject to prevailing wage requirements. Based on the specific facts of this case, the Director concluded that the transfer of two publicly-owned parcels from Santa Ana Redevelopment Agency ("Agency") to Santa Ana Transit Village, LLC ("Developer") for their combined fair reuse value was for less than "fair market price" and, therefore, a payment in whole or in part out of public funds within the meaning of Labor Code section 1720(b)(3).¹ Developer, which requested the Determination, did not file a notice of appeal and declined the opportunity to provide comment during the administrative appeal process.

Appellants were obligated to "state the full factual and legal grounds upon which the determination is appealed" in its Notice. (Cal. Code Regs., tit. 8, § 16002.5.) Appellants raised the following four distinct grounds for appeal: whether the Project is a public work subject to prevailing wage requirements; whether the Determination is a "radical departure" from prior determinations; whether the Determination is improper

¹ All further statutory references are to the California Labor Code unless otherwise specified.

legislative activity; and whether the Determination is subject to the requirements of rulemaking. Appellants subsequently added issues in a later submission, which include whether the Project enjoys a statutory exemption from prevailing wage liability under sections 1720(c) or (d) and whether the payment of public funds was payment *for* construction under section 1720(a)(1). Given the above-stated regulation, however, issues not raised in the Notice will not be addressed.

All of the submissions and arguments, including those of the California Redevelopment Association ("CRA"), have been considered carefully. For the reasons stated below, the appeal is denied; and the Determination that the Project is a public work, under the facts as originally presented, is affirmed. Because this Decision on Administrative Appeal addresses issues raised on appeal for the first time, it supersedes and replaces the Determination of December 5, 2005.²

II. FACTS

Appellants did not claim in their Notice that the Director misstated the facts. As the Determination stated:

The Project involves the construction of 108 attached live-work units within the City of Santa Ana ("City") pursuant to City's Transit Village Plan ("Plan"). The Project is being undertaken by Santa Ana Transit Village, LLC ("Developer") under a Disposition and Development Agreement ("DDA") entered into with the Santa Ana Redevelopment Agency ("Agency") on April 19, 2004. The DDA provides that once the 108 units are constructed, the units will be sold at market rates with covenants requiring that a title holder live in each unit and operate a small entrepreneurial or artistic enterprise, consistent with the specific transit village plan for the area.

The Project is being built on five contiguous parcels of land. Developer is purchasing three of the parcels through private sales for \$1,830,000 ("private parcels"). [fn. Developer represents that the average cost per square-foot of the three separately-sold and differently-priced private parcels is \$16.33.] City owned the other two parcels but sold them to Agency for \$2,084,700 to assist the Agency in land assembly for the Project ("public parcels"). One of the public parcels is a vacant parking lot located at 927 Santa Ana Boulevard ("Parcel 927"), and the other is a

² As such, PW 2004-035, *Santa Ana Transit Village, City of Santa Ana* (December 5, 2005) is designated as precedential. Accordingly, it will no longer be followed by the Director and should no longer be considered guidance by the regulated public after the date of this Decision on Administrative Appeal.

building of offices and small shops located at 901 Santa Ana Boulevard, which is currently occupied by Rancho Santiago Community College, whose rent is \$1 per year ("Parcel 901").

Under the DDA, Agency agreed to sell the public parcels to Developer. Prior to the sale, City, Agency and Developer obtained both a fair market value appraisal for each of the public parcels considered separately and a fair reuse value analysis for the two public parcels considered as one, as set forth below.

Fair market value is the value of the land at its highest and best use as determined by a bona fide appraisal. The appraisal determined the highest and best use of Parcel 927 to be its proposed use as live-work units; its fair market value at that use is \$25 per square-foot or \$1,300,000. The highest and best use of Parcel 901, when occupied, was determined to be an "office/shop building," its pre-existing, non-conforming use; its fair market value at that use is \$1,739,800. The highest and best use of Parcel 901, when vacant, was determined to be its proposed use as live-work units; its fair market value at that use is \$35 per square-foot or \$1,708,000.

By contrast, fair reuse value is the value of the land in relation to the covenants and conditions that control its development under the DDA, as determined by a calculation of the development's projected costs, income and profitability. Beatty, *Redevelopment in California* (2004), p. 151. The fair reuse value analysis estimated the projected proceeds from the sale of the 108 units. From that amount, the estimated cost of construction, the expected profit to Developer and the cost of acquiring the private parcels were subtracted. The remainder, \$1,620,000, was deemed to be the fair reuse value of the public parcels, with no differentiation between the two parcels.

As required by Health and Safety Code section 33433, Agency prepared a Report ("33433 Report") describing the disposition and development plan. In the Report, Agency represented the fair market value of the two public parcels to be \$25 per square-foot or \$2,520,000, and the fair reuse value of said public parcels to be \$1,620,000. [fn. The Report does not explain either of the following: (1) Agency's adoption of \$25 per square-foot from the appraisal of Parcel 927, rather than \$35 per square-foot from the appraisal of Parcel 901, as the measure of fair market value of the two public parcels; or (2) Agency's calculation of \$2,500,000 as the fair market value of the public parcels rather than what which was determined by the appraisal - \$3,039,800 (\$1,300,000 for Parcel 927 plus \$1,739,800 for Parcel 901 if occupied) or \$3,008,000 (\$1,300,000 for Parcel 927 plus \$1,739,800³ for Parcel 901 if vacant).]

³ Error in original. The correct figure is \$1,708,000.

In the DDA, Agency and Developer set the total purchase price for the public parcels at \$1,620,000. The DDA set the price for Parcel 927 at \$1,300,000, its fair market value. In setting the purchase price for Parcel 901 at \$320,000, Agency and Developer appear to have subtracted the fair market value of Parcel 927 (\$1,300,000) from the fair reuse value of the public parcels (\$1,620,000). The \$320,000 purchase price for Parcel 901 is not based on any methodological measurement of that parcel's value; it does not derive from either the fair market value appraisal or the fair reuse value analysis. Clearly, the parties agreed to a total purchase price equal to the fair reuse value of both parcels and worked backwards from there.

Determination, pp. 1-3 (some footnotes omitted).⁴

III. DISCUSSION

THE TRANSFER OF THE PUBLIC PARCELS FOR FAIR REUSE VALUE, CALCULATED AS THE RESIDUAL LAND VALUE, IS A TRANSFER OF AN ASSET FOR LESS THAN FAIR MARKET PRICE UNDER LABOR CODE SECTION 1720(B)(3) BECAUSE THERE IS NO EVIDENCE THAT THE FAIR REUSE VALUE CALCULATION WAS MARKET BASED.

Section 1720(b)(3) defines "paid for in whole or in part out of public funds" to include a "transfer by the state or political subdivision of an asset of value for less than fair market price." In cases involving the transfer of real property, as here, there is no question that the fair market value of the property is equivalent to its "fair market price" within the meaning of this section.⁵

In PW 2003-040, *Sierra Business Park/City of Fontana* (January 23, 2004), the Director left open the question whether fair reuse value is equivalent to fair market price where, for example, "a public agency places restrictions on the use of property." (*Sierra Business Park, supra*, fn. 6.) Because the facts in *Sierra Business Park* did not involve a transfer of real property at its fair reuse value, there was no need to answer the question

⁴ Subsequently, on or about December 12, 2005, Agency and Developer entered into a First Amendment to Development and Disposition Agreement. The parties agreed that the purchase price for Parcel 901 would be increased to equal its then appraised fair market value of \$2,050,000. The terms of the transaction had changed so that Agency received the fair market value for each of the two parcels. Agency did not submit this information to the Director until September 2006, well after issuance of the Determination.

⁵ This is consistent with PW 2003-040, *Sierra Business Park/City of Fontana* (January 23, 2004), p. 3. Had the facts as described in footnote 3 been presented to the Director at the time of the Determination, *Sierra Business Park* would have answered the question whether the Project was "paid for in whole or in part out of public funds."

whether such a transfer might constitute a payment of public funds under section 1720(b)(3).

As the Determination stated:

The legislative history of Labor Code section 1720(b)(3) provides no direct support for either Developer's or [State Building and Construction Trades] Council's view of what the Legislature meant by the phrase "fair market price." Generally, however, Senate Bills 975 and 972, which amended Labor Code section 1720 to expand the definition of public funds, were intended in part to capture the universe of public subsidies given by redevelopment agencies to private developers for their construction projects. A common way in which redevelopment agencies subsidize these projects is through the sale of publicly-owned property, sometimes acquired through the agency's power of eminent domain, to the developer at less than the property's fair market value. Beatty, *Redevelopment in California* (2004) 169 ...

Under basic rules of statutory construction, the words of a statute should be given their plain meaning. *Moyer v. Workers' Compensation Appeals Board* (1973) 10 Cal.3d 222, 230. "Fair market value" is a term of art in the appraisal community and generally performed in accordance with the Uniform Standards of Professional Appraisal Standards established by the Appraisal Institute. A fair market valuation reflects a property's value "on the date of valuation that would be agreed to by a seller, being willing to sell but under no particular or urgent necessity for so doing, nor obliged to sell, and a buyer, being ready, willing, and able to buy but under no particular necessity for so doing, each dealing with the other with full knowledge of all the uses and purposes for which the property is reasonably adaptable and available." Code Civ. Proc., § 1263.320; see also, Health & Saf. Code, § 25395.73. The fair market value assumes the purchaser will use the property for its highest and best use consistent with state and local law. For redevelopment projects, highest and best use contemplates a use consistent with the redevelopment plan. See, Health & Saf. Code, § 33433(b)(1). In public works coverage determinations involving the issue of fair market value, the Director will accept a bona fide appraisal performed by an independent and certified appraiser as determinative of fair market value unless credible evidence to the contrary is presented. *Sierra Business Park, supra*, p. 4.

Determination, pp. 4-5 (footnote omitted).

Appellants criticize the Director for relying on Code of Civil Procedure section 1263.320 to define "fair market value." Appellants, however, propose no other statutory definition of the phrase. While there may be a number of variations in the definition of

“fair market value” in the appraisal community,⁶ the definition adopted by the Director is the most commonly cited and understood meaning of the phrase; and, therefore, the Director’s reliance on it is justified. Usage of this definition also is consistent with the California Redevelopment Act. (Health & Saf. Code, § 33000 et seq.) A redevelopment agency must, as part of the report on a sale of property, provide the public with “the estimated value of the interest to be conveyed or leased, determined at the highest and best uses permitted under the plan.” (Health & Saf. Code, § 33433(a)(ii)(B)(ii).) If a sale is for less than the property’s fair market value “determined at the highest and best use consistent with the redevelopment plan,” the agency has to provide an explanation for the lower price. (Health & Saf. Code, § 33433(a)(iii)(B)(ii).)

In this case, the appraiser calculated the fair market value of Parcels 901 and 927 at their highest and best use consistent with the redevelopment plan, namely work-live lofts. That is, the fair market value appraisal took into account the restricted use of the public parcels contemplated in the redevelopment plan. Rather than setting the price for the public parcels at their appraised fair market value, Agency and Developer originally settled on a sales price for both public parcels based on a calculation of the residual land value of the public parcels, which is a calculation of the remainder from anticipated income after all other estimated costs (including projected overhead and profit) were deducted. The original \$320,000 price for Parcel 901 was determined by subtracting the appraised fair market value for Parcel 927 from the overall fair reuse value, calculated from the residual land value.⁷

The fair reuse value calculation, which relied on the residual land value analysis, was not market-based because it was based on speculative assumptions. As the Determination further stated:

⁶ See, Aubry, Garland, *Redevelopment Agency Real Property Transfers at Fair Reuse Value: Santa Ana Transit Village and Its Requirement For the Payment of Prevailing Wage* (2006) 15 California Land Use Reporter 151, 153-154.

⁷ The fair reuse value of both parcels was based on a price per square foot. Had the Agency used the same square foot price to determine the fair reuse value for Parcel 901 alone, the \$320,000 purchase price would not only have been below fair market price but also below that parcel’s fair reuse value. Even under Appellants’ own position that fair reuse value is equivalent to fair market price as a matter of law, that position is not supported by the facts.

"Fair reuse value" is a term unique to redevelopment projects. It assumes the proposed restrictions in the disposition and development agreement on the use of the property, and thereby distorts the property's value such that a market-based appraisal is not possible; that is, there is no "market" value. Fair reuse valuation is not a generally accepted appraisal method, and the Appraisal Institute does not recognize it as a means of determining market value. The fair reuse value is a speculative figure because it is based entirely on a set of assumptions as to the projected income, costs, and profit of the proposed development. A change in one assumption will result in a dramatically different result. In the context of public works coverage determinations, in no section of the Labor Code is the phrase "fair reuse value" anywhere mentioned.

* * *

In light of the core differences in meaning between "fair market value" and "fair reuse value" and the legislative purpose of Senate Bills 975 and 972 as described above, Developer's interpretation of Labor Code section 1720(b)(3) is untenable. Developer's position would have the Director ignore the word "market" in "fair market price" and accept "fair reuse value" in its place even though the calculation of fair reuse value bears no relationship whatsoever to the market. To read into the concept of "market" a calculation that is subject to mathematical manipulation is not the Director's role. Thus, the resolution of this issue rests on the word "market" in the phrase "fair market price." In order for a transfer to be considered at fair market price within the meaning of Labor Code section 1720(b)(3), there must be evidence that the purchase price is determined by competitive forces in the "market." Here, the purchase price was set below the market value in a private negotiation between the Developer and Agency, not in a competitive market environment.

Determination, pp. 7, 6.

CRA criticizes the requirement to show a market-based price as not practical in redevelopment, with its focus on eliminating blight. This, however, does not appear to be a view universally shared throughout the redevelopment community as the CRA's own publications demonstrate. As the Determination stated:

Redevelopment agencies can also examine the market in connection with the sale of a property with additional verifiable use restrictions for purposes of establishing a fair market price. See, Allardice, *When is "Fair Market Price" The Same As "Fair Reuse Value,"* Redevelopment Journal, February 2003, pp. 9, 14. If a 33433 Report demonstrates that the purchase price has been determined based on competitive forces in the market, such as when a restricted property is offered for sale either on the

open market or through a request for proposals that results in competitive bidding, such a price may be "fair market price" within the meaning of Labor Code section 1720(b)(3). The facts of this case, however, do not demonstrate that the purchase price of the public parcels was based on any competition in the market.

Determination, p. 7.

In the context of the specific facts of this case, *as originally presented*, the transfer of the public parcels for their fair reuse value, which was arrived at through a residual land value calculation, constitutes a transfer of an asset for less than fair market price within the meaning of section 1720(b)(3) and therefore is a "payment in whole or in part out of public funds."

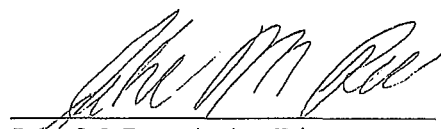
This analysis is based on the statutory change in law that occurred with the enactment of Senate Bills 975 and 972. Appellants' argument that the Determination is a "radical departure" from prior determinations is rejected. Appellants' argument fails to take into account the change in the statutory scheme. Appellants' argument that the Determination is an unwarranted act of legislative activity is rejected as unsupported by law. Contrary to Appellants' argument, coverage determinations are quasi-legislative interpretations of the California Prevailing Wage Law that are issued within the Director's plenary authority. (*Lusardi Construction v. Aubry* (1992) 1 Cal.4th 976.) Finally, Appellants' argument that the Determination had to be issued in compliance with the rulemaking requirements of the Administrative Procedures Act (Gov. Code, § 11340 et seq.) is incorrect. The Determination, which was addressed to a specific party and relied on the specific facts presented, is not subject to rulemaking requirements. (Gov. Code, § 11340.9(i).)

IV. CONCLUSION

For the reasons stated above, the appeal is denied and the Determination that the Project is a public work under the facts presented is affirmed. This Decision constitutes final administrative action in this matter.

Dated:

25 June 07


John M. Rea, Acting Director