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Letter No. LR-96-02

Subject: Application of Federal labor standards to HOME projects

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The National Affordable Housing Act of 1990 (NAHA) created the HOME Investment Partnerships Program (HOME), a housing development program with new language in the provision concerning Federal (Davis-Bacon) labor standards applicability. Guidance for HUD field staff and clients on the application of Davis-Bacon requirements to HOME projects was provided on a case-by-case basis until general policy decisions could be made and those policies could be tested against actual project proposals. We believe that sufficient experience has been gained to enable us to compile general guidance in this area for HUD staff and client use.

The following is provided with the cooperation and advice of the Community Planning and Development's Office of Affordable Housing and the Office of General Counsel.

I. Statutory and regulatory provisions.

Federal (Davis-Bacon) wage requirements are made applicable to the HOME program by *Section 286 of the NAHA* which provides, in part, as follows:

"Any contract for the construction of affordable housing with 12 or more units assisted with funds made available under this subtitle shall contain a provision requiring that not less than the wages prevailing in the locality, as predetermined by the Secretary of Labor pursuant to the Davis-Bacon Act..., shall be paid to all laborers and mechanics employed in the development of affordable housing involved,...."

HUD regulations (*24 CFR 92.354*) paraphrase the statutory provision and clarify that the contract for construction must contain these wage provisions if HOME funds are used for any project costs, including construction or nonconstruction costs, for housing with 12 or more HOME-assisted units.

The regulations further explain that a construction contract that includes a total of 12 or more HOME-assisted units is covered by Davis-Bacon requirements even if the contract covers more than one HOME "project" and prohibits arranging multiple construction contracts within a single project for the purpose of avoiding Davis-Bacon coverage. Once triggered, the wage provisions apply to the construction of the entire project - HOME-assisted and non-assisted portions, alike.

The NAHA and program regulations also provide for the exclusion of certain **sweat equity** labor from Davis-Bacon coverage. Members of an eligible family who provide labor in exchange for acquisition of a property for homeownership or toward rental payments are not subject to Davis-Bacon wage requirements. Additionally, **volunteers** may be employed in accordance with *24 CFR Part 70*.

The HOME labor standards provision is unlike labor standards clauses in other HUD programs. For example, the labor standards for Community Development Block Grants (CDBG) apply to *construction work financed in whole or in part* with the assistance received through CDBG and cover residential property only if the *property contains not less than 8 units*. For HOME, we are directed to "**construction contracts**" (not construction work or properties) where the standard is whether 12 or more of "units" covered by the contract are "**assisted**" (not whether construction work is directly financed). These differences serve both to focus the unit threshold window on the "contract" and to broaden the scope of coverage to construction and non-construction costs and assisted and non-assisted portions.

II. Unit Threshold.

The Davis-Bacon "trigger" relates to the *number of HOME-assisted units contained in a construction contract*. It is important to recognize that the two (2) factors are: 1) the number of HOME units - there may be units which **are not** HOME-assisted in the contract; and 2) the scope of the construction contract - **not** the "project."

The number of HOME-assisted units is determined in accordance with guidance provided by the program office in *Notice CPD 94-12* (April 26, 1994). This determination is made by the participating jurisdiction (PJ), insular area or Indian tribe (referred to collectively as *recipients*) primarily for purposes other than labor standards applicability. The Offices of Labor Relations, General Counsel and CPD have agreed that the number of HOME-assisted units identified pursuant to this Notice is acceptable for Davis-Bacon unit threshold purposes. The number of assisted units within a specific project should be available from the recipient and is also reflected on HUD Form 40094, Homeownership Assistance/Rental Housing Project Set-Up Report. (*Note that the recipient determines the number of assisted units in a project, not a construction contract.*)

Once the number of HOME-assisted units is determined, the construction contract(s) must be identified. Each contract must then be considered for coverage based upon the number of HOME units contained in the contract: contracts with 12 or more HOME units are covered; contracts with 11 or less HOME units are not. Two important factors must be weighed in this determination:

- 1) **A HOME project can not be divided into multiple contracts to avoid Davis-Bacon coverage.** There may be other, legitimate reasons that a single project would be constructed with separate contracts that would each contain 11 or less HOME units and the contracts would not be covered. But it is not permissible to arrange multiple contracts solely to circumvent labor standards requirements.
- 2) **A construction contract with 12 or more HOME-assisted units is covered even if the contract involves more than one HOME project.** For example, if, for whatever reason, four projects each containing 4 HOME-assisted units are "pooled" into one construction contract, the contract would be covered.

Special note on Group Home and Single Room Occupancy (SRO) projects:

Notice CPD 94-01 (January 4, 1994) defines group homes and SROs for HOME assistance purposes. A **group home** is usually a large single family residence consisting of common space such as kitchens, dining areas, living rooms and bathrooms, along with separate private or semi-private space (i.e., bedroom) for each occupant. An **SRO** consists of single room dwelling units that are the primary residences of its occupants, and may have shared common dining, sanitary and/or recreation facilities. Depending upon certain parameters established by the program office (*See Notice CPD 94-01*), PJs may choose to consider group homes as a single unit for HOME assistance purposes or may classify them as single room occupancy units. In the latter case, if the number of HOME-assisted SRO dwelling units covered by a contract for construction equals 12 or more, Davis-Bacon labor standards are applicable.

III. Scope of coverage.

It has been determined that applicability of Federal wage requirements is not affected by the specific use of HOME funding. That is, it does not matter whether HOME funds are used for construction or non-construction project costs; if the threshold is met then the labor standards provision is triggered. (*See also CPD Notice 92-19, dated June 9, 1992.*) This determination hinges in part on the difference between "assisted" and "financed" - "assisted" is a much broader term. In addition, under the statute Federal wage rates apply whenever a construction contract contains 12 or more *units* that are assisted, whether the *contract* is assisted or not. Housing units in a HOME project that are constructed with private funds may still be "assisted" by HOME even though the construction of the units is not directly "financed" by HOME.

It has also been determined that once triggered, the labor standards apply to the construction of the entire project. For example, if it were practical to funnel all of the HOME funds to the construction costs for a portion of a project it would not limit labor standards applicability to that HOME-funded portion. (*See also CPD Notice 94-12.*)

IV. Homeownership projects.

Some HOME projects are designed to provide homeownership opportunities to low-income families. These projects may not involve the use of HOME funds for the construction of the housing in any way but, for example, involve only down payment or mortgage assistance to the homebuyers.

Construction work for projects in which HOME funds are used only to assist homebuyers to acquire single family housing is not covered UNLESS there is an agreement with the owner or developer of the housing in advance of the construction work that HOME funds will be used to assist homebuyers to buy the housing and the construction contract covers 12 or more HOME-assisted units.

V. Case Studies

Many of the following examples are based on actual projects that were presented for labor standards coverage determinations. A description of the project is followed by the coverage decision and rationale. Remember that in most cases the key to applicability is not the use or targeting of the HOME funds but the number of HOME-assisted units that are in a contract for construction.

1) a. Proposal The project involves the construction of a 59-unit single family residence subdivision. HOME funds will provide project construction financing and secondary permanent financing to prospective low-income homebuyers. The PJ, as the lender and with concern about the overall viability of the project, is willing to commit to the development of the subdivision only in phases of 10 or 11 units at a time. Funding for subsequent phases will be contingent on the successful completion and marketing of the preceding phase(s). Separate construction contracts will be awarded for each phase.

b. Decision The proposed construction work will not be covered. None of the contracts for construction will contain 12 or more HOME-assisted units and it appears that the division of the project into multiple contracts is a precautionary measure to protect the lender and is not for the purpose of avoiding Davis-Bacon coverage.

2. a. Proposal The project involves the construction of a 60-unit multifamily property (all 60 units will be HOME-assisted) and a 100-unit single family development (of the 100 single family units, 33 units will be HOME-assisted). The construction work will be accomplished in four separate contracts: one for the 60-unit multifamily property; and 3 contracts for the single family homes each contract containing no more than 11 HOME-assisted units. HOME funds will be used for land acquisition and site development for the construction of all of the housing units. The developer and PJ have entered into an agreement in advance of construction that HOME assistance will be provided for homebuyers to purchase 33 of the single family units. The PJ and developer assume that the multifamily building will be covered but ask for confirmation that structuring the single family portion in the manner described will avoid Davis-Bacon coverage.

b. Decision The construction of the entire development is covered. The assumption that the multifamily building is covered is correct. As to the single family units, there is no reasoning presented that explains why this portion has been divided into 3 separate contracts other than to avoid prevailing wage requirements. In fact, the inquiry so much as states that avoiding Davis-Bacon is the reason for the multiple contract strategy.

Special notes on this Case Study: This scenario, modified only slightly, could result in a very different coverage decision relative to the single family units: What if the PJ established the single family units as three separate *projects* each containing 11 HOME-assisted units and the developer awarded a separate construction contract for each project?

While the regulations prohibit creating multiple contracts within a single project to avoid Davis-Bacon coverage, *there is no prohibition against arranging multiple projects* within a development proposal. In other words, the regulations would not prohibit a PJ - which considers a developer's proposal to build a 100-unit single family HOME project - from establishing multiple "projects" (each with 11 or less HOME-assisted units) and the developer awarding a separate construction contract for each project. This arrangement would result in no Davis-Bacon coverage. **However**, if the developer grouped these "projects" under one construction contract so that the total number of HOME-assisted units contained in the contract is 12 or more, the work would be covered. The key is the number of HOME-assisted units contained in a contract for construction.

3. a. Proposal A developer, with a commitment from the PJ for HOME assistance, proposes to develop 40 single family units for homeownership. HOME funds combined with private funds will be used for site acquisition and to finance the construction of the units, which will be performed under one contract. Prospective homebuyers will execute real property sales contracts, presumably conveying ownership of the land, prior to the construction of the single family units. Each unit will be entered as a single project in the HUD cash management system (CM/I). The PJ asks for confirmation that executing sales contracts prior to construction and entering the units as separate "projects" in the CM/I database would not trigger Davis-Bacon requirements.

b. Decision The construction work will be covered. The two factors presented, ownership of the land and separate entry into the CM/I database, have no significant bearing on labor standards applicability. Davis-Bacon coverage will be triggered because the construction contract will contain 12 or more (40) HOME-assisted units.

4. a. Proposal A PJ requests guidance in relation to six (6) HOME projects totaling 22 units which will be owned and operated by one community based non-profit organization. All 6 projects, ranging from 2 to 4 units each, are in varying stages of processing and are being handled independent of each other with separate applications, loans and construction contracts. However, due to an approaching financing commitment deadline, all six projects were entered into the CM/I system on the same date.

b. Decision Davis-Bacon wage requirements would not apply to these projects. None of the contracts for construction will contain 12 or more HOME units. The date of entry into the CM/I system has no bearing on Davis-Bacon applicability.

5. a. Proposal The project involves the construction of 15 units in two buildings (9 units in one building; 6 in the other) on contiguous lots. A combination of HOME funds, low-income tax credits and developer equity are financing the project. Construction of both buildings was begun under one contract using Davis-Bacon wage rates. Disputes between the owner/developer and the contractor led to work stoppage and ultimately the contractor was dismissed. With both buildings only partially completed, the tax credit contributions were in jeopardy unless completed and occupied units were delivered quickly. In order to secure the tax credits, the PJ and developer propose to contract for completion of one building and then contract for the completion of the second building. The same contractor would be used for both buildings but the contract for the second building would be executed only after successful completion of the first.

b. Decision Davis-Bacon wage requirements would not apply to the construction of these buildings. Neither of the contracts for construction will contain 12 or more HOME-assisted units and it appears that the division of the project into multiple contracts is intended to expedite progress for tax credit benefits and not to avoid Davis-Bacon coverage.

6. a. Proposal A developer proposes to construct a multifamily project with 2 buildings of 8 HOME-assisted units each. HOME funds will be used for site acquisition and certain "soft costs" such as site surveys and architectural drawings. The construction work will be performed under one contract. No HOME funds will be used for the construction of the units.

b. Decision The construction of the project is covered. Unlike the CDBG program, the HOME labor standards provision is triggered whether HOME funds are used for construction or non-construction project costs. Since the construction contract will contain 12 or more HOME-assisted units, Davis-Bacon rates will apply.

7. a. Proposal The project involves the new construction of a 14-unit HOME (single family homeowner) subdivision. CDBG and HOME funds will finance site improvements for the subdivision. The improvements will be performed under one contract and constructed only within the boundaries of the subdivision site. The improved site/housing lots will be turned over to three (3) community housing development organizations (CHODOs). The CHODOs will contract for the construction of the individual housing units separately and will have no more than two lots in their control at any time. The remaining lots will be made available to the CHODOs as construction of the units is completed.

b. Decision The site improvements contract will be covered and the contracts for the housing construction will not. The question here is not so much coverage but what kind of wage decision is applicable. For Davis-Bacon purposes we can view the site improvements and housing construction as a single development since the purpose of the site improvements is solely to support the construction of single family residences. In this case the site improvements are "incidental" to the housing construction and therefore would be subject to a residential wage schedule.

Any questions concerning this *Letter* may be directed to the Office of Labor Relations at (202)708-0370 or, in the case of HUD program participants, to the HUD Field Labor Relations Staff with jurisdiction for your area.

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