



DATE: June 22, 2020

TO: Mayor and Members of the City Council

VIA: Dante Hall, Interim City Manager

FROM: Norm Dorais, Public Works Director/City Engineer
Edmund Suen, Finance Director

SUBJECT: LEVEE PROTECTION PLANNING AND IMPROVEMENTS PROJECT
(CIP 301-657) – PROJECT COST ANALYSIS AND TIMING OF
GENERAL OBLIGATION BOND AD VALOREM PROPERTY TAX RATE
LEVY

RECOMMENDATION

It is recommended that the City Council receive the cost analysis on the Levee Protection Planning and Improvements Project (CIP 301-657) and provide direction to staff, by Minute Order, on whether to set a general obligation bond ad valorem property tax rate levy in Fiscal Year 2020-2021 or Fiscal Year 2021-2022.

EXECUTIVE SUMMARY/ANALYSIS

This report summarizes the progress of the Levee Protection Planning and Improvements Project (Levee Improvements Project) since the last City Council update at its June 4, 2020 City Council Special Meeting and includes a discussion of the following:

- The variance in the estimated total project costs from \$90 million to \$109 million, between June 2017 and today; and
- Whether to set the general obligation bond ad valorem tax levy in FY 2020-2021 or FY 2021-2022.

LEVEE IMPROVEMENTS PROJECT COST ANALYSIS

At the City Council Regular Meetings of April 6 and May 4, 2020 and at the City Council

Special Meeting on June 4, 2020, staff provided updates on the Levee Improvements Project. As part of the updates, staff shared the most recent construction cost estimates based on the third party constructability review of the 90% design, submitted in March 2020. During the June 11, 2020 Levee Subcommittee meeting, which consists of Councilmembers Richa Awasthi and Jon Froomin, staff outlined how the initial \$90 million cost estimate was established. A summary of the variation between the initial cost estimate, and current cost estimate is outlined in the following table:

Levee Project Cost Estimate (in Millions)				
	June 2017	March 2020	Variance Amount	Variance %
Construction	52.8	68.1	15.3	29.0%
Markups	11.4	17.9	6.5	57.0%
Contingencies	15.8	9.0	-6.8	-43.0%
Subtotal	80.0	95.0	15.0	18.8%
Design, Permits, Landscaping, ROW, Constr. Mgmt.	10.0	14.0	4.0	40.0%
Total	90.0	109.0	19.0	21.1%

The overall project cost increase between the June 2017 baseline cost estimate and the current cost estimate is a direct result of a delay in the project delivery. This is attributed to the challenges encountered while obtaining the regulatory permits and the resulting impact the permit conditions have had in increasing the project's construction duration.

Regulatory Permit Delays: The Levee Improvements Project required the acquisition of permits from four major regulatory agencies: the State Lands Commission (SLC), the Regional Water Quality Control Board (RWQCB), the San Francisco Bay Conservation and Development Commission (BCDC), and the U.S. Army Corps of Engineers (USACE). The June 2017 cost estimate had assumed the completion of construction in December 2020 based on design occurring concurrently with the permit review by the various agencies. However, because of the challenges in securing the needed permits, several of the initial assumptions turned out to be incorrect. It was learned that some of the regulatory agencies required a near complete design set prior to permit issuance as well as several iterative reviews to incorporate the special conditions to satisfy that agency's requirements. In addition, the issuance of the Army Corps permit was dependent upon the City's acquisition of the BCDC permit. As a result, the fourth and final regulatory permit was not secured by the City until January 7, 2020, two years later than originally anticipated.

Construction Duration: The original construction duration was established at 18-24 months. The design team sought contractor input, and considered the type of work, sequencing, and dependencies of certain project tasks on others to establish the project

schedule. During the regulatory permit approval process, conditions were established by the agencies, which restricted construction in sensitive areas of the levee for months at a time (i.e.: no work in the bay on levee segments between December 1 and May 31, and no work between February 1 and August 31 in areas where nesting birds have been observed). The addition of these restrictions resulted in the project team extending the estimated construction duration for one additional year to provide an adequate amount of time for the contractor to construct the project.

In total, these delays have added approximately three years to the projected construction completion date which has had a direct impact on project costs. Construction is now anticipated to be completed in the fall of 2023. Given the construction climate, and as competition for qualified labor in the Bay Area has increased, materials and labor costs have correspondingly increased over the past three years. While construction management (CM) services were initially anticipated to only be needed for the original two year construction window, CM services are now needed for three years (resulting in a CM contract that is approximately 50% more than originally anticipated). And finally, due to the long approval process to obtain all the regulatory permits, additional effort from the design team, environmental consultant, and City Attorney was required.

The total project cost estimate of \$109 million, presented to the City Council in April 2020, is 21% higher than the 2017 cost estimate. Based on OneSF's Annual Infrastructure Construction Cost Inflation Estimate (AICCE), the average annual rate of inflation for the last three years has been 5.58%. Over three years, this translates to a factor of 16.67% to account for inflation, which is within 5% of the current 21% variance.

The project documents and the call for bids were approved at the May 4, 2020 City Council Meeting. The project documents were released to the ten pre-qualified bidders on May 5 with the bids due on June 30, 2020. After the bid opening on June 30, 2020, the City will have a much more accurate estimate of the total project cost for the Levee Improvements Project.

GENERAL OBLIGATION BOND

Over the last several months, City staff, the financing team, and bond counsel have held numerous conference calls to discuss best options for the sale of General Obligation (GO) Bonds required for funding of the Levee Improvements Project. As reported to the City Council on April 6, 2020, the City is planning a negotiated bond sale to provide itself greater flexibility in responding to market conditions and impacts from COVID-19. In a negotiated sale, the issuer works with a pre-selected bond underwriter which allows for a much nimbler entry into the market (or withdrawal) and changes to the pricing structure on the day of the offering in response to investor demand.

GENERAL OBLIGATION BOND TAX RATE LEVY

The financing team is planning to structure the GO Bonds with a combination of low debt service costs and tax rates over a 30-year term with a significant original issue premium. Preliminary estimates for the sources and uses of GO Bond proceeds are as follows:

Sources of Funds*	
Bond Proceeds	
Par Amount	90,000,000.00
Net Premium	7,894,294.75
Total Bond Proceeds	97,894,294.75
Uses of Funds*	
GO Bonds Project Fund	89,735,000.00
Debt Service Fund	7,669,294.75
Cost of Issuance	265,000.00
Underwriter's Discount	225,000.00
Total Uses	97,894,294.75
*Preliminary, subject to change	

Ordinarily, upon the issuance of GO bonds, an ad valorem property tax levy is placed in the 1st available tax year (i.e. FY 2020-21). However, it is possible to postpone the tax levy by one year to FY 2021-2022 by structuring a delay in the principal payment to 2022 and use the original bond premium to make the 1st year's interest payments (Alternative 1). As indicated in the table below, Alternative 1 does increase the maximum tax rate levy by \$1 to \$37 per \$100,000 AV (assessed value). It also increases the total net debt service of the bonds by \$2.7 million to \$142,236,378.

	Base Case Scenario	Alternative 1	
	Base Scenario with Tax levy effective FY 2020-21; Maturity in Aug 2050	Tax levy effective FY 2021-22 Principal Deferral to Aug 2022; Maturity in Aug 2050	Difference from Base Case
Principal Amortization	2021-2050	2022-2050	
Par Amount	90,000,000	90,000,000	-
Net Bond Proceeds	89,735,000	89,735,000	-
Original Issue Premium	7,669,295	7,883,531	214,236
True Interest Cost	3.03%	3.04%	0.01%
Average Tax Rate levy (per \$100K AV)	29.42	29.69	\$0.27
Max Tax Rate levy (per \$100K AV)	36.00	37.00	\$1.00
Total Net Debt Service	139,535,807	142,236,378	2,700,571

In looking strictly at the economics, the municipal advisors and City staff recommends the base case and starting property tax levy in FY 2020-2021. Similarly, on June 11, 2020, the Levee Subcommittee also recommended the base case.

As indicated in the schedule below, City staff plans to bring forth GO Bonds financing documents for the City Council's approval on July 6 and will incorporate the City Council's decision on the timing of the property tax levy. Moreover, should the City Council decide on starting the property tax levy in FY 2020-2021, City staff will need to provide the tax levy amount to the County by July 7, 2020.

CURRENT SCHEDULE

Bid Opening	June 30, 2020
Approval of GO Bonds Financing Documents and Tax Rate Levy	July 6, 2020
City Provides Tax Rate Levy to San Mateo County	July 7, 2020
Award of Contract	July 20, 2020
Closing of Bond Sale/Funds Available	August 2020
Notice to Proceed	August 2020
Start of Construction	September 2020
Construction Completion	Fall 2023

At this time, City staff request that the City Council provide direction via Minute Order on whether to start the general obligation bond tax levy in FY 2020-2021 or FY 2021-2022.

FISCAL IMPACT

There is no fiscal impact for the project cost analysis update. The Levee Improvements Project Bid Opening is scheduled for June 30, 2020. Should any CIP Project Funding augmentation be needed, it will be requested as part of the staff report authorizing award of the construction contract which is currently scheduled for the July 20, 2020 City Council Meeting.

There is no fiscal impact on providing direction on the timing of the GO Bond property tax levy at this time. Upon the approval of financing documents on July 6, 2020, the City Council will be committing to the City's issuance of General Obligation debt and related debt service payments and the timing of the property tax levy.