

Memorandum

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To: CHAIR AND COMMISSIONERS
CALIFORNIA TRANSPORTATION COMMISSION

CTC Meeting: March 13-14, 2019

Reference No.: 2.5e.(5) - **REPLACEMENT**
Action Item

From: STEVEN KECK
Chief Financial Officer

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Subject: **SUPPLEMENTAL FUNDS - PUBLIC PRIVATE PARTNERSHIP – PRESIDIO PARKWAY PROJECT (PPNO 04-0619P) RESOLUTION FA-18-40**

RECOMMENDATION:

The California Department of Transportation (Department), with support from the San Francisco County Transportation Agency (SFCTA) as joint partners on the Presidio Parkway Public-Private Partnership (P3) Project (Project), recommends that the California Transportation Commission (Commission) allocate \$33,700,000 in supplemental funds for Project expenses. This approval will bring the total allocation for the Project to \$1,288.34 million.

ISSUE:

The Department's request for supplemental funds pertains to contractual obligations and related new costs associated with the two settlement agreements previously approved and the resulting completion of project work, including site work on the Presidio, landscaping allowance work within the Department's Right of Way, environmental commitments, extra work and permit related delays, and owner-controlled insurance. The contractor has completed all work on the project site and this is the final request from the Department for the construction of the Project.

BACKGROUND:

Unlike traditional project delivery methods, such as Design-Bid-Build (DBB), the P3 was structured on the premise that the Developer would secure independent financing and finance the design and construction of the Project. As set out by the Federal Highway Administration (FHWA) in the table below, the risks appropriately transferred in a P3 project are unique to the project type and delivery methods utilized, and are premised on allocating risks to the party best able to manage them.

| Risk | Traditional (DBB) | Presidio Parkway P3 (DBFOM) |
|---|--------------------------|------------------------------------|
| Change in Law | Public | Public |
| Change in Scope | Public | Public |
| Construction | Private | Private |
| Design | Public | Private |
| Final Acceptance | Public | Private |
| Financing | Public | Private |
| Force Majeure | Public | Shared |
| Ground Conditions | Public | Private |
| Hazardous Materials | Public | Shared |
| Independent Verification/ Validation | Public | Public |
| Landscaping | Public | Shared |
| NEPA Approvals | Public | Public |
| O&M | Public | Private |
| Permits | Public | Shared |
| Quality Assurance/ Quality Control | Public | Private |
| Right of Way | Public | Shared |
| Security | Public | Shared |
| Utilities | Public | Shared |

Under a Design-Build-Finance-Operate-Maintain (DBFOM) P3 model such as this Project, the responsibilities for designing, building, financing, operating and maintaining a project are bundled together and transferred to or shared with private sector partners. However, even in this model there are some responsibilities - or risks - that are better managed by the owner and are therefore retained by the owner. In determining which risks are to be transferred to the private sector, the owner must first determine who is in a better position to manage the particular risk. Transferring too little risk to the private sector negates the benefits of partnering. Alternatively, transferring too much risk, such as a risk that the private sector is unable to manage, would result in high-risk premiums, likely making the project cost prohibitive. In identifying and allocating risk appropriately, best practices dictate that if a risk is difficult to assess or manage, it may be appropriate to share it between the public and private sectors.

This Project involves the Presidio Trust (Trust), a significant, non-signatory third party that owns the land and imposes requirements outside of the P3 Agreement based on the FEIS/EIR and Programmatic Agreement, affecting the Project's scope of work, schedule and costs. The Trust's central role throughout design, construction and close-out introduced unexpected complexities and risks beyond both the Department's and the Developer's control. One such complexity has been the management of work by the Trust via the issuance and enforcement of permits by the Trust. As set forth in the above table, Permits are a shared risk between the Developer and the Department and risk has been shared on this Project. The process of obtaining and closing out Trust permits came with significant project delays and unanticipated changes to project criteria. Not complying with the permits and process that became necessary

to obtain and close out the permits would have prevented the Developer from completing the work on time to deliver the Project.

Project Overview

The Project is located in the city and county of San Francisco on Doyle Drive (U.S. Highway 101) and Richardson Avenue from Lombard Street to the Golden Gate Bridge Toll Plaza. The Project replaced the structurally deficient roadway built in 1936, serving as the southern access to the Golden Gate Bridge, connecting Marin and San Francisco counties and providing a major regional traffic link between the San Mateo Peninsula and North Bay Area counties. The Project posed several significant challenges that included: the need to keep the existing roadway open to traffic during construction; participation of four federal agencies with overlapping jurisdictions; construction within an environmentally sensitive National Park, with the requisite permitting processes; and operation and maintenance of bridge and tunnel structures with technological challenges. Furthermore, the Department, with SFCTA, was required to negotiate a Right of Entry (ROE) Agreement with the Trust (the landowner) for access to the land on which the Project was being built, for the right to construct the Project on Trust property and for the Department to secure the highway easement deed for the operating period of the project and highway operations overall on the new alignment.

In May 2010, the Legislature approved an original \$1,401.79 million budget for the Project. In January 2011, due to a favorable bidding environment and after submission of the Project to the Legislature for a mandatory review, the Department, in cooperation with the SFCTA, reached commercial close and executed the P3 Agreement with the Developer for \$1,080.54 million. Under the terms of the P3 Agreement, the Developer had the obligation to design, build, finance, operate and maintain the Project.

There were two settlement agreements already approved during the Project. In August 2016 and June 2016, the Commission approved two supplemental funds requests totaling \$120.1 million for a global settlement with the Developer. This first settlement addressed previous change orders (including reducing the scope of work for Trust related landscaping), all unresolved potential claims through August 2016 and the dismissal of a lawsuit filed by the Developer. In March 2018, for the second settlement agreement the Commission approved a supplemental funds request of \$37 million as the State's share of the \$54 million settlement with the Presidio Trust that also transferred the final landscape work within the Trust's Right of Way to be done by the Trust reducing Project risk. This second settlement agreement, which was with the Presidio Trust, did not fund, but did include, new scope for the Developer to complete by change order; which is now included in this request to approve a third, final settlement agreement now with the Developer. The current total supplemental funds approved by the Commission is \$174.10 million. Approval of this supplemental funds request would bring the total allocation for the Project to \$1,288.34 million for completion.

BASIS FOR SUPPLEMENTAL FUNDS

This proposed third settlement will resolve all outstanding disputes brought by the Developer. Any disputes with the Trust have been resolved in previous supplemental funds requests. The Developer is contractually entitled to seek “relief” and the Department is required to compensate the Developer for events that occur and are outside the Developer’s reasonable control. The P3 Agreement ([Appendix 1](#)) includes 23 specified events for which the Developer is entitled to relief in the form of either cost and/or time. Such examples of Relief Events include but are not limited to the following:

- Uncontrollable occurrences like *force majeure* events;
- Changes in law or project criteria that were not known to the Developer and in some cases the Department;
- Department Changes;
- Department’s failure to perform or observe any material covenants or obligations under the P3 Agreement or other Contract Documents;
- Department-Caused Delay.

Pursuant to the P3 Agreement, the Developer may file potential claims if it believes it is entitled to costs based on delays or extra work, extensions of time, for work it believes it is not required to perform under the Contract Documents. This is an essential process to allow the Department to be alerted by the Developer of the possibility of a claim for additional time or money and is an expected part of the project. For any potential claims not resolved during the life of the contract, the parties can file litigation after Final Acceptance of the Project. There are two potential claims being resolved pursuant to this settlement agreement and they are the only remaining claims on the Project. Both fall into the Relief Event categories of Department Changes, changes to project criteria that were not known to the Developer or the Department and Project Delays that although were not caused by the Department, were also not caused by the Developer but were caused by a third party and were not anticipated by either the Department or the Developer. These potential claims arose subsequent to the 2016 Settlement Agreement with the Developer and were partially reduced but not fully eliminated by the 2018 Settlement Agreement with the Trust.

The Department and Developer have worked diligently in recent months to complete all remaining construction and resolve costs and claims. The basis for additional funds is associated with work performed outside of the P3 Agreement, requirements from both the 2016 Settlement Agreement with Developer and the 2018 Settlement Agreement with the Trust and the related year delay. This request provides for the resolution of necessary work after the 2016 Settlement Agreement, to address additional unforeseen site conditions, design and construction modifications, delays, and environmental permits and Trust’s requirements, to achieve Project’s close-out.

This \$33.7 million request is for construction capital. The capital increase is for claim resolution of additional work scope outside of the P3 Agreement, construction delays, longer OCIP coverage, Resident Engineer office’s rent/utilities, and confirmation and implementation of outstanding environmental commitments.

Construction Capital Increase: \$33.7 million

- A. Developer Claims resolution for Department Change Orders, Extra Work and Delays: \$25.63 million

Developer claims the Department directed performance of work that was beyond obligations under the P3 Agreement and the 2016 Settlement Agreement. The Developer also claims it has suffered unanticipated delays for which it is seeking compensation. The Department agrees the Developer is entitled to payment for the extra work and for a portion of the delays and has worked with the Developer to negotiate the amount the Developer should be paid for the extra work and the period of delays for which the Developer should be compensated.

The work subject to Department Change Orders includes design modifications and other changes due to unforeseen site conditions, and additional requirements from the Trust and environmental permits. This work was due in large part to the landscaping work on Trust Right of Way. Neither party anticipated or could have anticipated, the amount and type of work that would be required to be performed by the Developer to turn it over to the Trust. This extra work was in the form of additional Storm Water Pollution Prevention Plan (SWPPP) measures, soil management plans, and other necessary measures to leave the site in a safe and stable condition until the Trust begins work on their landscaping projects on the tunnel tops and quarter master reach areas.

The Developer and the Department have negotiated and agreed to settle these potential claims, thereby allowing the Developer and the Department to comply with the construction completion and closeout milestones outlined in the Department's 2018 Settlement Agreement with the Trust. The Department secured the Highway Easement Deed on November 29, 2018, for the Developer to continue with the 30-year operations and maintenance, and the Department is returning the Property to the Trust, in accordance with the requirements of the Right of Entry Agreement.

- Trust's Requirements and Fees: \$4,079,500
To meet the Trust's standards and permits, additional submittals and reviews were required for drainage, grading, railing, fencing and other design modifications, utility devices and connections, architectural features, changes to accommodate future Trust improvements, and close-out documentation.
- Environmental Requirements: \$592,700
The Regional Water Quality Control Board required additional water pollution control measures and groundwater remediation for permit compliance.
- Department Change Orders (DCO): \$6,926,600
Changes were necessary to address Trust's horticulture soil requirements, utility conflicts, Golden Gate Bridge District's permit compliance, historical structures protection, restoration of the Multi-Use Trail (MUT), design modifications related to safety/electrical standards and unforeseen site conditions.

- Delays: \$14,031,300
Due to unanticipated delays in obtaining permits from the Trust, Developer was unable to complete construction on schedule, which resulted in additional costs for site management, remobilization, labor and materials cost escalation, rental costs, financing and Time Related Overhead (TRO). At the time of the 2016 Settlement Agreement with the Developer, construction was scheduled to be done by December 2016, but since then the Trust has required 46 additional permits to complete the remaining work. On average, it took over 5 months to approve each permit, well over the assumed 10-day turn-around per the P3 contract specifications. The Department was able to negotiate a reduced delay period, and the Developer has agreed to take responsibility for a total of seven months of this delay period.

B. Outstanding Environmental Commitments: \$6.6 million

U.S. Army Corps of Engineers and Regional Water Quality Control Board permits (404 and 401 respectively) require storm water treatment. While the Project maximized limited opportunities for onsite storm water treatment, additional offsite storm water treatment is necessary to mitigate deficits in treatment area. The Department and resource and partner agencies have been collaborating closely to finalize the proposed location, treatment area, scope of work, and long-term maintenance and reporting requirements, to complete the offsite mitigation by 2020.

C. Owner Control Insurance Program (OCIP): \$1.28 million

The delay in the overall construction completion from December 2016 to February 2019 necessitates the coverage extension and additional service cost. The P3 Agreement requires the Department to provide and maintain the OCIP until Final Acceptance, which is currently scheduled for spring of 2019.

D. Resident Engineer's Office: \$0.19 million

Delays in project completion from December 2016 to spring of 2019 resulted in additional costs for Resident Engineer's office rent, utilities, and relocation.

NEXT STEPS:

The settlement of the potential claims has been aggressively negotiated between the Parties for the better part of a year. The alternative of rejecting the settlement and proceeding with litigation will likely add to the risk of higher payouts, which will include attorney fees and interest. The complexity of the project and of the P3 contracts will contribute to an unpredictable trial outcome. Additionally, while claims on construction projects typically go to public works arbitration with the Office of Administrative Hearings, the P3 Agreement allows for litigation in the Superior Court of the County of San Francisco. Therefore, the settlement avoids the risk inherent in a jury trial. As with any "Major Projects" the Department has already engaged FHWA and, based on our ongoing discussions, believes that the supplemental funds will be approved for federal reimbursement.

Because the Project is the first P3 delivered under the authority granted in SBX2 4, it will naturally be a topic of debate regarding this delivery method. While this supplemental funds request will no doubt figure into that conversation, useful conclusions are unlikely to emerge until a thorough post-project analysis can be conducted. A thorough examination should ultimately yield data-based conclusions about the impact of changing delivery methods after the first phase of a complex project, about limitations of risk transfer and assumptions and consequences of the level of contingency funds assigned to a project. The effects of those decisions, among others, along with the unusual complications of building in a national park without land ownership and under the oversight of a uniquely structured authorizing agency, deserve robust analysis. The SFCTA is conducting a Project evaluation study with assistance from the University of Maryland and the University of Colorado in coordination with the Department. In addition, the Department is committed to conducting an exhaustive analysis and will publish a report on lessons learned and best practices with regards to the Project, and future P3 projects.

FINANCIAL RESOLUTION:

Resolved, that \$33,700,000 in Construction Capital be allocated to provide funds for project close-out on the P3 Presidio Parkway Project – Phase 2.

Project's Location:



“Provide a safe, sustainable, integrated and efficient transportation system to enhance California’s economy and livability”