



**SUPPLEMENTAL**

COUNCIL AGENDA:03/23/04  
ITEM: 3.9

# Memorandum

**TO:** HONORABLE MAYOR AND  
CITY COUNCIL

**FROM:** Scott P. Johnson

**SUBJECT:** SEE BELOW

**DATE:** March 23, 2004

Approved

Date

3/23/04

**COUNCIL DISTRICT:** City-wide  
**SNI AREA:** N/A

## SUPPLEMENTAL

**SUBJECT: UPDATE ON FUNDING ALTERNATIVES FOR THE CUSP PROJECT, AN INTEGRATED UTILITY BILLING, CUSTOMER SERVICE AND PERFORMANCE MONITORING SYSTEM**

### BACKGROUND

On March 10, 2004, staff presented an update on the CUSP project, an integrated utility billing, customer service and performance monitoring system, to the Making Government Work Better (MGWB) Committee. Included with the presentation was an ROI analysis that included a funding plan that would expand the City's commercial paper (CP) program to fund the project related costs. The MGWB Committee requested that staff also review and analyze two additional funding options in lieu of external borrowing; 1) use existing balances that may be available in the respective utility funds, and 2) borrow available balances from other funds. Staff computed the net present value of each option. Based on the analysis, the commercial paper program option would yield the lowest cost to the City with a net present value benefit of approximately \$1.36 million compared to borrowing project costs from other City funds. This supplemental memorandum provides the requested analysis.

### ANALYSIS

Although the Council previously directed staff to proceed with the request for proposal process for CUSP, given the current budget challenges, staff reviewed additional alternative solutions to be considered by the MGWB Committee. Based on the risks and costs associated with each option, the MGWB Committee directed staff to move forward and present two options to council; 1) proceed with CUSP, an off the shelf, licensed software solution with on-going technology support from the City's Information Technology Department; or 2) Contract with an outsource vendor for the CUSP system who would provide support for CUSP system. It should be noted that the outsource option would be a contractual arrangement between the City and a

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third party vendor over a two year period. The City would not own the CUSP project. In reviewing funding options, the Outsource option would not qualify for the commercial paper program described below due to the inability to capitalize and finance a system that the City would not ultimately own. The estimated total costs to implement the first option, through the "go-live" date are \$7.8 million. Go-live cost components include the following implementation and stabilization costs, which are to be expended over an eighteen-month implementation period once an implementation vendor has been chosen:

- Software;
- Hardware;
- Implementation vendor travel and related expenses;
- Initial software licensing;
- Dedicated city staff, lease space; and
- Project management and coordination.

As a means to fund the implementation costs for the CUSP project, staff has considered three alternatives as directed by the MGWB Committee. The table below lists each funding alternative, average annual project costs and opportunity benefits for each alternative, and the net present value of these components over a ten-year period. Discussion relative to each alternative considered is presented immediately following the table.

**CUSP Project Funding Alternatives**

Funding Alternative	Average Annual Project Payment <sup>(1)</sup>	Average Annual Opportunity Benefits <sup>(2)</sup>	Net Present Value - Total Cost to City
Use of Commercial Paper Program	\$932,165	\$346,466	\$(4,854,789)
Use of existing balances in respective utility funds <sup>(3)</sup>	N/A	N/A	N/A
Borrow available balances from other funds	\$940,263	\$200,145	\$(6,195,639)

(1) Average annual payments are calculated over a 10-year payback period for each option (principal, interest and borrowing costs), amortized from the first year the respective option would go live. Assumes the annual operating revenues for each utility service receiving benefit would fund the amortized repayment amounts.

(2) Average annual opportunity benefits include the continued ability to earn interest on funds remaining in City Investment Pool.

(3) Based on a pro-rata distribution of project costs, existing funds are insufficient to fund the required go-live costs for the CUSP project.

*It should be noted that the average annual payment is one-half of one percent (0.5%) of total annual revenues of \$170 million generated by the four City utility services benefiting from the project. The impact on future rates has not been calculated. The model assumes that the annual payments would begin in fiscal year 2006-07 (the first year following implementation.)*

Use of Commercial Paper Program

Staff has reviewed an alternative to expand the use of the Commercial Paper program to include the go-live costs of the CUSP project. Under the Commercial Paper alternative, the City would issue commercial paper notes as cash expenditures are paid for project implementation costs over an estimated eighteen-month period. The repayment, including interest and borrowing costs, would be amortized over a ten-year period, beginning in fiscal year 2006-07 (when the CUSP system would “go-live” and becomes available for use).

Using the Commercial Paper program to fund CUSP project costs allows the City to maintain existing cash reserves necessary to fund existing operations, while prolonging the City’s ability to invest unexpended funds during the term of the payback period. As presented in the table above, the Commercial Paper program results in the most economic benefit for the City at the lowest cost to the City, from a net present value perspective (results in a savings of nearly \$1 million compared to borrowing up-front from internal City funds).

Use of Existing Balances in Respective Utility Funds

Staff has reviewed required project cost-sharing levels for the four utility funds that will receive direct benefits as a result of implementing CUSP:

<u>Fund</u>	<u>Share of Project Cost</u>
<i>Integrated Waste Management Fund (Fund 423)</i>	<i>\$ 4,400,000</i>
<i>Water Utility Fund (Fund 515)</i>	<i>\$ 960,000</i>
<i>Storm Sewer Operating Fund (Fund 446)</i>	<i>\$ 825,000</i>
<i>Sewer Service and Use Charge Fund (Fund 541)</i>	<i>\$ 1,615,000</i>

The pro-rata share of project costs for each utility fund is based on: 1) the number of annual bills sent to customers for each utility service; and 2) the amount of annual operating revenue generated by each utility fund.

After analyzing the respective utility fund’s projected budget “statements of sources and uses of funds” (including projected rate increases), the initial analysis indicates that funding may be available in the Water Utility and Sewer Service and Use Charge Funds while the levels of unrestricted fund balance available in the Integrated Waste Management and Storm Sewer Operating Funds are not sufficient to cover their pro-rata share of the CUSP project estimated costs.

Based on a pro-rata distribution of project costs, existing funds are insufficient to fund the required go-live costs for the CUSP project. Therefore, it would be necessary to borrow from available fund balances in other City funds.

Borrow From Other Funds

Staff continues to review the feasibility of borrowing cash resources available in other City funds to pay for the implementation costs of the CUSP project. Staff has identified the Sewer Treatment Connection Fee Fund (Fund 539) as a possible alternative to facilitate a loan for the CUSP implementation costs. The loan payback period would commence during fiscal year 2006-07, when it is anticipated that the CUSP project will go live. Payback periods and payment schedules would be established for each borrowing fund consistent with the levels of resources

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estimated to be available over the term of the loan. Loan payments would include interest commensurate with the amount earned by the City's Investment Pool.

Regardless of the amount loaned from another fund to cover the cost of the CUSP project, paying for the project using the borrowing alternative results in a \$7.8 million outlay of funds during the first two years of the project. Unlike the Commercial Paper funding option, expending all project-related funds from existing City cash balances results in lost opportunities for the City to invest the unexpended funds at a higher rate than the borrowing rate in the commercial paper program.

### CONCLUSIONS

In conclusion, based on the net present value calculations for each option, the City would be better off to utilize the expanded commercial paper program to fund the CUSP project costs. Staff estimates that the net benefit to the City for the commercial paper program compared to borrowing internally from other City funds would be approximately \$1.36 million. This net benefit is due to lower borrowing costs for the commercial paper program and increased interest earnings resulting from investing the City's cash on hand in the City pool. Additionally, in reviewing fund balance in other funds, staff was unable to identify a fund that has sufficient available balances or that does not have sufficient funds available to commit over a ten year period. Therefore, if Council directs staff to move forward with procuring the licensed CUSP solution, staff recommends expanding the City's commercial paper program to fund the project.

### COORDINATION

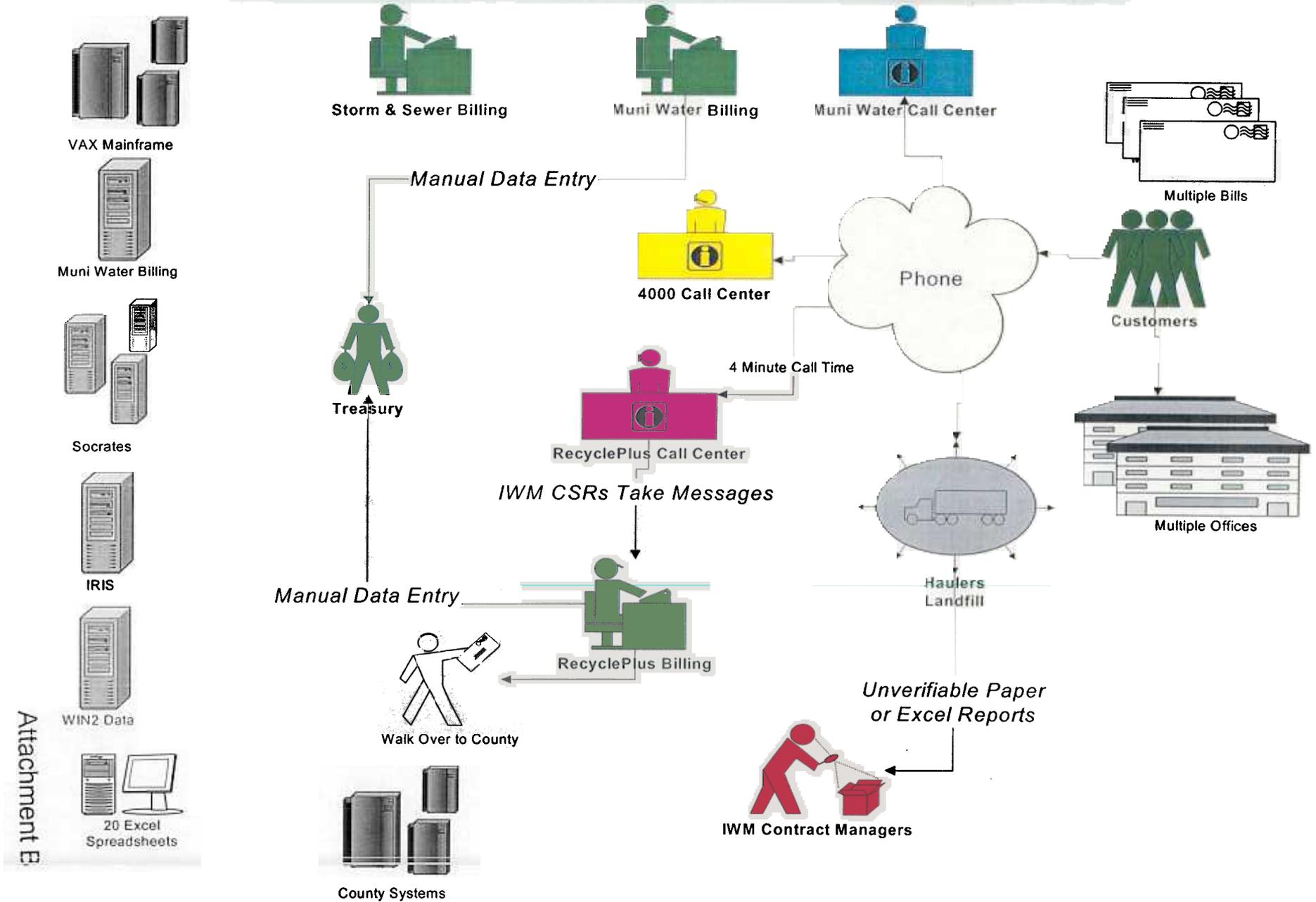
This memorandum has been coordinated with the Departments of Environmental Services, Information Technology and Finance and the Offices of the City Attorney, Budget and City Manager.

  
SCOTT P. JOHNSON  
Director, Finance Department

ATTACHMENT A

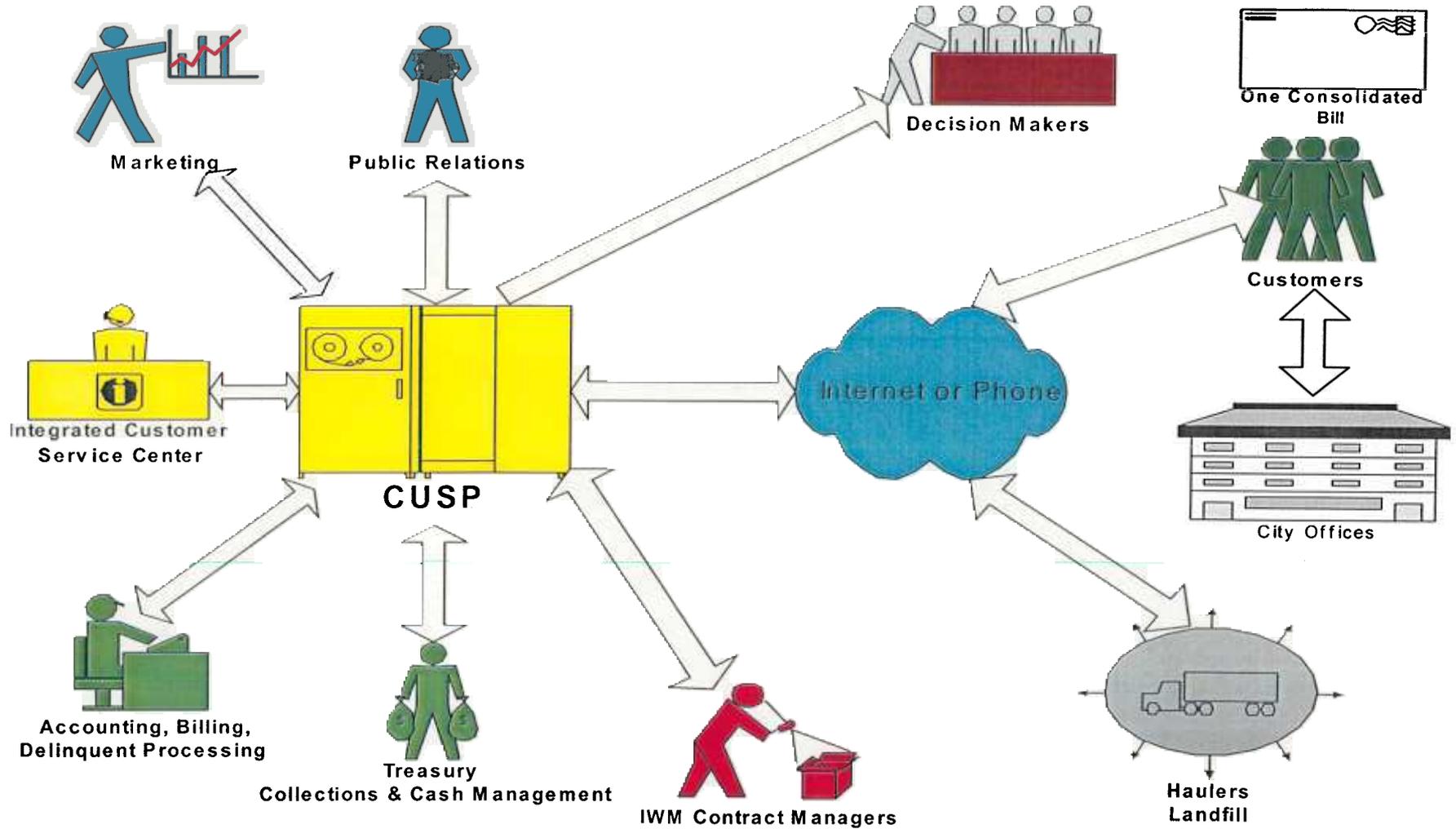


# Current Environment





# CUSP Conceptual Design



# Scope

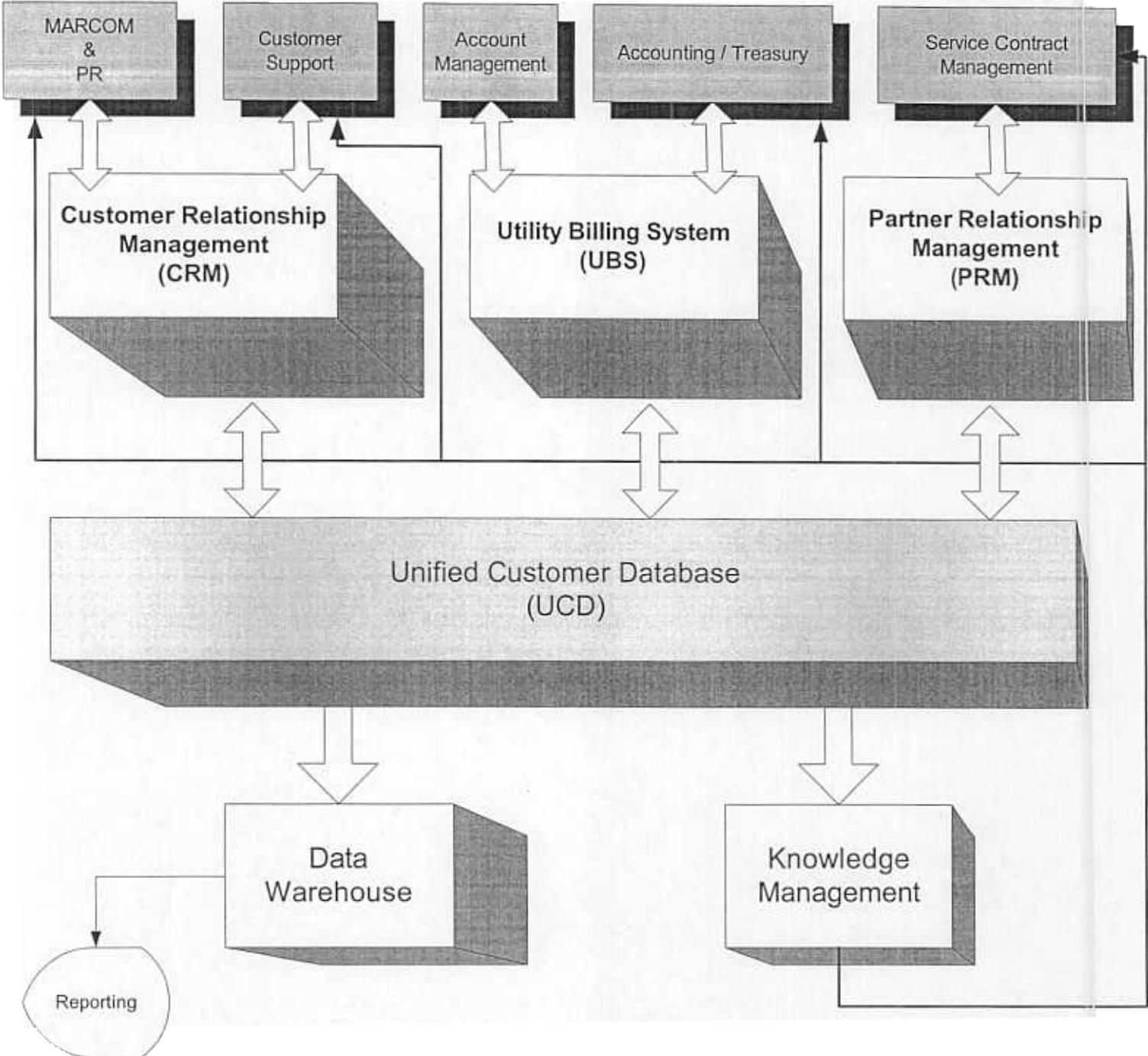
- Website Content
- Online Forums
- Event Management
- Fulfillment
- Media Relations
- Community Building

- email
- Chat
- Message Board
- Phone
- FAQ
- Forms
- Smart Documents

- 3<sup>rd</sup> Party Data
- New Accounts
- Account Maintenance
- Bill Printing & Mailing
- Online Acct Management
- Delinquent Accts

- MFD Updates
- Reporting
- Mail/Cash Deposits
- Automatic Deposits
- Online Payments
- Revenue Forecast

- Performance Monitoring
- Contract Maintenance
- New Contracts
- Document Mgmt
- Work Order Management



## CUSP Evaluation Methodology and Criteria

The following methodology was developed by the project team and with the help of TMG, an industry recognized CIS evaluation consultancy firm specializing in evaluation, selection and negotiations for procuring CUSP like systems.

**Phase 1: Minimum Requirements Review** - General Services Department staff screened the proposals to insure that they met the minimum requirements stated in the RFP.

**Phase 2: Functional Proposal Review** – An Evaluation Panel consisting of City Finance, ESD, City Manager’s Office and IT staff was formed to review all twelve proposals.

Phase 2 of the evaluation process was based on the following criteria:

Scoring Criteria	Weight	Definition
Domain Experience	30%	The proposals were evaluated based on their implementation experience with refuse and water service providers along with municipality experience. The selection team also considered the total number of live Customer Information System (CIS) installations the vendor has in the market.
Functionality	25%	The selection team evaluated and scored each proposer’s solution based on the functionality requirements outlined in the RFP.
Technical Architecture	10%	The selection team scored the vendors’ responses to the technical architecture requirements that were included in the RFP.
Conformance with City Technical Standards	20%	The selection team evaluated each proposal against the City’s IT standards requirements as outlined in the RFP.
Project Management	15%	The selection team evaluated and scored the proposals based upon the vendor’s responses to the Project Management questions in the RFP.
Costs	Considered	Considered after initial functional & IT evaluation

A detailed weighting of 500 features listed in the RFP was developed within the categories noted above. Each member of the evaluation team scored the proposals based on the criteria.

**Phase 3: Product Demonstrations, Cost Evaluation and Interviews** – This phase consisted of two major steps. Step one included one-day product demonstrations with concurrent technical and project management interviews with each proposer. These product demonstrations and technical sessions were facilitated by TMG and scored on functionality, ease of use, technology, and project management by Finance, ESD, Central Call Center, and IT staff.

The following criteria were used to identify the finalists:

<b>Criteria</b>	<b>Weight</b>	<b>Description</b>
Functional	45%	Using scripted demos, the evaluation team was able to get a very accurate picture of the percentage of matching features (San Jose would like to avoid customizations).
Technical	30%	A list of detailed technical questions was sent to vendors that were answered and sent back to the CUSP Technical Evaluation team.
References	Pass/Fail	The Detail Functional Evaluation team made reference calls to live vendor sites. A form was prepared and used for all calls. This process had a Yes/No rating.
Optional Features	10%	Vendor's ability to fulfill San Jose's needs in the next phases of CUSP and their strategic plan for consolidated customer service and billing for the City is at the center of this section. Scoring the Optional Features section of the proposals helped to determine the overall vendor score.
Vendor Viability	Pass/Fail	Research vendor's financial health and overall capacity to implement systems of this size in the CIS domain. Also, vendor history and standing with past customers was scrutinized. This section applies to the systems integrators as well as product vendors involved in a single proposal.
Project Management	15%	The vendors answered a list of questions and a participated in a one-hour interview with the CUSP project manager to determine vendor scores

Step two of this phase consisted of high-level product demonstrations and oral presentations to the CUSP Steering Committee. After reviewing the prior rankings and related rationale from the Evaluation Team, making observations and conclusions from the product demonstrations and oral presentations, considering the architecture required for each solution proposed by the three vendors and reviewing the cost proposals and proposed timelines for implementation by each of the three proposers, the CUSP Steering Committee moved two finalists forward for the final evaluation, scoring and ranking.

The following criteria was used by the Steering Committee to rank the finalists:

Scoring Criteria	Weight	Definition
Look and Feel	10%	Ease of use of each product was scored during a product demonstration by the vendor to the Steering Committee.
Functionality	10%	We evaluated the functional requirements against each vendor's demonstration of the high-level features.
Technical Architecture	10%	The vendors were evaluated based on a high-level technical architecture discussion.
Domain Experience	15%	The vendors were evaluated based on their implementation experience with refuse and water service providers along with municipality experience. The selection team also considered the total number of live CIS installations the vendor has in the market.
Project Management	25%	The selection team evaluated and scored the finalists based upon the vendor's presentation on Project Management methodology and experience.
Fit	30%	Solution fit with the City's IT master plan, resources and standards.

For the purpose of getting an independent, external perspective on the evaluation process and its fairness, Nanda Kishore, Chairman of BridgeSpan, reviewed the evaluation methodology and scoring details during this step of the evaluation process.

## Return on Investment (ROI) Bearing Point/ PeopleSoft

BEARING POINT/ PEOPLESOFT	Implementation Period	Stabilization Period	Go Live (Implementation + Stabilization)	Post Implementation Period										Total Costs
	Aug-04 Months 1-13	Aug-05 Months 14-18	Feb-06 Total	Feb-07 Year 1	Feb-08 Year 2	Feb-09 Year 3	Feb-10 Year 4	Feb-11 Year 5	Feb-12 Year 6	Feb-13 Year 7	Feb-14 Year 8	Feb-15 Year 9	Feb-16 Year 10	
<b>PROJECT COSTS</b>														
Yearly Direct Project Costs			\$0	\$510,045	\$186,396	\$183,051	\$1,519,700	\$176,055	\$172,399	\$168,633	\$164,754	\$160,759	\$156,644	\$3,398,437
Amortization cost				\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$975,000	\$9,750,000
<b>Total Project Costs</b>	\$0	\$0	\$0	\$1,485,045	\$1,161,396	\$1,158,051	\$2,494,700	\$1,151,055	\$1,147,399	\$1,143,633	\$1,139,754	\$1,135,759	\$1,131,644	\$13,148,437
<b>Present Value of Total Project Cost</b>	\$0	\$0	\$0	\$1,441,791	\$1,094,728	\$1,059,780	\$2,216,509	\$992,910	\$960,928	\$929,878	\$899,733	\$870,465	\$842,050	\$11,308,772
<b>PROJECT BENEFITS</b>														
Estimated Revenue Opportunity		\$0											\$1,685,009	\$15,701,408
Project Benefits - Yearly Estimated Efficiency Benefits		\$0		\$1,202,670	\$1,238,750	\$1,275,912	\$1,314,189	\$1,353,615	\$1,394,224	\$1,436,050	\$1,479,132	\$1,523,506	\$1,569,211	\$13,787,258
<b>Total Project Benefits</b>				\$2,628,281	\$2,694,702	\$2,763,009	\$2,833,257	\$2,905,504	\$2,979,811	\$3,056,239	\$3,131,252	\$3,208,515	\$3,288,096	\$29,488,666
<b>Present Value of Total Benefits</b>	\$0	\$0	\$0	\$2,551,729	\$2,540,016	\$2,528,545	\$2,517,312	\$2,506,314	\$2,495,545	\$2,485,002	\$2,471,839	\$2,459,058	\$2,446,652	\$25,002,012
<b>Net Present Value*</b>														\$13,693,240

\*Assumed discount rate of 3.0%