



Memorandum

TO: HONORABLE MAYOR, CITY
COUNCIL AND REDEVELOPMENT
AGENCY BOARD

FROM: Debra Figone
Harry S. Mavrogenes

SUBJECT: SEE BELOW

DATE: December 17, 2008

SUBJECT: GUIDELINES FOR CAPITAL IMPROVEMENT PROJECTS WITH ANNUAL OPERATING AND MAINTENANCE (O&M) COSTS IN THE GENERAL FUND

RECOMMENDATION

Accept staff's proposal to implement the City Council approved Budget Principle #8 pertaining to capital improvement projects with annual operating and maintenance costs to be paid from the General Fund.

OUTCOME

Acceptance of staff's proposal for implementing Budget Principle #8 allows City Administration and Redevelopment Agency staff to develop administrative guidelines to ensure that individual plans and projects that will likely exceed \$100,000 in new annual General Fund operating and maintenance (O&M) costs will have O&M cost estimates provided to be used in decision-making throughout project development. In addition, all capital improvement projects with new annual General Fund O&M costs will be detailed in the Five-Year General Fund Forecast released by the City Manager's Office annually. Land banking for non-specific uses and projects that will likely result in O&M cost savings to the General Fund will be exempt.

Budget Principle #8 states that capital improvement projects with O&M costs exceeding \$100,000 shall not proceed unless Council certifies that funding for the entire project, including O&M costs, will not require a decrease in existing basic neighborhood services. For most capital improvement projects, this certification will occur in conjunction with annual adoption of the Capital Improvement Program; project-specific certification will only be required for projects that were not previously certified and expected to begin construction prior to the next CIP adoption. Projects with ongoing O&M costs that are found to impact the delivery of existing basic neighborhood services will not be recommended for approval by the City Administration and Redevelopment Agency.

BACKGROUND

As part of the 2008-2009 budget process, the City Council adopted the Budget Principles recommended in the Mayor's March 2008 Budget Message. Budget Principle # 8 pertains to capital improvement projects and directs that capital improvement projects with annual O&M costs "shall not proceed for projects with annual operating and maintenance costs exceeding \$100,000 in the General Fund without City Council certification that funding will be made available in the applicable year of the cost impact. Certification shall demonstrate that funding for the entire project, including operations and maintenance costs, will not require a decrease in existing basic neighborhood services."

On September 23, 2008, Council approved staff's recommendation as part of Council Agenda Item 9.1 that Budget Principle #8 be interpreted so that the Council makes a certification that (1) funding strategies will be pursued so that the projected funding for operation and maintenance of the project will be made available in the first year of operation and (2) appropriate efforts will be undertaken so that those funding strategies cover the entire cost of the project, including operations and maintenance costs, so as to not require a decrease in existing basic neighborhood services.

ANALYSIS

In order to implement the budget principle, staff will draft administrative guidelines to ensure that the City Council has a comprehensive picture of the O&M impacts on the General Fund of all capital improvement projects. In the past, the anticipated O&M impacts on the General Fund of Agency and City-funded capital improvement projects were often not included for City Council consideration during the early stages of project development. However, the proposed approach will ensure that O&M impacts to the General Fund, regardless of the construction funding source, are considered early in project development and within the context of other budget needs. The planned administrative guidelines will be consistent with Council Policy No. 1-18, which sets forth the overall guiding principles for the preparation and administration of the Operating Budget and Capital Improvement Program.

In summary, staff's recommended approach is to explicitly incorporate estimates and discussion of O&M costs throughout the development of master plans and individual CIP projects. City Council certification related to O&M costs will occur (a) as part of the annual CIP adoption process, or (b) individually for major projects not included or modified since CIP adoption.

Including O&M in Project Scoping and Development:

To ensure that potential O&M impacts are identified and brought to Council for timely consideration throughout the year, project delivery staff will incorporate O&M cost analyses into feasibility studies and coordinate with staff from City operating departments on master plans, capital improvement projects, and turnkey projects. Specifically, when funding and scopes of work are set for project development activities such as community outreach and project feasibility studies, staff will include the development of likely General Fund and total O&M cost

estimates. In addition, for Strong Neighborhood Initiative (SNI) Projects, Agency and City staff will work together to engage the community in discussions that attempt to align neighborhood and community project priorities with potential ongoing O&M costs.

As the budget principle applies specifically to capital improvement projects with O&M costs to be paid from the General Fund, costs to operate and maintain capital improvements (e.g. operating staff, custodial, grounds maintenance, utilities, supplies, etc.) will be specifically addressed. Capital replacement costs, as well as furniture, fixtures and equipment costs have NOT been included, in recognition that this issue must be addressed separately for existing as well as proposed capital improvements.

Recognizing that information will be less certain at the earliest stages of project development, estimated O&M costs may be limited to ranges and non-specific future dates but will reflect the best available estimate of costs associated with long-term City responsibility for the project. Land banking, where future uses have not been specified, would be exempt from this requirement. As costs are further defined throughout the project development, updates of these costs will be highlighted through the Forecast, CIP, or when requiring subsequent City Council action related to development of the project.

Where a project is expected to have a new cost impact that exceeds \$100,000 in annual O&M to be paid from the General Fund, scopes of work for studies and City Council approval recommendations will specifically address estimated O&M costs. The calculation of "new" costs will deduct current costs to be eliminated by a planned project. Accordingly, projects that will clearly result in a net General Fund savings compared to current expenditures will not be required to conduct detailed analyses.

Specific milestones for reporting this information will vary by individual projects, but would include the following stages of project development when City Council approval is otherwise involved:

- a. Approval of real property acquisitions for public facilities (excludes land banking)
- b. Adoption of SNI neighborhood plans, master plans, and concept plans that include new or renovated public facilities
- c. Approval of architectural, engineering, and construction management agreements for public facilities
- d. Award of construction contracts for public facilities
- e. Approval of agreements with developers for turnkey projects for public facilities

SNI neighborhood plans, program level master plans and concept plans represent visioning documents that typically result in the development and implementation of subsequent capital projects. In such instances, staff will provide the best available estimate of O&M costs at the time of plan approval, but City Council O&M certification action will be tied to the subsequent projects and not required for the plan.

City Council Certification of O&M Costs:

Project-specific O&M costs will be summarized and reported as part of the General Fund Five-Year Forecast, and City Council certification recommended as part of the annual Proposed Capital Improvement Program. The 2010-2014 Preliminary General Fund Five-Year Forecast is consistent with the implementation guidelines described in this memorandum. This Forecast, released in November 2008, identifies General Obligation Bond-funded capital projects previously approved by the City Council and other previously approved capital projects with General Fund O&M costs greater than \$100,000 annually. It is important to note that future potential capital projects not previously included in a City Council-approved City Capital Improvement Program or Agency Budget are identified separately and are not included in the Forecast estimates of General Fund expenses. These projects would not be incorporated into the Forecast projections until the City Council/Agency Board, as applicable, has approved these projects and the City Council has made the O&M certification.

A project will require certification action outside of the annual budget development process if it was not certified as part of the preceding annual CIP adoption and is likely to proceed to construction prior to the next CIP adoption. Recommendations on these individual projects will be brought forward for City Council consideration of certification at the earliest suitable milestone in project development. Standard language will be added to City Council memoranda that highlight anticipated O&M impacts to the General Fund within the context of the latest General Fund Forecast.

EVALUATION AND FOLLOW-UP

Upon City Council approval of these recommendations, staff will finalize and implement these guidelines through project development procedures and the annual Five-Year General Fund Forecast.

PUBLIC OUTREACH/INTEREST

- Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater.
- Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City.
- Criterion 3:** Consideration of proposed changes to service delivery, programs, or staffing that may have impacts to community services and have been identified by staff, the Board or Council, or a community group that requires special outreach.

COORDINATION

This memorandum has been coordinated among affected departments and the City Attorney's Office.

HONORABLE MAYOR, CITY COUNCIL AND AGENCY BOARD

December 17, 2008

Guidelines for Capital Improvement Projects with Annual O&M Costs in the General Fund

Page 5

CEQA

Not a project.



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For questions please contact ED SHIKADA, Deputy City Manager at 408-535-8190.