

Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: RICHARD DOYLE
City Attorney

SUBJECT: Settlement Agreement and
Release Between City and
Applegate Johnston – Fire
Station No. 19

DATE: December 14, 2011

RECOMMENDATION

Authorize the City Attorney to execute a settlement agreement and release with Applegate Johnston, Inc. waiving the City's liquidated damages claim on the Fire Station No. 19 project as consideration for Applegate Johnston's making certain modifications on the Environmental Innovation Center project.

OUTCOME

Approval of the settlement and authorization of the City Attorney to execute the settlement agreement.

BACKGROUND

During July, 2008, the City awarded Applegate Johnston, Inc. a contract for the construction of Fire Station No. 19. Applegate Johnston has completed construction of Fire Station No. 19.

The construction contract for Fire Station No. 19 provided for the assessment of liquidated damages if Applegate Johnston did not complete the project on time. In the engineer's final estimate for the project, the City claimed that Applegate Johnston was late in completing the project and sought \$282,000 in liquidated damages. Applegate Johnston disputed that it owed all of the liquidated damages claimed by the City.

During May 2011, the City awarded Applegate Johnston a contract for construction of the Environmental Innovation Center ("EIC") valued at approximately \$11,000,000. Concurrently, the City was also negotiating a New Markets Tax Credit ("NMTC") financing for the EIC project in the amount of approximately \$4,500,000. The NMTC lenders required the City to demonstrate a commitment to constructing the EIC project by the selecting a contractor for the project and awarding a construction contract.

After executing the construction contract for the EIC project, the NMTC lenders informed the City for the first time that Applegate Johnson would need to comply with additional insurance and bond requirements. Although the additional insurance and bond requirements tend to be standard lender requirements in a private development, they are not typical requirements in public works contracts.

Applegate Johnson informed the City that it would provide the additional insurance and bond requirements only if the City waived its liquidated damages claim on the Fire Station No. 19 project. The City was at risk of losing the NMTC financing if Applegate Johnson did not agree to provide the additional insurance and bond requirements being mandated by the NMTC lenders. In addition to losing the financing, the City would have been at risk of incurring up to \$250,000 in costs from other parties, and of not being reimbursed for approximately \$120,000 in due diligence expenses.

The NMTC lenders were requiring that the financing close on or before October 31, 2011. Based on staff's representations that it would recommend approval of the settlement contained in this memorandum, Applegate Johnson – acting in good faith – proceeded to obtain the necessary additional insurance and bond requirements. The NMTC financing has since closed, resulting in the City obtaining the additional NMTC funding for the EIC project.

ANALYSIS

The NMTC lenders required the City to bid the EIC project and enter into a construction contract to show a commitment to constructing the EIC project. However, the NMTC lenders put the City in a difficult position by notifying the City of additional insurance and bond requirements *after* the execution of the construction contract with Applegate Johnson. While the City has the authority to require a contractor to make changes in the scope of the work after the award of a construction contract, it generally does not have the same authority with regard to mandating changes in the other terms and conditions of the agreement.

Staff explored other alternatives to satisfying the additional insurance and bond requirements, including requesting the NMTC lenders to waive the requirements and having the City purchase the necessary insurance and bonds. The NMTC lenders refused to waive the requirements. Moreover, staff estimated that it would cost the City *at least* \$300,000 to purchase the bonds and insurance – although the cost for the contractor to obtain what was necessary to comply with the requirements was likely substantially less. Moreover, it was unlikely that the City could have achieved the purchase of the bonds and insurance before the October 31, 2011 close date.

In short, waiving the disputed liquidated damages claim on the Fire Station No. 19 project was the City's most reasonable alternative. For this reason – and because Applegate Johnson has, in good faith, already obtained the insurance and bonds

December 14, 2011

Subject: Fire Station No. 19 Settlement

Page 3

needed to close the NMTC financing - the City Attorney's Office recommends authorizing the City Attorney to execute the settlement agreement waiving the City's liquidated damages claim on the Fire Station No. 19 project as consideration for Applegate Johnston's having obtained the necessary insurance and bonds.

This Office has been informed that, the Environmental Services Department proposes to transfer \$250,000 to the Fire Department to partially replace the waived liquidated damages on the Fire Station No. 19 project. The proposed source of the funds would be a \$250,000 "developer fee" that will be paid to the City next fiscal year upon completion of the lien-free construction of the EIC as part of the NMTC funding program. The proposal would be that the Fire Department's capital budget would receive the funding to supplement its budget for Fire Station No. 21 and Fire Station No. 37 projects. Staff has indicated that it will seek whatever budget actions are needed at a later date.

PUBLIC OUTREACH/INTEREST

This memorandum and the proposed settlement agreement have been posted on the City's website for the January 10, 2012 City Council agenda.

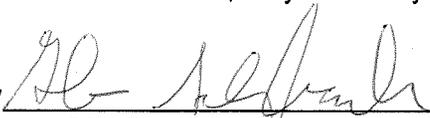
COORDINATION

The City Attorney's Office has coordinated the terms of the proposed settlement with the departments of Public Works and Environmental Services, and the City Manager.

CEQA

Not a Project; File No. PP10-066(h), Settlement Agreements.

RICHARD DOYLE, City Attorney

By 

GLENN SCHWARZBACH
Senior Deputy/City Attorney

cc: Debra Figone, City Manager
David Sykes, Director of the Department of Public Works
Kerrie Romanow, Acting Director of Environmental Services

For questions please contact Richard Doyle, City Attorney, at (408) 535-1900