

CITY OF SAN JOSE

2018-2019 PROPOSED CAPITAL BUDGET

BUDGET POLICIES

The Capital Budget and the Capital Improvement Program are prepared and administered in accordance with several sources of policy direction. First, the City Charter requires that the budget be balanced, include a complete financial plan for all City funds, and meet certain legal deadlines for submittal. Second, the City Council has established two budget policies: (1) the Operating Budget and Capital Improvement Program Policy (Council Policy 1-18), which includes guidelines, standards, and requirements for preparation and monitoring of both the Operating and Capital Budgets; and (2) the Estimating Construction Costs and Development of Project Budget Policy (Council Policy 8-12), which establishes guidelines for estimating construction project costs and developing project budgets (the complete text of the applicable adopted policies is presented below). Third, the budget is developed in accordance with the Mayor's budget priorities and direction as approved by the City Council in March and June of each year. Fourth, recommendations of special studies by Council-appointed task forces, boards, commissions, and committees may be considered upon the direction of the City Council. Finally, public input is considered throughout the process, with scheduled public hearings at key City Council decision points.

OPERATING BUDGET AND CAPITAL IMPROVEMENT PROGRAM POLICY (COUNCIL POLICY 1-18) (Partial Text)

CAPITAL IMPROVEMENT PROGRAM

1. Fiscal Policies

- a) Capital project proposals should include complete, reliable, and attainable cost estimates. Based upon a thorough analysis of the project, project cost estimates for the Five-Year Capital Improvement Plan will vary in reliability depending upon whether they are to be undertaken in the first or fifth year of the Plan. Project estimates for the Five-Year Capital Improvement Plan should include the basis on which the project costs were prepared (conceptual design, master plan, etc.), and the relative reliability of those estimated costs.
- b) Capital project proposals should include a comprehensive resource plan. This plan should include the amount and type of resources required, and the funding and financing strategies to be employed. The specific fund and timing should be outlined. The plan should indicate resources needed to complete any given phase of a project in addition to the total project. The City Manager's Office is responsible and accountable for providing Council with an accurate, comprehensive resource plan.
- c) Changes in project estimates for the comprehensive resource plan shall be fully reported to the City Council for review and approval.
- d) Project proposals should indicate the project impact on the operating budget. Each project that is proposed in any year of the Five-Year Capital Improvement Program shall have an estimate of the costs for furniture, fixtures, equipment, and technology and the annual operations and maintenance costs in the appropriate year of the Operating Budget or in the Five-Year Forecast and Revenue Projections.

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**OPERATING BUDGET AND CAPITAL IMPROVEMENT PROGRAM POLICY
(COUNCIL POLICY 1-18) (Partial Text)**

CAPITAL IMPROVEMENT PROGRAM

1. Fiscal Policies (Cont'd.)

- e) During the annual Capital Budget process for multi-year budgeted projects, the City Manager will provide the Council with more information regarding the project including the original budget, budget addendums, and the projected schedule in spreadsheet format.
- f) At the time of award of the construction contract, each project shall include reasonable provision for contingencies.
- g) At the time of award of the construction contract, each project shall include reasonable provisions for furniture, fixtures, equipment, and technology that are separately identified in a line item or items in the construction budget and those costs shall be noted in the staff report to the Council.
- h) At the time of award of the construction contract, each project's estimated annual operating and maintenance costs shall be identified in the staff report to the Council and shall be included in the Operating Budget or in the Five Year Forecast and Revenue Projections for projects expected to be completed after the end of the budget year.
- i) The contingency amounts to be used for various types of projects were approved by the City Council on December 3, 2002 and amended on December 15, 2009, and are as follows:
 - 5% of the total contract for street, sidewalk and park projects;
 - 10% of the total contract amount for trails, utilities and building projects;
 - 15% of the total contract amount for building renovation projects; or
 - Such other amounts as approved by the Mayor/City Council for a particular project.
- j) Project contingencies may, unless otherwise determined by the City Council, be used only to compensate for unforeseen circumstances requiring additional funds to complete the project within the original project scope and identified needs.
- k) For budgeting purposes, project contingencies are a reasonable estimating tool. At the time of contract award, the project's budgeted appropriation, including contingency, will be replaced with a new appropriation equal to the approved project contract contingency developed in the manner described above.
- l) The City Administration shall seek ways of ensuring that administrative costs of carrying out the Capital Improvement Program are kept at appropriate levels.

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**OPERATING BUDGET AND CAPITAL IMPROVEMENT PROGRAM POLICY
(COUNCIL POLICY 1-18) (Partial Text)**

CAPITAL IMPROVEMENT PROGRAM

1. Fiscal Policies (Cont'd.)

- m) The Annual Capital Budget shall include only those projects that can reasonably be accomplished in the indicated timeframe. Multi-year budgeting of projects shall be used to ensure a reasonable timeframe for projecting costs. The detail sheet for each budgeted capital project should include a projected schedule.
- n) The status of all capital projects, and the entire Capital Budget, will be monitored by the Mayor/Council as part of the Mid-Year Budget Review. Large projects of crucial importance may be monitored on a more frequent basis as determined by the City Council.
- o) Capital projects that are not encumbered or completed during the fiscal year will be re-budgeted to the next fiscal year except as reported to and subsequently approved by the City Council. All re-budgeted capital projects should be so noted in the Proposed Capital Budget.

2. Capital Improvement Plan Policies

Public participation in the Capital Improvement Program is a priority concern for the City. Among the activities conducted to address this need are the following:

- a) The Capital Improvement Plan shall be provided to the City Council in a timely manner as required by the City Charter to allow for Council members to review the proposal with constituents before it is considered for adoption.
- b) Council budget review study sessions on the Capital Improvement Plan shall be open to the public and advertised sufficiently in advance of the meetings to allow for public attendance.
- c) Prior to the adoption of the Capital Improvement Plan, the City Council shall hold noticed public hearings to provide an opportunity for residents to express their opinions on the proposed plan.
- d) The City Planning Commission shall review the proposed Capital Improvement Plan and provide their comments on its contents before the Council considers the plan for final adoption.

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**OPERATING BUDGET AND CAPITAL IMPROVEMENT PROGRAM POLICY
(COUNCIL POLICY 1-18) (Partial Text)**

CAPITAL IMPROVEMENT PROGRAM

2. Capital Improvement Plan Policies (Cont'd.)

- e) All projects included in the Capital Improvement Program shall be consistent with the City's General Plan and the City's Energy and Water Policies. The goals and policies within the General Plan relating to community development, housing, services and facilities, transportation, solid waste, aesthetic, cultural and recreational resources, natural resources, and hazards should be followed in the development of the Capital Improvement Plan. The General Plan service-level goals will be clearly stated in the Capital Improvement Program.
- f) Capital projects shall be financed to the greatest extent possible through user fees and benefit districts where construction of the project results in direct benefit to users.
- g) The Council will annually review and establish criteria for measuring proposed capital improvement projects. Among the factors that will be considered for priority ranking are the following:
 - Projects that have a positive impact on the operating budget, such as reduced expenditures or increased revenues.
 - Projects that are programmed in the Five-Year Operating Budget Forecast.
 - Projects that can be completed or significantly advanced during the Five-Year Capital Improvement Plan.
 - Projects that can realistically be accomplished during the year they are scheduled.
 - Projects that implement prior Council-adopted reports and strategies.
- h) Projects that involve inter-governmental cooperation in planning and funding should be established by an agreement that sets forth the basic responsibilities of the parties involved.

3. Debt

The City Council adopted a Debt Management Policy (Council Policy 1-15) that establishes the following equally important objectives:

- a) Minimize debt service and issuance costs.
- b) Maintain access to cost-effective borrowing.
- c) Achieve the highest practical credit rating.
- d) Full and timely repayment of debt.
- e) Maintain full and complete financial disclosure and reporting.
- f) Ensure compliance with applicable state and federal laws.

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**OPERATING BUDGET AND CAPITAL IMPROVEMENT PROGRAM POLICY
(COUNCIL POLICY 1-18) (Partial Text)**

CAPITAL IMPROVEMENT PROGRAM

3. Debt (Cont'd.)

As described in Council Policy 1-15, prior to bringing forward a lease financing (financing the acquisition, construction, or improvement by the City of real property or equipment) to the City Council for approval, the Finance Department shall perform initial due diligence on the project to be financed. The due diligence will include identifying the revenue source for repayment, and performing a feasibility study to determine the volatility of the revenue and provide a sensitivity analysis on project revenue projections, including worst/best case scenarios and the impact on any repayment source identified as the backstop to the project revenues. In order to proceed with the preparation of the documents necessary for the lease financing, two-thirds majority approval by the City Council of the proposed plan of finance is required. When the lease financing is brought forward for City Council approval, the Finance Department will provide the City Council with an update to the due diligence report and any feasibility study. Approval of the lease financing will require two-thirds majority approval by the City Council. These provisions do not apply to a refunding of a lease financing transaction.

In order to reduce principal on outstanding debt and minimize debt service costs, one-time savings generated from debt restructurings and refundings should be used to pay down the outstanding principal of other existing City debt, whenever possible, taking into consideration any fund restrictions.

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ESTIMATING CONSTRUCTION COSTS AND DEVELOPMENT OF PROJECT BUDGET POLICY (COUNCIL POLICY 8-12)

The City Council adopted on August 22, 2000, an Estimating Construction Costs and Development of Project Budget Policy (Council Policy 8-12) to improve the quality and effectiveness of the City's Capital Budget Process and accuracy of capital project construction by assuring that:

1. Capital projects have realistic budgets.
2. The City Council has enough information and data to establish the budget once a project is approved.
3. The public is clearly informed about project "budgets".

This policy improves the Capital planning and budgeting process by setting definitions of project estimation relative to the degree of project design definition and level of completion. The policy establishes a consistent and uniform approach for estimating and reporting construction project costs and establishing realistic construction project budgets.

POLICY

"Program" and "Preliminary" level estimates are useful tools in a long-term capital budget planning process. However, an estimate must have a level of certainty provided by a "Budget" level estimate to realistically establish a final project.

From project initiation as a concept through the award of a construction contract, there are six essential milestones or steps in the development of a project. These steps are shown below.

At various points within these steps, four different kinds of estimates that are prepared as the project progresses from start to finish. As more detail, specificity and definition are developed through the stages of design, these estimates become more certain and realistic as noted below.

The six milestones or steps in a project and the point at which these estimates are prepared are as follows:

<u>Project Milestone/Phase</u>	<u>Type of Estimate</u>
1. Project Initiation	Program Estimate
2. Planning/Programming	Preliminary Estimate
3. Design	
Conceptual Design	
Schematic Design	Budget Estimate
4. Construction Documents/ Bidding/Contract Award	Engineer's Estimate
5. Construction	
6. Occupancy/Opening	

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POLICY

The four estimates are defined by this policy as follows:

- **The “Program Estimate”** is created in the Project Initiation Phase for the long-term, multi-year planning and for initial feasibility studies. It is based on a general description of the project as a concept and does not include any design, architectural work or detailed scope. It may typically include components for land acquisition, design, construction, and construction management.
Level of Certainty: $\pm 35\%$
- **The “Preliminary Estimate”** is prepared during the Planning/Programming Phase and is based on an initial program containing building and site square footages and general site work. It is typically not based on any formal engineering or architectural work, which usually has not yet occurred. The Preliminary Estimate is most commonly used to develop the next year’s budget or to add a project to a current year budget to allow for further design development. For smaller projects of shorter duration and minimal complexity, the Program Estimate step may be eliminated in favor of the Preliminary Estimate.
Level of Certainty: $\pm 20\%$
- **The “Budget Estimate”** is prepared during the Schematic Design Phase and is based on a defined scope and schematic design work. It is prepared using estimated material quantities and unit prices taken from the plans and applying a general unit cost to each item. This estimate includes all changes in definition and scope that have been identified and incorporated into the project design since the Preliminary Estimate. Items associated with the commencement of construction such as bonds, insurance, mobilization and overhead costs are also included. This estimate is used for evaluating project alternatives, value engineering, and evaluation of the project budget established by the Preliminary Estimate in the Planning/Programming Phase. For projects of a multi-year duration, the Budget Estimate should include an inflationary factor that escalates the cost to the dollar value at the mid-point of the construction schedule.
Level of Certainty: $\pm 10\%$
- **The “Engineer’s Estimate”** is a detailed estimate prepared using the final construction documents prior to bidding and contract award. It is prepared using unit prices for exact quantities of materials and labor taken from the plans. The Engineer’s Estimate is used to establish the final funding within the budget and to evaluate bids received.
Level of Certainty: $\pm 5\%$

Smaller projects of shorter duration may not require all four levels of estimates. In most cases, however, a larger project would require as a minimum “Preliminary”, “Budget”, and “Engineer’s” estimates.

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**ESTIMATING CONSTRUCTION COSTS AND DEVELOPMENT OF PROJECT
BUDGET POLICY (COUNCIL POLICY 8-12)**

POLICY

To support the establishment and implementation of this policy, a set of detailed administrative procedures to be followed for project managers and staff engaged in capital construction projects will be developed. These procedures are to provide specific and detailed instructions and guidelines on how and when estimates are prepared, reviewed and approved in accordance with this Council Policy.