OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Civic Center Complex

OVERVIEW

On Monday, July 19, 2010 the City Council is being asked to approve the necessary actions to move forward with the proposed design and construction of a new Civic Center Complex. The significant actions being requested of the City Council include:

- Approve submission of a proposition on the November 2, 2010 ballot to approve the execution of an agreement for the design and construction of a new Civic Center Complex.
- Authorize the Chief Financial Officer to appropriate and expend up to $293.5 million from the newly created Capital Improvement Project – San Diego Civic Center Complex contingent upon approval of the ballot measure.
- Authorize the Mayor to enter into any contracts necessary for the design and pre-development of the Civic Center Complex in an amount not to exceed $7.6 million. The $7.6 million includes $2.0 million from reserves in Fiscal Year 2011 and an additional $5.6 million in Fiscal Year 2012. It should be noted that the $5.6 million will require a future action either through the Fiscal Year 2012 Budget Process or through a separate action. Staff anticipates reimbursing the $7.6 million from bond proceeds in late Fiscal Year 2012.

The purpose of this report is to review the proposal for a new Civic Center Complex as presented by the Mayor. For our analysis we have relied on the numbers presented by Jones Lang LaSalle (JLL). Our office has been given access to the spreadsheets developed by JLL for their assumptions. In addition, we have had direct access to JLL staff to further discuss the basis for the assumptions.

FISCAL/POLICY DISCUSSION

What are the Changes from the Original Civic Center Proposal presented in June 2009 to the Revised Proposal?

The following chart provides an overview of the significant changes from the Original proposal presented in June 2009 to the revised proposal. We have also provided additional information related to the changes to augment what has already been provided to the City Council.

Features of June 2009 Concept Proposal Versus Final Civic Center Proposal

Feature	Original	Revised
Cost (Before Financing)	$440 Million	$293 Million
Total Gross Square Footage (GSF)[1]	983,816	576,093
Cost Per GSF[2]	$447	$509
Total Office GSF	964,756	560,006
Number of Employees	3,140	2,420
Space Requirement as of 2013	660,659	479,288
Office Space per Employee[3]	210 SF	198 SF
Meets Needs Until:	2060+	2025[4]
Employee Growth Projected	Flat 2012-2015, .6%/2015-2060	Flat 2012-2015, .6%/2015-2060
Council Chambers Square Footage	22,990 SF	20,744 SF
Data Center	10,000 SF	None[5]
Sustainability Features	LEED-NC Silver	Minimum LEED-NC Silver
Underground Parking Spaces	1,576	461[6]
Ground Floor Retail	19,060 SF	16,087 SF
Private Sector Development	2.0 Million SF	None[7]
Fire Station #1	Addressed but costs not included in GED's proposal	No Immediate Plans
Emergency Operations Center	Not addressed	Not addressed
City Operations Building Status	Redeveloped	Vacated, No Immediate Plans

[1] Does not include GSF related to subterranean parking

[2] Includes Subterranean Parking, Voice and Data Infrastructure, Furniture, Fixtures, and Equipment expenses

[3] Formula is Space Requirement as of 2013/Number of Employees

[4] New 40,000 GSF Public Utilities Building required in 2025 and additional lease space thereafter

[5] Will remain at Existing Rose Canyon Facility

[6] These spaces would be in addition to the 1,100 spaces in the Evan Jones Parkade

[7] Blocks 1, 13 and 15 will be available for future redevelopment

Changes in Building Size

The 660,000 square feet of office space needs projected for the Original proposal were significantly overinflated and did not correlate with the City's current budget reality or fully reflect the significant staff reductions of the past several years. The original proposal reflected space requirements for 3,141 employees compared to 2,420 employees for the smaller building. At the same time, the usable space assumed per employee has been only slightly reduced between the original building (210 SF/employee) and the revised building (198 SF/employee). Both are in line with the office space standards associated with newer, more efficient office facilities.

While both buildings continue to reflect growth requirements of .6% per year beginning in 2016, nearly all of the 142,000 square feet of growth space assumed in the original building space projections has been eliminated in the revised building. The original building was projected to accommodate the City's space needs for 47 years, through 2060. The revised building will meet the projected growth until 2025, at that time a second building sized at 40,000 square foot is projected to be needed (twelve years after move-in) to provide additional space outside of City Hall. An additional 102,000 square feet of space may need to be built or leased through 2034-2060 to accommodate additional growth. These costs have been reflected in the projections for the revised building as compared to the "Hold Steady" option.

An issue to consider is the economics of constructing a larger facility at today's favorable construction costs (increasing costs today but providing sufficient office space into the future), versus a smaller building which will require construction of a second 40,000 GSF building in 2025 and additional leased space starting in 2035 to meet space needs through 2060.

Data Center

The original proposal included a 10,000 square foot Data Center located in the proposed facility. This facility was to function as the City's primary facility for electronic and voice connectivity for City employees. The estimated costs for the Data Center were $3.5 million. The revised proposal does not include a Data Center. Staff has stated that the decision to omit the Data Center from the new facility was based on a "cloud computing" approach whereby all departmental data and application resources will be housed at an off-site facility. It is unclear how this change will impact the City's current Data Center located in Rose Canyon and operated by San Diego Data Processing Corporation.

Sustainability Features

The revised proposal will include a City Hall built to LEED-NC Silver standards which is consistent with the original proposal. In addition, the revised proposal includes many eco-friendly design elements that are consistent with the original proposal.

It should be noted that for cooling, the revised proposal continues to use a combination of the City's existing systems and a proposed connection to NRG's current Energy Center. In addition, the revised proposal anticipates that a satellite NRG chilled/hot water plant will be located on the new Civic Center premises. NRG Energy currently supplies district cooling to buildings in a four-square mile service area in the central business district of San Diego.

Staff has stated that the existing cooling plant has four chillers that were installed in 2003. The current chillers have a 1,300 total ton capacity that services COB, CAB, Golden Hall, and the Civic Theatre. The new facility will need 500 – 1,700 tons of capacity, depending upon whether or not there is on-site storage. Connecting to the current NRG loop would require the City to pay a nominal cost and the expenses would be based on either having to buy additional capacity (in lieu of adding size or storage) or selling of excess capacity (if storage is ultimately added). In the event that an acceptable arrangement cannot be made with NRG, on-site capacity can be increased for up to $2.0 million, which is provided for in the "sustainability" line item of the budget which totals $7.2 million.

Underground Parking

The original proposal provided 1,576 new underground parking spaces. The revised proposal includes 461 underground spaces. This would be in addition to the 1,100 spaces located in the Evan Jones Parkade. Currently 1,112 City employees park in the Evan Jones Parkade and the World Trade Center. In buildings where the City leases space, the City has no parking allocations, and employees purchase their parking spaces directly from the building owners. As of July 12, 2010, the number of employees who have parking at the leased facilities include three employees at 600 B Street and 110 employees at the Executive Complex. No data is available for the Civic Center Complex building.

Retail Space

The original proposal contained 19,060 Gross Square Feet (GSF) of retail space. In addition, the original proposal called for Gerding Edlen to master lease the space through the bond financing period, after which the City would directly lease retail space to tenants. The revised proposal includes 16,087 GSF of retail space. Of this retail space, 13,933 GSF is assumed to generate revenue. A small designated retail area between the loading area and parking garage (2,154 GSF) could be used for a City maintenance shop/central supply area if needed which would result in no revenue to the City.

For the 13,933 GSF retail space, the City is assuming to master lease this space to a retail operator who will take responsibility for lease-related risks and paying for tenant improvements and commissions.

Fire Station #1 and Emergency Operations Center (Both currently located in COB)

With the revised Civic Center proposal the City's Fire Station #1 and Emergency Operations Center (EOC) will remain in place. CCDC is looking for an alternative location for Fire Station #1. As we noted in our report on the Civic Center Complex Exclusive Negotiation Agreement (IBA Report # 09-78), CCDC has included the total cost of site acquisition ($8.8 million) and construction ($36 million) for a new Fire Station #1 in their long-term budget. It should be noted that a renovation of Fire Station #1 was just completed and is contemplated to extend the life of the station through 2015.

Concerning the EOC, staff has stated that there is currently no plan to relocate the facility. In times of disaster the EOC is the central command and control location for the City's operations. The current facility is in poor physical condition and is located on a site in close proximity to a known active seismic fault. Regardless of where the new EOC is located, the facility will require enhanced infrastructure as mandated by the State of California's Essential Services Building Act.

City Operations Building (COB) Redevelopment

With the revised Civic Center Proposal, staff has stated that the Development Services Department will continue to occupy COB until the department moves into the new facility which will not occur until 2014. If the Civic Center proposal is approved by the voters, the City will have three years to formulate a reuse strategy for the facility. During that time a detailed evaluation will be undertaken as to the best disposition of the asset. This could include a lease, sale, or redevelopment of the property. If none of these alternatives are economically feasible at the time Development Services vacates the facility, it may be that the building is shuttered until redevelopment or reuse is practical.

What Financing Structure is being Contemplated and what are the Key Assumptions?

Although a detailed plan of finance has yet to be developed, estimated annual project costs contemplate using Lease Revenue Bonds to finance the Civic Center project. Previous project reports discussed the possibility of issuing tax-exempt debt to finance the Civic Center through a nonprofit corporation authorized to issue such debt under Internal Revenue Service ruling 63-20; however, staff now believes the use of Lease

Revenue Bonds is a more straightforward and cost-effective approach. Lease Revenue Bonds were recently used to refinance approximately $100 million of deferred capital improvement projects in May 2010. The revised proposal assumes the issuance of approximately $320 million of 30-year fixed-rate Lease Revenue Bonds at a true interest cost (including all costs of issuance) of 5.25%. Including interest, debt service payments for the bonds over 30 years will total approximately $613 million.

As noted in Chapter III of the City's Debt Policy, Lease Revenue Bonds are lease obligations secured by an installment sale or by a lease-back arrangement between the City and another public entity (i.e., the City's Public Facilities Financing Authority - PFFA), where the general operating revenues of the City are pledged to pay the lease payments, which are, in turn, used to pay debt service on the bonds. In this case, the leased asset would be the new Civic Center being financed or other City assets until construction of the new Civic Center is completed. The resulting lease obligations do not constitute indebtedness under the state constitutional debt limitation and, therefore, would not be subject to voter approval.

In simple terms, the use of Lease Revenue Bonds would involve creating a lease between the City and another public entity like PFFA. The City would lease the new Civic Center, or other City assets, to the public entity for a nominal rent of $1. The public entity would then lease back the same asset(s) to the City, at a rate sufficient to cover the annual debt service on the Lease Revenue Bonds. The lease back to the City would be considered a contingent obligation because it is subject to abatement if the City does not have beneficial use of the leased assets for any reason. The City is required to budget and make lease payments from any general funds legally available to it, but the requirement to make lease payments is not one for which the City is obligated to levy or pledge any form of taxation.

Annual debt service for the City's outstanding General Fund backed Lease Revenue Bonds expressed as a percentage of the FY 2011 General Fund budget is approximately 3.9%. In assessing an agency's debt affordability, rating agencies would characterize this percentage as a low to moderate debt burden. Adding the estimated debt service for a new Civic Center would increase this percentage to approximately 6%, which is closer to a moderate debt burden. Considering this debt affordability measure, the IBA believes that Lease Revenue Bonds are an appropriate form of financing for a new Civic Center.

The revised proposal assumes 30-year bonds would be issued at the beginning of 2012 at a true interest cost of 5.25% with the first semi-annual debt service (lease) payment due mid-year in 2012. The Hold Steady proposal similarly assumes issuing 30-year 5.25% bonds in July 2017; however, the total amount being financed under Hold Steady grows from $320 million to $379 million primarily reflecting inflated costs of construction. In order to develop their cost comparison, JLL assumes that the borrowing rate of 5.25% would be the same in 2012 and 2017. The 5.25% estimate reflects recent bond market conditions which are likely to change by an indeterminable amount before bonds would be issued in either 2012 or 2017.

As the new Civic Center would not be ready for lease during its construction, the City can opt to increase the amount of the borrowing (bonds) to include capitalized interest. Capitalized interest can cover all or a portion of the bond interest during the construction period. The current cost comparison assumes $7.9 million of capitalized interest for the project financing which is approximately 26% of total estimated bond interest during the construction period.

The decision to partially capitalize interest for the cost comparison was based on an assumption that the City will have funds available to make total estimated bond interest payments of $8 million in calendar 2012, $8.5 million in calendar 2013 and $14 million in calendar 2014. However, management has yet to identify a source of additional funds for the bond interest payments in these years or discuss how this new funding requirement can be accommodated within the constraints of the General Fund which is already projecting deficits for each of the next five years. The City could alternatively elect to structure the bonds to capitalize all of the bond interest payments during the construction period. While this would eliminate General Fund bond interest payments during the construction period, it would also increase the size of the borrowing, total bond interest expense and annual debt service after the initial construction period.

As noted in the staff report, a sensitivity analysis was prepared by JLL to determine what affect a 1% increase in the borrowing rate (to 6.25%) would have on annual debt service. As modeled by JLL, debt service payments remain unchanged for the first three years and thereafter increase by approximately $3.2 million to $4.0 million a year through 2042. This equates to approximately $91 million of additional debt service for the Revised Project attributable to a 1% increase in the borrowing rate. The IBA notes that any significant increase in the assumed 5.25% borrowing rate will significantly increase the City's total and net annual cost for a new Civic Center.

What is the Impact of the Civic Center Project and Hold Steady Options on the City's Five-Year General Fund Financial Outlook?

In April 2010, a revised Five-Year Financial Outlook was issued incorporating the impacts of the budgetary reductions implemented in December 2009. No changes to the Outlook were made at that time related to the Civic Center project.

The IBA has adjusted the shortfall amounts reflected in the April 2010 Outlook revision to incorporate the cost estimates based on the revised Hold Steady scenario, and the revised Civic Center project, as proposed, and as reflected in Attachment A to this report.

FY 2011 – 2015 Five-Year Financial Outlook General Fund Shortfall (in millions)			
Fiscal Year	**April 2010 Outlook Projected Deficit**	**Projected Deficit with Hold Steady Costs***	**Projected Deficit with Civic Center Costs***
FY 2011	-	$(11.0)	$(3.5)
FY 2012	$(72.5)	$(83.9)	$(83.7)
FY 2013	$(68.4)	$(79.9)	$(79.5)
FY 2014	$(69.9)	$(81.7)	$(81.5)
FY 2015	$(48.1)	$(51.4)	$(51.2)
Total:	**$(258.9)**	**$(307.9)**	**$(299.4)**

*Hold Steady and Civic Center Projects reflect estimates based on calendar year basis; as example, calendar year 2011 costs reflected in Fiscal Year 2011 to provide comparison and summary with previously stated projected FY shortfalls.

What is the Impact to the City's Reserves?

As of June 30, 2010, the City's General Fund Reserves total $77.1 million, including the City's Emergency Reserve Fund of $55 million, and the Unallocated Reserve of $22.1 million. The City's Reserve Policy and the FY 2011 Budget are based on maintaining a General Fund Reserve, in total, at 7% of total General Fund revenues. The FY 2011 General Fund Budget totals $1.096 billion; a 7% reserve level requires $76.7 million. With reserves currently at $77.1 million, the City's 7% reserve target is achieved.

In addition, based on final Council budget decisions, included in the FY 2011 General Fund Budget is an Appropriated Reserve of $4.1 million. The Appropriated Reserve is also considered when assessing the General Fund reserve level. Adding the General Fund Reserve of $77.1 million to the Appropriated Reserve of $4.1 million creates a total reserve of $81.2 million, or 7.4% of the total General Fund. The Council has committed to utilizing up to $1.2 million from the Appropriated Reserve for November ballot expenses, and has had ongoing discussions about utilizing the remainder for the possible reinstatement of budgetary reductions. The IBA has also cautioned that some level of reserves may be needed to maintain a balanced budget in the event revenues do not achieve budgeted levels.

The Civic Center proposal requests Council approval of an amendment to the FY 2011 Appropriation Ordinance to increase the General Fund budget by $2.0 million from the Unallocated Reserve, in order to fund pre-design and design costs for the Civic Center project, contingent on the passage of the ballot measure by voters. The proposal indicates an additional $5.6 million will be needed for these expenses in FY 2012. Funding for design costs for this project was not considered or included in the Mayor's Proposed

Budget or the Mayor's May Revision for the FY 2011 Budget. These costs have also not been reflected in recent revisions to the City's Five-Year Financial Outlook.

FY 2011 Reserve	Amount (in millions)	% of General Fund Revenues
Emergency Reserve	$55.0	
Unallocated Reserve	22.1	
Appropriated Reserve	4.1	
Reserve Total	**$81.2**	**7.4%**
Less: Election Costs	(1.2)	
Less: Design Costs	(2.0)	
Revised Reserve Total	**$78.0**	**7.12%**

Reducing the Unallocated Reserve by $2.0 million in FY 2011 would bring total General Fund Reserves to $78.0 million, or 7.12% of the total General Fund budget, and would still comply with the City's Reserve Policy. However, reducing the reserves to this level limits the Council's ability to utilize reserves for unanticipated needs, service restorations, or to offset revenues without being in danger of dropping below the 7% reserve goal.

It is the intent of the proposal that these funds would be reimbursed from the City's bond financing, once completed, and reserve funds would be reinstated. However, there is the risk that design costs are incurred and bond financing, for some reason, is not able to be fully executed. In that case, the reserve funding would not be returned.

The first and second reading and introduction and adoption of the FY 2011 Appropriation Ordinance are expected to occur at the Council meetings of July 19 and 26, 2010. The Council is being asked to consider an amendment to the FY 2011 Appropriation Ordinance, prior to its adoption.

The IBA has previously stated that the FY 2011 General Fund Budget is tenuous, primarily due to some major revenue growth assumptions that are likely to be proven to be overly optimistic. Based on preliminary data from the County Assessor and periodic reports of recent retail sales activity, it is expected that the City will undergo a budgetary reduction process in the months ahead, which will be necessary to ensure a balanced General Fund budget.

Committing now to the use of the Unallocated Reserve for this purpose prior to the outcome of the election is not necessary, and an updated evaluation of the City's finances would be useful before such a decision is made.

The IBA recommends that the contingent funding actions requested now be postponed until the election occurs, and that these actions return for Council review and approval following the receipt of voter approval. This will allow time for an evaluation of the City's finances for the FY 2011 budget year and permit the City Council to make a more informed decision.

What are the Financial Projections/Assumptions Related to the Revised Proposal and the Hold Steady Alternative?

We have reviewed the assumptions contained in the Jones Lang LaSalle (JLL) financial projections, which compare the Revised Proposal and the Hold Steady alternative. The calculations and assumptions for these projections are contained within complex spreadsheets. Detailed assumptions are built into the projected costs for the Revised Proposal and Hold Steady alternative.

As a supplement to the JLL projections, our office has included a chart as Attachment A of this report. The purpose of the chart is to show a comparison of the 2010 base year costs to the total annual costs over 10 years for both the revised proposal and the Hold Steady alternative. This chart illustrates possible impacts to the General Fund or a combination of funds.

A general overview of elements in the JLL projections, including projected costs for the first 10 years, is presented below, followed by a discussion of issues in the out-years (years 2020 through 2059).

Capital Expenses – Owned Buildings

Capital expenses are anticipated for building deficiencies identified in the AECOM Facilities Condition Assessment Supplement, including improvements related to fire, mechanical and electrical systems.

- Revised Proposal – $10.2 million, which includes $5.8 million for the Evan Jones Parkade, $3.3 million for the City Administration Building (CAB), $1.1 million for the City Operations Building (COB) and no projected expenditures for the Concourse building.
- Hold Steady – $42.9 million, which includes $5.8 million for the Evan Jones Parkade, $16.4 million for CAB, $7.4 million at COB and $13.3 million for the Concourse building.

Operating and Maintenance Expenses – Owned Buildings

- Revised Proposal – $46.5 million, including CAB and COB expenses through July 2014. Also included are operating expenses for the new city hall, which will begin in July 2014. Additional operating expenses for the new Public Utilities building will be incurred beginning in 2025.

- Hold Steady – $40.2 million, including CAB and COB expenses (which will end January 2020). Additional operating expenses for the new city hall and new Public Utilities building will begin in 2020 and 2025, respectively.

Net Parking Revenue

Evan Jones Parkade revenue is based on employee utilization of 1,000 of the existing 1,100 spaces until the new city hall is occupied. At that time, employee utilization is anticipated to drop to 512 spaces, when 461 underground spaces at the new city hall become available – beginning July 2014 for the Revised Proposal and January 2020 for the Hold Steady alternative. This will leave 588 Evan Jones Parkade spaces available for public parking revenue.

- Revised Proposal – $24.8 million, including net revenue from the Evan Jones Parkade, as well as the underground parking garage in the new city hall. Net parking revenue from the new city hall underground parking garage is based on income from 271 single spaces and 190 tandem spaces.
- Hold Steady – $19.2 million, which is comprised of net revenue for the Evan Jones Parkade. The new city hall parking revenue will not commence until 2020.

Rent/Operating & Maintenance Expenses – Leased Buildings

Landlord proposals for the existing leases at 600 B Street, the Executive Complex and the Civic Center Plaza have not been made public, to protect the City's negotiation position. Currently, the blended rental rate for these three buildings is $1.68/square foot/month. Upon the rental rate resets for the three buildings, between June 2013 and August 2014, the blended rate will be $2.17/square foot/month. The most recent landlord proposals do not provide for tenant improvement allowances, which means that there will be no upgrades/improvements, effectively lowering the rental rates.

- Revised Proposal – $53.0 million, including the current lease expense through July 2014.
- Hold Steady – $128.7 million, including expenses associated with the current leases. Additional lease expenses continue beyond 10 years, through January 2020.

Net Retail and Meeting Space Revenue/Expense

The Concourse building's operating expenses exceed meeting space revenue by $1 million in 2010, growing to $1.2 million (annualized) in 2017.

- Revised Proposal – $65,000 net revenue, including meeting space and retail income from the new city hall, beginning July 2014. Offsetting net expenses related to the Concourse building are projected to end December 2011, prior to the building's demolition.
- Hold Steady – $8.1 million in net expenses related to the Concourse building, which are projected to end June 2017, prior to the building's demolition. The new city hall meeting space and retail income will not commence until 2020.

<u>Debt Service</u>

The project/construction costs to build the new city hall are estimated to be $293.4 million under the Revised Proposal. For the Hold Steady alternative, these costs are escalated by 18.35%, to $347.2 million. Bonds to finance the new City Hall would be issued under the Revised Proposal and the Hold Steady alternative in 2012 and 2017, respectively. Under both alternatives, the assumed interest rate is 5.25%.

- Revised Proposal – $119.8 million
- Hold Steady – $26.8 million

<u>Relocation Costs</u>

Relocation costs under both scenarios include costs to temporarily relocate the print shop and library book distribution center from the Concourse building upon its demolition.

- Revised Proposal – $1.6 million, including relocation costs for the new city hall in July 2014.
- Hold Steady – $738,000. The new city hall relocation costs will not be incurred until 2020 and therefore, are not included in this 10-year total.

<u>Incremental Costs – New Process</u>

Estimated consultant costs of $2.0 million for a new developer selection process and negotiations would be incurred if the City were to move forward with the Hold Steady alternative.

<u>Out-years – Years 2020 through 2059</u>

It is anticipated that a future Public Utilities facility will be built, which will mitigate the effects of future increases in the City's employee population. For this facility, the same projections are applied under both the Revised Proposal and Hold Steady alternative. The anticipated move-in date under both scenarios is 2025. The cost to build a new

40,000 square foot Public Utilities facility on current City-owned land is an estimated $9.4 million. This estimate is based on 2010 construction costs of $150/square foot, which are escalated by 3.5% per year to $234.59/square foot (in 2023). Operating expenses are also included in the projections. Bond financing at 5.25% interest and 30-year amortization is assumed.

The City is also expected to acquire additional leased space in future years as its employee population increases: 24,114 square feet in 2035, 37,780 square feet in 2045, and 40,107 square feet in 2055. Estimated rental rates reflect the recent landlord proposed rates, which are represented in the blended rate of $2.17/square foot/month. Adjustments to this rate include a tenant improvement allowance.

Office space for each of the nine Council districts is currently allocated at 3,384 square feet. The move-in day size for each office (10 employees), increased by the projected 0.6% growth rate over the duration of the 50 year analysis, equates to an approximate staff size of 13 employees per Council office. In order to accommodate increasing staff sizes, employees who are currently allocated 64 square foot workstations would have their workstations downsized to 48 square feet.

General Projection Observations

Many detailed assumptions are built into the projected costs for the Revised Proposal and Hold Steady alternative. JLL's supporting spreadsheets for these preliminary cost estimates appear to be thoroughly constructed. The projections are based on a variety of assumptions, including current expenditures provided by City staff, rental rates based on current landlord proposals, a revised Facilities Condition Assessment provided by AECOM, and inflation factors for the various costs and revenues.

Although the assumptions contained in JLL's projections appear reasonable, it is difficult to accurately predict future costs and revenues. We are living in a time of heightened economic uncertainties. Interest rates in the future are uncertain, and a change in the projected bond interest rate could have a sizable impact over the life of the project. For example, a 1% increase in the assumed bond interest rate of 5.25% could cause the debt service costs to increase by $90.9 million for the Revised Proposal scenario. Actual cost escalations for operating and maintenance expenses, rental expenses and construction costs may differ from projected escalators, causing actual costs to vary from projected costs by tens of millions of dollars, or more.

Additionally, there is a risk associated with the Five-Year Outlook. As shown in Attachment A to this report and discussed earlier. Both the Revised Proposal and the Hold Steady alternative are projected to generate incremental costs over the 2010 base year. Those projected incremental costs for calendar years 2011 through 2015 total $40.5 million and $48.9 million for the Revised Proposal and Hold Steady alternative, respectively. The General Fund portions of these additional costs have not been built into the most recent Five-Year Outlook for the City.

Lastly, the proposed ordinance for the Civic Center ballot measure provides that “whereas the Council finds that the use of City-owned office space in the proposed Civic Center is anticipated to save the City $40 million over 20 years compared to the cost of delaying the construction for 10 years…” The projections provided by JLL show such a savings, in the amount of $41.3 million.

Review of Draft Ordinance and Ballot Measure Language

The proposed ballot measure includes the allocation of $1 million annually for ten years, totaling $10 million over a ten year period, for public safety, community services, and road improvements. This allocation is based on the claim that $40 million will be saved over twenty years by comparing the “Hold Steady” option to the revised proposal.

Section 12 of the draft ordinance reads “Upon adoption of this Measure, the Chief Financial Officer is authorized to establish an account for the purposes of receiving $1,000,0000 in savings each year for 10 years, to be expended towards any of the following: road maintenance and repairs, public safety, and community service; to begin upon completion of the Civic Center.”

As written, the Ballot and ordinance language does not seem to require that $1 million in actual lease or other savings be achieved (or verified) before the commitment of $1 million for road maintenance and repairs, public safety, and community service. In addition, as we note in our review of the impacts to the Five-Year General Fund Outlook, it is highly unlikely that the City will realize savings when compared to the actual budget.

If the new Civic Center is Not Approved What Will Need to occur?

If the new Civic Center project is not approved the City would need to rapidly develop a plan to address the current facilities’ deficiencies. In their May 2009 Facilities Condition Assessment Supplement, AECOM, the sub-consultant to JLL, developed a minimum deficiencies expenditure summary for the current facilities. For five years the minimum expenditure would be $19.5 million and for ten years the costs would be $40.1 million. These expenditures would address a number of deficiencies including fire and life safety, mechanical, plumbing, and structural needs. Even if the City were to move forward with these expenditures, AECOM notes in their report “that a minimum expenditure approach to maintaining these buildings over a five-year period, and especially a ten-year period will render these buildings in a condition that will force them to be demolished at the end of the pro forma period.”

Funding to address the deficiencies would be a challenge. One option would be to reprioritize funding from Land Sales proceeds. Currently, proceeds from Land Sales are programmed for deferred maintenance and ADA projects. However, if the City Council elected to pursue this option, deferred maintenance and ADA projects would be delayed resulting in the possibility of increased costs.

Another possible option would be to utilize debt financing to fund the deficiencies. The challenge with the use of debt financing is that it is likely that the term of the debt payments would exceed the life of the facility which AECOM projects to be ten years. In addition, the City would need to ensure that each of the deficiencies would qualify as a capital expense.

The default option would be to fund the deficiencies through the City's General Fund. With a projected deficit in FY 2012 of $72.5 million and no new revenue sources, the City would likely be in a situation of reducing services to fund deficiencies in facilities that would need to be redeveloped in ten plus years.

As in the past, the City could elect to fund only emergency repairs to the Civic Center structures as they occur. However, if one or more of the Civic Center structures were to experience a major failure of electrical, mechanical, or power plant facilities, the City would likely have to evacuate the structures for an extended period of time. In addition, there are risks associated with employees being housed in substandard facilities, for example, where asbestos exists.

CONCLUSION

We concluded our June 5, 2009 report on the Civic Center Redevelopment (IBA Report #09-48) by noting that over the last twenty years the City has continued to make short term decisions concerning the future of the Civic Center Plaza without a long-term plan. We also noted that the current facilities are at the end of their useful life and the inaction of previous administrations in regard to deferred maintenance has resulted in health and safety risks to employees and citizens that must be addressed.

In this report we have reviewed assumptions provided by JLL and conclude that the Revised Civic Center Proposal as recommended by the Mayor does project a savings of $40 million over 20 years as compared to the "Hold Steady" option. Therefore, the IBA recommends moving forward with placing the Civic Center on the Ballot in November. We believe that this is the fiscally prudent course for the City's future. We make this recommendation understanding that this will further impact the City's General Fund as noted in our discussion on the impact on the Five-Year Outlook. However, it is important to note that either option, moving forward with a new Civic Center, or the "Hold Steady" option, will require the City to expend substantial resources in the future. We also see this decision as a choice of expending limited resources on a facility that will meet the City's needs until at least 2025 or on a facility that will need to be torn down in ten years. More importantly, the City has been put on clear notice by reputable experts that the current facilities are sub-standard and in some cases hazardous. The current "do-nothing" approach is no longer an option for the City.

If the City Council elects to move forward with the proposal, the IBA recommends that the contingent funding actions requested now be postponed until the election occurs, and that these actions return for Council review and approval following the receipt of voter approval. This will allow time for an evaluation of the City's finances for the FY 2011 budget year and permit the City Council to make a more informed decision.

[SIGNED]

Lisa Byrne
Fiscal & Policy Analyst

[SIGNED]

Jeff Kawar
Fiscal & Policy Analyst

[SIGNED]

Elaine DuVal
Fiscal & Policy Analyst

[SIGNED]

Tom Haynes
Fiscal & Policy Analyst

[SIGNED]

Brittany Coppage
Research Analyst

[SIGNED]

Jeffrey Sturak
Deputy Director

[SIGNED]

Andrea Tevlin
Independent Budget Analyst

Attachment