

Memorandum

Date : December 8, 1997

To : Craig Brown, Director
Department of Finance
State Capitol, Room 1145
Sacramento, CA 95814

From : Department of General Services
Executive Office
1325 J Street, Suite 1910, Sacramento, CA 95814

Subject : **OPERATING AGREEMENT BETWEEN THE DEPARTMENT OF FINANCE AND THE
DEPARTMENT OF GENERAL SERVICES**

The attached Operating Agreement between the Department of Finance and the Department of General Services concerning Capital Acquisition and Development Projects and Long Term Leases dated October 8, 1997, replaces the Memorandum of Understanding (MOU) between our respective departments dated July 3, 1995. This Operating Agreement is the result of a request by Fred Klass to Steve Olsen to revisit the MOU and improve its focus and reflect the current operations between our departments.

I have read the attached Operating Agreement and support the terms and conditions. I will ensure that the appropriate branches within the Real Estate Services Division abide by the requirements of this Operating Agreement.

Enclosed are two duplicate signed originals of the Operating Agreement. Please sign both originals and return one to me for distribution within the Department of General Services.

We look forward to a continued cooperative and productive relationship with the Department of Finance. If you need further information or assistance, you may wish to have your staff contact Margaret K. Hudson, Chief, Project Management Branch, at (916) 445-0781.



PETER G. STAMISON, Director
Department of General Services

LW:ar:dc:101

Attachments

cc: George Valverde, Deputy Secretary, State and Consumer Services Agency
Steve Olsen, Chief Deputy Director, Department of General Services
Eugene A. Spindler II, Deputy Director, Real Estate Services Division, Department of General Services
Fred Klass, Program Budget Manager, Department of Finance
Tom Dithridge, Assistant Program Budget Manager, Department of Finance
Margaret K. Hudson, Chief, Project Management Branch, Real Estate Services Division, Department of General Services

OPERATING AGREEMENT

**CONCERNING CAPITAL ACQUISITION AND DEVELOPMENT
PROJECTS AND
LONG TERM LEASES**

by the STATE OF CALIFORNIA

Department of Finance and the Department of General Services

October 8, 1997

A. INTRODUCTION

1. **Purpose** - The purpose of this Operating Agreement is to document the understanding between the Department of Finance (DOF) and the Department of General Services (DGS), related to policy and procedural issues concerning capital acquisition development projects and long term leases.
2. **Objectives** - This Operating Agreement should improve the ability of the DOF and the DGS to accomplish their stated missions and meet their individual objectives.
 - a) **DOF Objectives** - *Prior to legislative authorization, ensure that the project or lease proposal is warranted based on workload and space standards criteria, meets policy objectives, is the best practical financial and program solution, demonstrates strong potential for economic benefit to the State, and has an acceptable funding source. During implementation, assess the project impacts of any change in key program assumptions, and monitor the project or lease to ensure that:*
 - 1) *it remains within authorization parameters, including any administrative agreements on project budget and scope,*
 - 2) *it considers reasonable implementation alternatives,*
 - 3) *it continues to demonstrate acceptable long-term benefits and near-term impacts, and*
 - 4) *the financing approach meets administrative and statutory requirements.*
 - b) **DGS Objective:**
DGS' objective is to identify and resolve any fiscal issues related to project development in a timely manner so that it can fulfill its overall mission.

The mission of the Department of General Services is to ensure quality, cost consciousness, and timely assistance and support to State and other public agencies so they can efficiently deliver needed services to the citizens of California.

With the leadership of the Governor and in cooperation with the Legislature, we seek to provide creative business solutions and serve our customers in a responsive and flexible manner.

B. COMMUNICATIONS

1. **Responsible Branch** - The Director of DGS through the Deputy Director of Real Estate Services Division shall ensure that one branch (Responsible Branch) within the Real Estate Services Division (RESA), is assigned the single point of responsibility for each proposed project.
2. **Preliminary Feasibility Reports** - DGS may be requested by another Department (Requesting Department) within the State to prepare feasibility reports that include scope definition, site analysis, cost estimates, economic analysis, project schedules and other items of information. This report will be used by the Requesting Department to

assist in making a decision as to whether it will officially propose a project. In general, potential projects at this stage are not reportable to DOF.

3. **Initial Notification to DOF** - For projects that meet the criteria of Section C(1) of this Agreement, the Responsible Branch shall notify DOF promptly when there is a reasonable possibility that the project will move forward. This notification must be in writing and describe the scope of the proposed project and the potential financing sources. The written notification will provide the opportunity for DOF, DGS and/or the Requesting Department to exchange information and determine if a feasibility analysis, per this Agreement, is required.
4. **Interactions with the STO** - DGS will notify STO of potential project financing needs in accordance with administrative policy set forth in Sections 6582 and 6586 of the State Administrative Manual. DGS agrees to abide by the description of responsibilities as presented in Sections 6574 through 6588.
5. **Status Meetings** - The DOF and the RESD shall establish a schedule for status meetings consistent with need. For each project, RESD will provide a status summary, current project cost estimate and last approved cost estimate, summary schedule, and a discussion of all significant issues including but not limited to tenant programming problems, budget risks, possible scope changes, and any significant open financing issues.
6. **Leases and Pre-Lease Agreements** - No lease shall be signed for any project requiring a feasibility analysis per this Agreement prior to DOF's concurrence with the feasibility analysis and the lease provisions. DGS agrees to treat pre-lease agreements such as letters of intent as if they were lease agreements, for purposes of obtaining DOF review and concurrence with financial policy provisions prior to execution.
7. **Economic Analyses** - DGS will provide DOF with conceptual and full feasibility analyses for projects identified in Section C(1) of this Agreement from the point of proposed project authorization to project completion and final financing. DGS will maintain a record of project cost and scope as initially approved as well as project cost and scope on an as-built, as-financed basis.
8. **Early Budget Resolution for Anchor Tenants** - DGS and DOF agree that before DGS programs a client department as an anchor tenant, the client department must resolve the question of future budget adjustments for rent with DOF. DOF's general policy will be to provide rent adjustments for tenants in new office buildings where merited and feasible. When budget adjustments are not provided, DGS' alternatives are to identify new tenants for the project or to elevate the option of a forced move to the agency level.

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C. FEASIBILITY ANALYSIS

1. **Types of Projects** - Generally, a feasibility analysis per this Agreement will be submitted on the following types of projects:
 - 1.1 Major capital constructions (generally with an estimated project cost in excess of \$20,000,000, or another threshold amount as agreed upon by DOF and DGS);
 - 1.2 Lease-purchase projects in excess of \$2,000,000;
 - 1.3 Any lease with a purchase option in excess of \$2,000,000. Also, any lease with a nominal (i.e., \$1.00) bargain purchase option, regardless of option amount, i.e., a capitalized lease;
 - 1.4 Acquisitions with a cost in excess of \$20,000,000, or another threshold amount as agreed upon by DOF and DGS;
 - 1.5 Any capital project, including lease-purchase projects, regardless of amount, which does not have a statutory appropriation limit;
 - 1.6 Any project which, pursuant to statutory language, requires a demonstration of specific cost/benefits;
 - 1.7 Any lease consolidation project, not otherwise noticed to DOF using the Space Request (Form 9) process, necessitating future rent adjustments to the budgets for client departments;
 - 1.8 Other projects, generally those of a sensitive nature, as agreed upon by DOF and DGS.
2. **Format** - While different projects will present different issues and risks, the feasibility analysis will include a description and review of all pertinent aspects of the project, identification of the proposed anchor tenants and overview of their program space requirements, an explanation of all assumptions, risks, unusual features, alternatives and recommendations. Generally, there will be two formats: a conceptual feasibility analysis format used before project scope and budget are refined (generally at the project authorization stage), and a full feasibility analysis format used after scope and budget are substantially defined. Formats should be consistent with those shown on Attachment "A" of this Operating Agreement. DGS and DOF may revise formats by mutual agreement without revision to this Agreement.
3. **Time For Preparation of the Feasibility Analysis By DGS** - The time required for the preparation of a feasibility analysis will vary depending on the size and complexity of the project and the availability of staff resources. Generally, DGS will require approximately three weeks for preparation and one week for DGS management and Requesting Department review.

4. **Payment For Preparation of the Feasibility Analysis By DGS** - DGS shall be paid for the preparation of the feasibility analysis by the Requesting Department.
5. **Time For Review of the Feasibility Analysis By DOF** - Generally, DOF will require a minimum of three weeks for review and one week for DOF management review and approval of the feasibility analysis. An additional week of review may be required for any feasibility analysis received during the months of October through December and February 15 through May 1.
6. **Submittal of Feasibility Analysis** - The conceptual feasibility analysis will be submitted to DOF by the Responsible Branch with proposed legislation or the budget change proposal (BCP). The Responsible Branch shall submit the full feasibility analysis so that the DOF management can respond within the following time requirements; or within alternate time frames agreed to by DOF and DGS:
 - 6.1. Minimum of thirty days prior to request for funds from the Pooled Money Investment Account (PMIA) or any other available source.
 - 6.2. Minimum of thirty days prior to the execution of any acquisition, construction agreement or a long term lease in excess of \$2,000,000 planned for acquisition by the DGS.
 - 6.3. Minimum of fifteen days prior to the advertising for any Request For Proposal (RFP).
7. **Statement by DOF** - Prior to the execution of any of the above referred to agreements, the Responsible Branch shall obtain a written statement from DOF that DOF concurs with the project proceeding. This statement will identify any limitations or constraints required by DOF.
8. **Updates to the Feasibility Analysis** - DGS shall submit brief project updates upon the occurrence of certain key events, which may include:
 - 8.1. Completion of the Environmental Impact Report (EIR),
 - 8.2. Bond sale,
 - 8.3. Project completion,
 - 8.4. Any change in data used to project break-even points, including approved project budget, and
 - 8.5. Any change in key assumption, including identification of anchor tenants.

Unless DOF requests a complete revision, only those sections of the feasibility analysis requiring updating shall be resubmitted.

9. **Notification of Material Changes** - The Responsible Branch shall notify the DOF at the earliest possible time of any event (including a significant change in key assumptions) for any project that is inconsistent with the most recent project feasibility report, not in the best interest of the State or that would adversely affect the recommendations made by the Responsible Branch or the DOF.
10. **Pooled Money Investment Account (PMIA)** - The Responsible Branch shall provide the DOF with a copy of all PMIA loan applications as submitted to the Pooled Money Investment Board (PMIB).
11. **Lease Notification** - The Responsible Branch shall provide the DOF with a copy of all lease notifications when submitted to the Legislature.

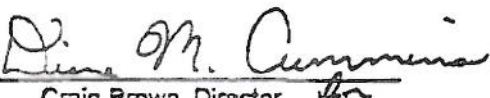
OPERATING AGREEMENT

October 8, 1997

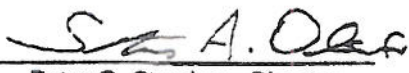
Department of Finance and Department of General Services

This Operating Agreement is to remain in full force and effect until either modified or terminated by written agreement by the respective Directors of the Departments.

Department of Finance

By:  Date 1/14/98
Craig Brown, Director *for*

Department of General Services

By:  Date 12/11/97
Peter G. Stamison, Director

cc: Secretary, State and Consumer Services Agency

Memorandum

Date : October 10, 1996

To : Shelley Mateo, Assistant Program Budget Manager
Department of Finance
915 L Street
Sacramento, CA 95814

From : Department of General Services - Office of Project Development and Management

Subject : STANDARD ECONOMIC MODEL - AGREEMENT ON FORMAT

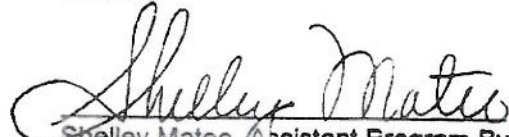
Thank you for your letter dated October 8, 1996. Based on that letter and meetings with our respective staffs, we are pleased to reach agreement with you on the format for the full economic analysis.

While all capital projects will be different, the content of each Economic Analysis submitted to the Department of Finance should generally include the same content as on the attached STANDARD ECONOMIC ANALYSIS FORMAT dated October 10, 1996.

We look forward to continuing to work effectively with you and your staff. Please let me or Lee Willoughby know if you have any proposed changes to the contents of this memorandum. If you have no changes, please signify your concurrence by signing below and return a copy to me. We will then implement the procedures described in this memorandum on all future economic analyses.


Margaret K. Hudson, Chief

Concur:


Shelley Mateo, Assistant Program Budget Manager
Department of Finance

cc: Gene Spindler II
Tim Heffer
Lee Willoughby
Mike Courtney
Ian Dey
Lane Richmond

STANDARD ECONOMIC ANALYSIS FORMAT

October 10, 1996

The format used in the **Economic Analysis – New Headquarters Building – California Environmental Protection Agency** dated July 10, 1996 and the **Addendum** dated August 21, 1996 shall be the standard for future economic analyses, with the following changes or additions:

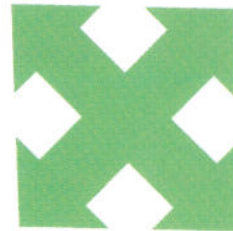
1. **Table of Contents** – Include a more detailed Table of Contents with page numbers.
2. **Project Description** – Include a more detailed project description similar to the exhibit in the CalEPA lease.
3. **Alternatives** – Include a narrative of alternatives considered, including status quo, site and leasing alternatives – and those that are valid and those that were dismissed.
4. **Unusual Features** – A discussion of all features, especially any unusual ones, which affect project cost or otherwise require special consideration.
5. **Background** – A discussion of the project's background leading to the decision to prepare an economic analysis.
6. **Schedule** – Include a master schedule similar to the one in the CalEPA analysis, with the addition of Economic Analysis activities and activities involving the STO.
7. **Risk** – Describe risk factors in more detail. Describe potential cost decreases as well as increases to present a complete assessment of the total risk.
8. **Moving** – Unless there are very unusual circumstances, the cost of moving shall be excluded from long-term financing. This is typically a support cost and should not be financed with the project.
9. **Future and Present Value** – Include Future Value and Present Value calculations for both annual and cumulative costs.
10. **Break-even** – Both annual and cumulative break-even points should be highlighted.
11. **Graphs** – Graphs are acceptable but not necessary for DOF analysis.
12. **Reserve for Replacement** – A Reserve for Replacement amount should be included with operating and maintenance costs. (This item will be part of the resolution of the Building Rental Account rate.)
13. **Yield Rates** – The bond yield rates for each project should be discussed and agreed upon between PMB and DOF.
14. **Discount Rate** – The discount rate for each project should be discussed and agreed upon between PMB and DOF.
15. **Copies** – Submit three copies of each economic analysis to DOF.
16. **Memorandum** – Include a cover memorandum with each economic analysis stating the purpose of the submittal to DOF.



Existing Condition
State-owned or Privately-leased



Private-Sector Development
Lease with an Option to Purchase

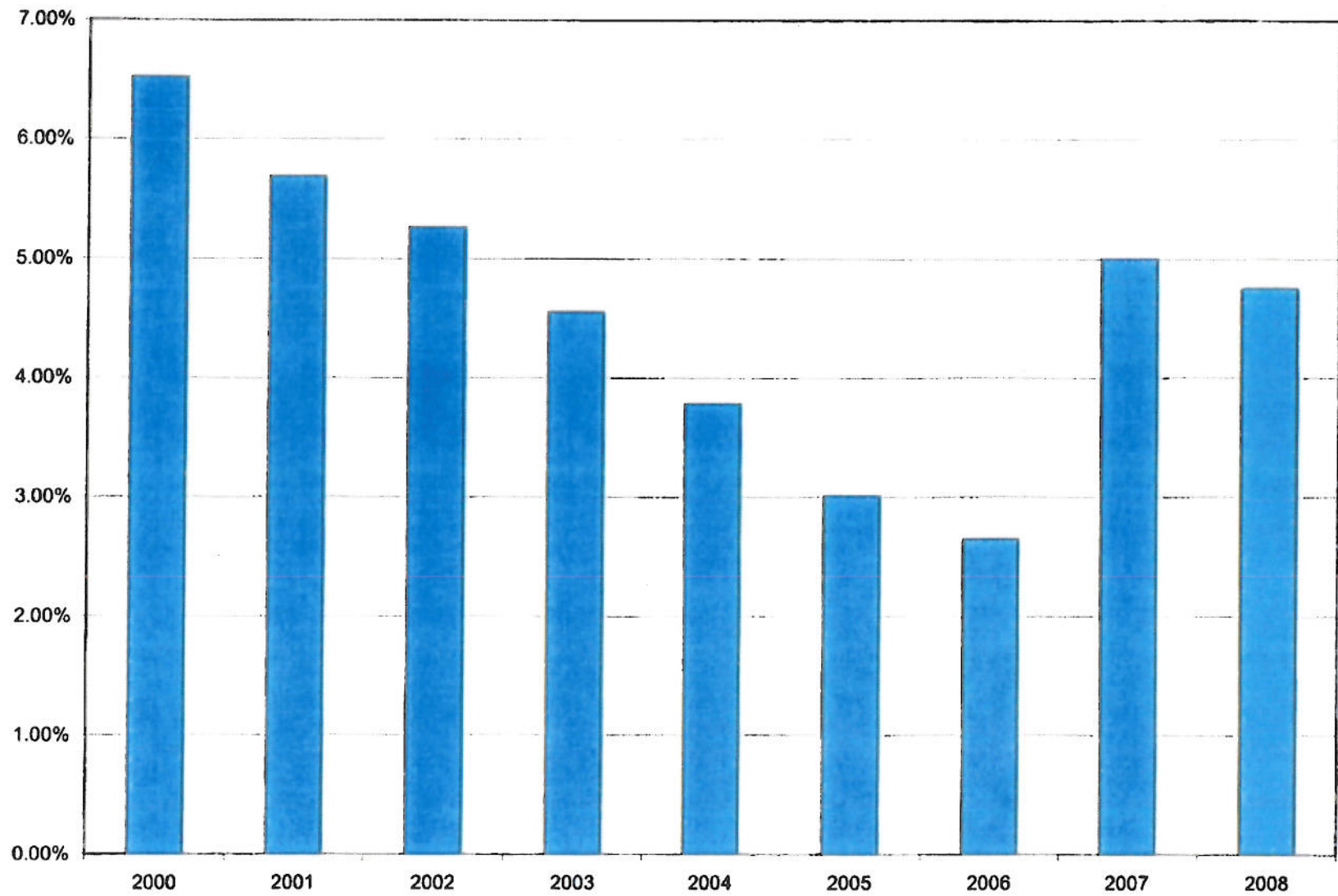


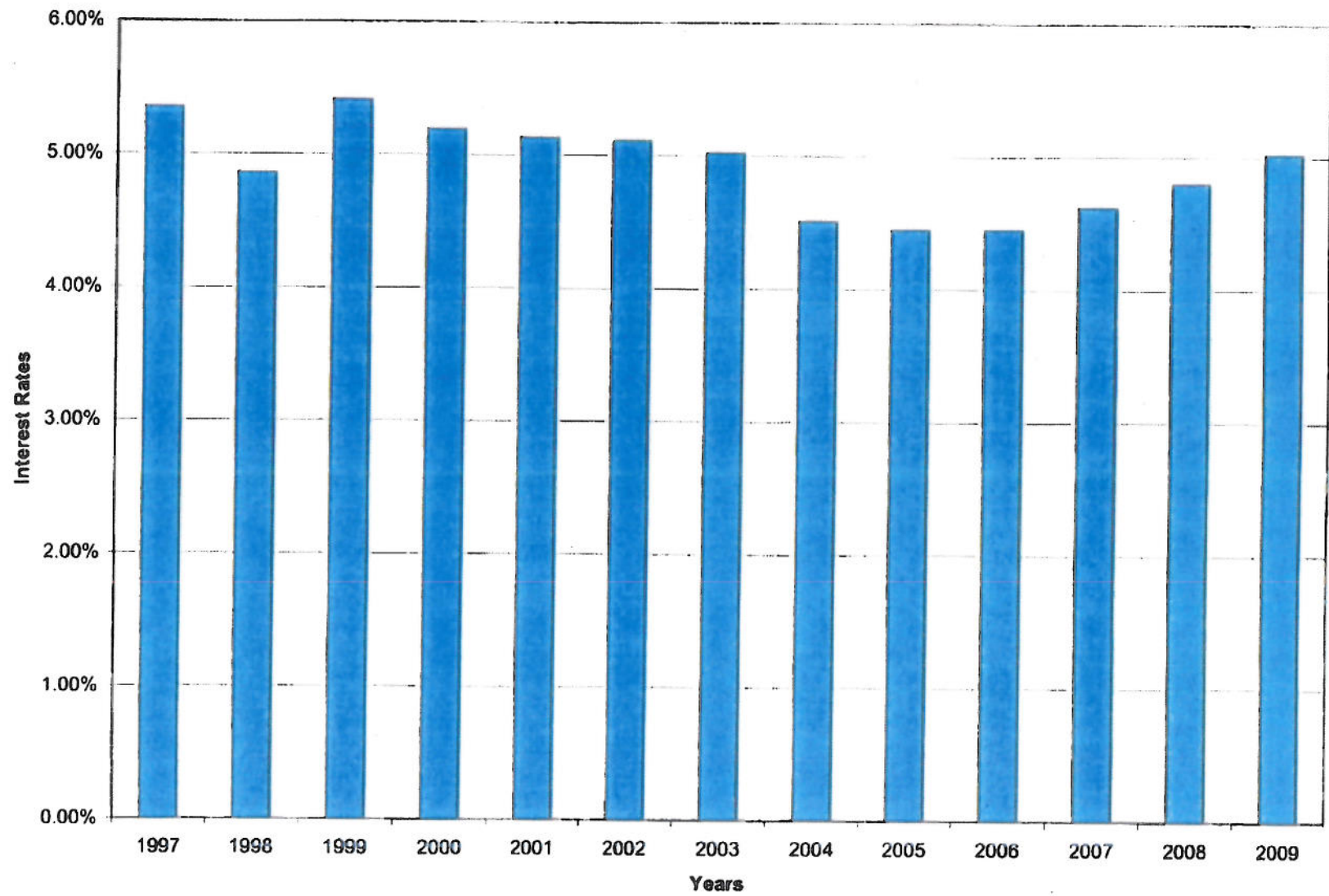
Consolidated Lease
No Option to Purchase; No Equity

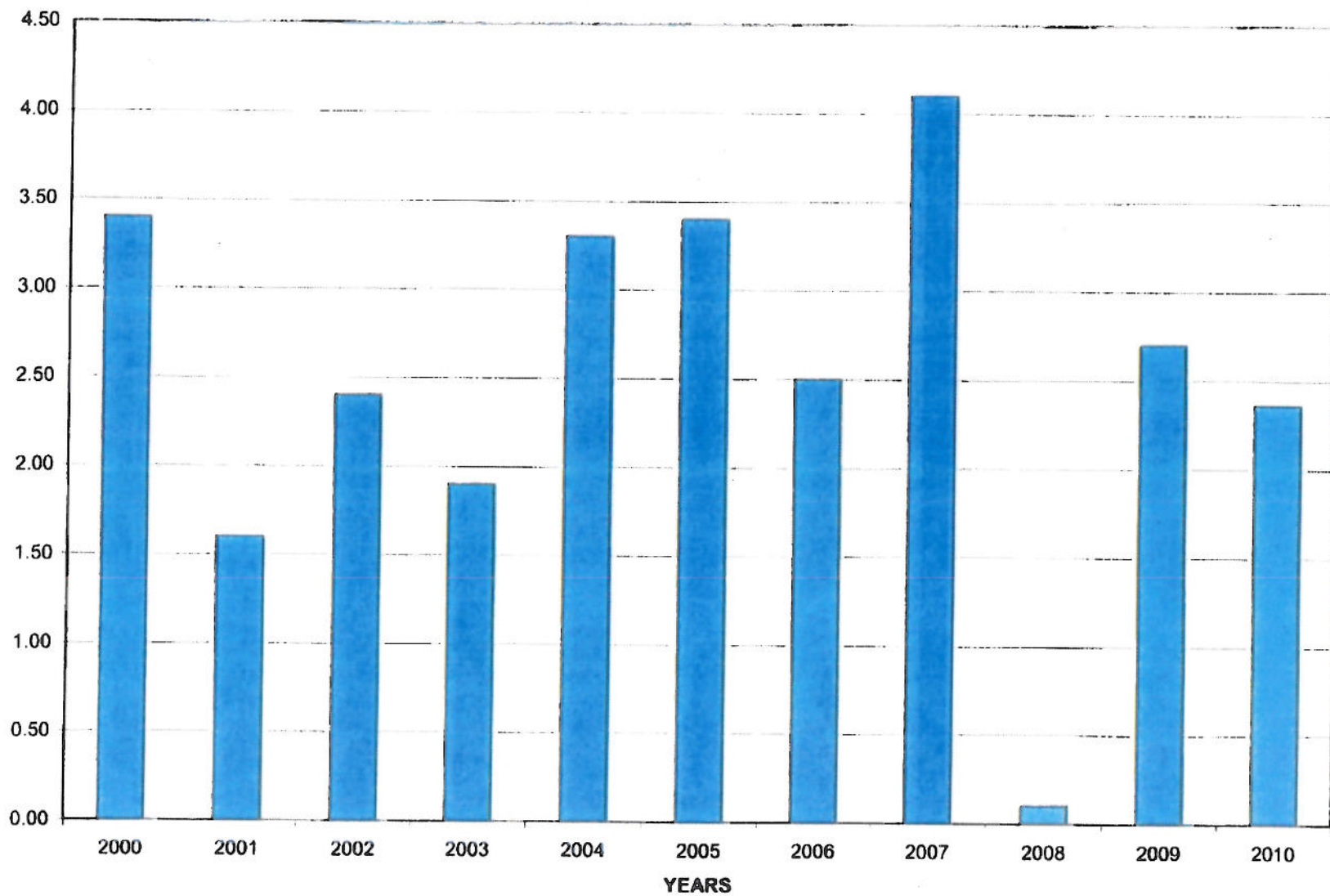


Public-Sector Development
Capital Outlay (Lease-Revenue Bonds)









Source: US Department of Labor

CONSUMER PRICE INDEX

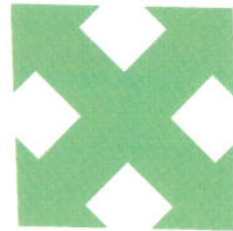
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Existing Condition
State-owned or Privately-leased



Private-Sector Development
Lease with an Option to Purchase



Consolidated Lease
No Option to Purchase; No Equity



Public-Sector Development
Capital Outlay (Lease-Revenue Bonds)