

CITY AND COUNTY OF SAN FRANCISCO
BOARD OF SUPERVISORS
BUDGET AND LEGISLATIVE ANALYST

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January 4, 2013


TO: Budget and Finance Committee 
FROM: Budget and Legislative Analyst
SUBJECT: January 9, 2013 Budget and Finance Committee Meeting

TABLE OF CONTENTS

Item	File	Page
1	12-1167 Accept and Expend Grant – Code for America Labs, Inc. - \$105,000	1-1
5	12-1139 Lease and Use Agreement – China Airlines, Limited	5-1
6	12-1170 Real Property Lease Amendment – Autodesk, Inc. – Pier 9.....	6-1
7	12-1169 Contract Amendment – Aon Insurance Services West, Inc. – Central Subway Project – Not to Exceed \$8,280,000.....	7-1

Item 7
File 12-1169

Department:
San Francisco Metropolitan
Transportation Agency

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve the Second Amendment to the contract between the San Francisco Metropolitan Transportation Agency (SFMTA) and Aon Risk Insurance Services West, Inc. (Aon) for Aon to provide to the SFMTA insurance brokerage services for an Owner Controlled Insurance Program (OCIP) to (a) increase the amount of excess liability insurance provided by SFMTA for the Central Subway Project by \$150,000,000, from \$150,000,000 to \$300,000,000, and (b) increase the contract amount provided by the SFMTA to Aon by \$8,280,000, from not-to-exceed \$9,808,750 to not-to-exceed \$18,088,750 for the eight-year insurance policy term beginning January 23, 2012 and ending January 22, 2020.

Key Points

- The Central Subway Project is the second phase of the SFMTA's Third Street Light Rail Project. The Project will issue an estimated \$1,080,577,722 in construction contracts, including (a) two utility relocation contracts, (b) one tunnel contract, and (c) one contract ("station contract") to construct one surface-level and three underground subway stations, tracks, and related systems.¹ The two utility relocation contracts have been completed, the tunnel contract has been awarded and is under construction, and the station contract was submitted for competitive bid in October 2012 with bids due in March 2013.
- Initially, SFMTA required the tunnel contractor to provide \$350,000,000 and the station contractor to provide \$200,000,000 in primary liability insurance. SFMTA was to provide an additional \$150,000,000 in excess liability insurance through the OCIP to cover both the tunnel contract and the station contract.
- In February 2012, SFMTA selected Aon, based on a competitive Request for Proposals (RFP), to provide OCIP brokerage services to obtain \$150,000,000 of excess liability insurance for both the existing tunnel contract and the proposed station contract. However, because potential bidders for the station contract were not able to obtain \$200,000,000 in primary liability insurance, SFMTA has decided through the proposed Second Amendment of the contract with Aon to reduce the primary liability insurance to be provided by the station contractor by \$150,000,000 from \$200,000,000 to \$50,000,000, and add an additional \$150,000,000 of excess liability insurance to be provided by SFMTA, increasing the total excess liability insurance amount to be provided by SFMTA from \$150,000,000 to \$300,000,000.

¹ The three underground subway stations are (a) Chinatown Station at Stockton and Washington Streets, (b) Union Square/Market Street Station, and (c) Yerba Buena/ Moscone Station. The surface level station is on 4th Street between Brannan and Bryant Streets.

Fiscal Impact

- The contract amount of \$18,088,750 is included in the Central Subway Project budget. According to Mr. Arthur Wong, the SFMTA's Central Subway Project's Construction Manager, the total Central Subway Project budget is an estimated \$1,578,300,000 of which \$1,080,577,722 are construction costs. Mr. Wong further noted that Federal, State, and local funding for the Central Subway Project has been committed.

Policy Consideration

- Actual expenditures of \$9,271,240 under the existing contract with Aon are \$537,510 less than the not-to-exceed previously authorized amount of \$9,808,750 under the existing contract with Aon. According to Mr. Rob Stone, Deputy City Attorney, amending the proposed resolution to reduce the total requested contract not-to-exceed amount by \$537,510, from \$18,088,750 to \$17,551,240, would require further SFMTA Board of Directors approval, delaying implementation of the proposed Second Amendment for SFMTA to purchase the necessary \$150,000,000 of additional excess liability insurance for the Central Subway Project. Therefore, in order to not delay implementation of the proposed Second Amendment and still acknowledge that the needed not – to-exceed contract expenditures are \$17,551,240, the Budget and Legislative Analyst recommends amending the proposed the proposed resolution to add the following resolved clause:

“Further resolved, the San Francisco Municipal Transportation Agency acknowledges that the needed contract expenditures are \$17,551,240, which is \$537,510 less than the requested contract not-to-exceed amount of \$18,088,750 under the proposed Second Amendment”

Recommendations

- Amend the proposed resolution to add the clause: “Further resolved, the San Francisco Municipal Transportation Agency acknowledges that the needed expenditures under the Aon contract are \$17,551,240, which is \$537,510 less than the requested contract not-to-exceed amount of \$18,088,750 under the proposed Second Amendment.”
- Approve the proposed resolution as amended.

MANDATE STATEMENT/ BACKGROUND

In accordance with Charter Section 9.118, any agreement (a) for more than \$10,000,000, (b) that extends for longer than ten years, or (c) with an amendment of more than \$500,000, is subject to Board of Supervisors approval.

Background

The Central Subway Project is the second phase of the SFMTA's Third Street Light Rail Project that will add 1.67 miles of light rail track from the northern end of the new Third Street Light Rail at Fourth and King Streets to a terminal in Chinatown. The Project will issue an estimated \$1,080,577,722 in construction contracts, which include:

- (a) Two utility relocation contracts that have been completed;
- (b) One tunnel contract that was awarded to Barnard, Impregilo, Healy Joint Venture Partnership (Barnard, Impregilo, Healy) through a competitive bid in June 2011; and
- (c) One contract ("station contract") to construct one surface-level and three underground subway stations, tracks, and associated systems that was submitted for competitive bid in October 2012 with bids due in March 2013.²

Initially, SFMTA required (1) the tunnel contractor to provide two tiers of insurance coverage: \$200,000,000 in primary and \$150,000,000 in excess liability insurance, totaling \$350,000,000; and (2) the station contractor to provide one tier of insurance coverage of \$200,000,000 in primary liability insurance. SFMTA was to provide \$150,000,000 in excess liability insurance through the Owner Controlled Insurance Program (OCIP) to cover both the tunnel contract and the station contract.³

On February 7, 2012, after a competitive Request for Proposals (RFP) process, SFMTA executed a contract with Aon Risk Insurance Services West, Inc. (Aon) for OCIP insurance brokerage services, in which Aon provides to SFMTA \$150,000,000 of excess liability insurance for both the existing tunnel contract between SFMTA and Barnard, Impregilo and Healy, and the proposed station contract, which has not yet been awarded. The original contract between SFMTA and Aon is for a not-to-exceed amount of \$9,808,750 and an eight-year term. That contract was not subject to Board of Supervisors approval because it was for a term of less than ten-years and an amount less than \$10,000,000.

According to Mr. Arthur Wong, the SFMTA's Central Subway Project's Construction Manager, subsequent to the award of the contract to Aon, SFMTA submitted two Central Subway station construction contracts – Union Square/Market Street and Chinatown – to competitive bid. The responsive bids exceeded construction estimates, in part, according to Mr. Wong, because the

² The underground subway stations are (a) Chinatown Station at Stockton and Washington Streets, (b) Union Square/Market Street Station, and (c) Yerba Buena/ Moscone Station. The surface level station is on 4th Street between Brannan and Bryant Streets.

³ The \$150,000,000 in excess liability insurance provided by SFMTA through the OCIP is "rolling coverage", in which the amount of coverage remains constant, even as phases of tunnel or station construction are completed.

cost to contractors to obtain \$200,000,000 in primary liability insurance was prohibitively high.⁴ According to Mr. Wong, the bidder's premium quotes ranged from \$8,000,000 to \$13,000,000 per station, which would result in premium costs that would exceed the Central Subway Project budget.

SFMTA conducted a second competitive RFP process in October 2012, combining the three subway stations, one surface level station, tracks and associated systems into one bid, as noted above, with bids due in March 2013. Under the second competitive process, the subway station contractor's primary liability insurance requirement was reduced by \$150,000,000 from \$200,000,000 to \$50,000,000 in order to reduce contract costs and encourage more contractors to bid.

SFMTA proposes to provide the balance of \$150,000,000 in excess liability insurance through an amendment to the existing OCIP contract between SFMTA and Aon. Therefore, SFMTA will provide \$300,000,000 in excess liability insurance for the Central Subway Project, including \$150,000,000 under the original contract between SFMTA and Aon, and \$150,000,000 under the proposed Second Amendment as shown in Table 1 below.⁵ The resolution to authorize the contract's proposed Second Amendment for the second tier of excess liability insurance was adopted by the SFMTA Board of Directors on November 6, 2012.

Table 1 – Central Subway Station Construction Liability Insurance

Insurance Provided by:	Original OCIP Contract Amount	Proposed Second Amendment	Increase/ (Decrease)
Tunnel Contractor (First Tier)	\$200,000,000	\$200,000,000	\$0
Tunnel Contractor (Second Tier)	150,000,000	150,000,000	0
Subway Station Contractor	<u>200,000,000</u>	<u>50,000,000</u>	<u>(150,000,000)</u>
Subtotal, Insurance to be Provided by Contractor	550,000,000	400,000,000	(150,000,000)
Insurance to be Provided by SFMTA	150,000,000	300,000,000	150,000,000
Total Liability Insurance	\$700,000,000	\$700,000,000	\$0

DETAILS OF PROPOSED LEGISLATION

The proposed Second Amendment would amend the contract (Contract No. CS-163-1), between SFMTA and Aon for insurance brokerage services for an Owner Controlled Insurance Program (OCIP)⁶ to (a) increase the amount of excess liability insurance provided by SFMTA for the Central Subway Project by \$150,000,000, from \$150,000,000 to \$300,000,000, with a corresponding reduction of \$150,000,000 of primary liability insurance to be provided by the

⁴ According to Aon, the increased price in primary liability insurance is due to (a) recent natural disasters which have increased demand in the liability insurance market and (b) the City's presence in the insurance market seeking excess liability insurance coverage for the Central Subway Project

⁵ The First Amendment to the contract provided changes to the procedures for making premium payments.

⁶ An OCIP is an insurance policy that is held by the property owner during construction which covers all liability and loss for the owner, contractors and subcontractors that could result from the project.

Central Subway Project contractor from \$200,000,000 to \$50,000,000, and (b) authorize SFMTA to bind each layer of excess liability insurance coverage that Aon negotiates up to a maximum of \$150,000,000 for station construction⁷.

Under the proposed Second Amendment, the contract not-to-exceed amount provided by the SFMTA to Aon would increase by \$8,280,000, from \$9,808,750 to \$18,088,750. The contract term would remain at eight years, beginning January 23, 2012 and ending January 22, 2020.

FISCAL IMPACTS

The estimated increased cost for the additional \$150,000,000 of excess liability insurance coverage, to be provided by the SFMTA, payable by the SFMTA to Aon, is \$8,280,000 inclusive of all premiums, fees, costs and taxes as shown in Table 2 below.

Table 2: Second Tier Insurance Premium Expenditures under the Agreement between SFMTA and Aon Risk Insurance Services

Second Tier Excess Liability Insurance Premium	Amount
Insurance	\$8,000,000
Taxes & Fees (3.5% of Premium)	280,000
Total	\$8,280,000

According to Mr. Wong, the estimated cost for the second tier of excess liability insurance was based on the (1) availability of the excess liability insurance in the market, (2) the construction value of the project, (3) the overall risk of the construction work, and (4) the premium costs previously negotiated with the underwriters that provided the first tier of excess liability coverage.

As shown in Table 3 below, the total estimated cost for the Central Subway Project is \$1,578,291,000. \$1,080,577,722 of the total Project cost is for construction, including the general liability insurance and contingencies for the station contracts.

Table 3: Central Subway Project Budget & Financial Plan

Cost	(\$Million)
Construction including Liability Insurance and Contingency	\$1,080,577,722
Right-of-Way, Land, Existing Improvements	37,389,029
Vehicles	26,385,653
Professional Services	359,216,593
Unallocated Contingency	74,722,003
Total Estimated Central Subway Cost	\$ 1,578,291,000

⁷ According to Mr. Matt Hansen, General Service Agency's Risk Management Division Director, because \$150,000,000 of excess liability coverage is a large amount, Aon must negotiate coverage levels and premium costs with several different underwriters. Each underwriter's coverage represents a different "layer" of coverage stacked upon one another to total \$150,000,000 of excess liability insurance. Binding each layer of insurance coverage obligates the underwriter to provide the specified amount of coverage at the premium that was presented in the underwriter's proposal. The agreement is bound until the final policy is issued.

As shown in Table 4 below, the estimated subtotal for the station contracts' General Liability Insurance is \$19,799,210, which includes \$8,280,000 for the second tier of excess liability insurance and \$11,519,210 for the general contractor to obtain \$50,000,000 of primary liability insurance. Mr. Wong noted that the premium cost for the \$50,000,000 of primary liability insurance will be higher than the premium cost for excess liability insurance because of the increased likelihood that claims will be filed for \$50,000,000 or less, as compared to claims that are filed for more than \$50,000,000, requiring the primary insurance provider to pay those claims.

Table 4: Estimated Central Subway Project Construction Contract Budget

Construction Project	Construction Cost	Liability Insurance Premiums (2.9% of Total Construction Costs)	Contingency (8.5% of Total Construction Costs)	Total Cost
Tunneling, Utility Relocation & Construction Related Services ¹	\$267,090,490	\$8,232,872	\$35,936,972	\$311,260,334
<u>Station Contracts²</u>				
Union Square/ Market Street	204,275,608	5,863,925	16,307,103	226,446,636
Chinatown	227,941,186	6,315,411	16,859,197	251,115,794
Moscone	129,043,117	3,587,280	4,124,576	136,754,973
Tracks and Systems	<u>141,453,880</u>	<u>4,032,594</u>	<u>9,513,511</u>	<u>154,999,985</u>
Subtotal Station Contracts	702,713,791	19,799,210	46,804,387	769,317,388
TOTAL	\$969,804,281	\$28,032,082	\$82,741,359	\$1,080,577,722

¹ Includes SFMTA's premium cost to provide \$150,000,000 of excess liability coverage under the original contract between Aon and SFMTA.

² Includes the station contractor's premium cost to provide \$50,000,000 of primary liability coverage and SFMTA's premium cost to provide \$150,000,000 of excess liability insurance under the proposed Second Amendment.

Funding for the Central Subway Project has been committed by Federal, State and local sources, as shown in Table 5 below.

Table 5: Funding Sources for Central Subway Project

Funding	(\$Millions)
Federal 5309 New Starts Program	\$942,200,000
Federal Congestion Mitigation & Air Quality Program (CMAQ)	41,030,000
State Regional Transportation Improvement Program Grant ¹ (RTIP)	88,000,000
State Traffic Congestion Relief Program Grant (TCRP)	14,000,000
State Proposition 1A - High Speed Rail	61,310,000
State Proposition 1B – Public Transportation Modernization, Improvement, and Service Enhancement Account (PTMISEA)	307,780,000
Proposition K Sales Tax Funds	123,980,000
Total Central Subway Funding	\$ 1,578,300,000

¹ According to Mr. Wong, State RTIP funds have been committed but will not be received until August 2017.

POLICY CONSIDERATION

Based on an inquiry by the Budget and Legislative Analyst's Office, according to Mr. Wong, the SFMTA has expended \$9,271,240 on the first tier of \$150,000,000 of excess liability insurance which is \$537,510 less than the existing not-to-exceed authorized amount of \$9,808,750 under the existing contract with Aon. Therefore, the estimated amount needed for the additional excess liability insurance premium payments and related costs is \$17,551,240, which is \$537,510 less than the requested contract's not-to-exceed amount of \$18,088,750. However, according to Mr. Rob Stone, Deputy City Attorney, amending the proposed resolution to reduce the requested not-to-exceed contract amount by \$537,510, from \$18,088,750 to \$17,551,240, would require further SFMTA Board of Directors approval, delaying implementation of the proposed Second Amendment for the SFMTA to purchase the necessary \$150,000,000 of additional excess liability insurance for the Central Subway Project. Therefore, in order to not delay implementation of the proposed Second Amendment and still acknowledge that the needed not-to-exceed contract amount with Aon is \$17,551,240, or \$537,510 less than the requested not-to-exceed amount of \$18,088,750, the Budget and Legislative Analyst recommends amending the proposed resolution to add the following resolved clause:

“Further resolved, the San Francisco Municipal Transportation Agency acknowledges that the needed Aon contract expenditures are \$17,551,240, which is \$537,510 less than the requested contract not-to-exceed amount of \$18,088,750 under the proposed Second Amendment.”

RECOMMENDATIONS

1. Amend the proposed resolution to add the clause: “Further resolved, the San Francisco Municipal Transportation Agency acknowledges that the needed expenditures under the Aon contract are \$17,551,240, which is \$537,510 less than the requested contract not-to-exceed amount of \$18,088,750 under the proposed Second Amendment.”
2. Approve the proposed resolution as amended.