

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

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**TO:** Budget and Finance Sub-Committee  
**FROM:** Budget and Legislative Analyst  
**SUBJECT:** March 2, 2011 Budget and Finance Sub-Committee Meeting

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<b>Item 2</b> <b>File 11-0068</b>	<b>Departments:</b> Assessor-Recorder; Controller
<b>EXECUTIVE SUMMARY</b>	
<p><b>Legislative Objectives</b></p> <ul style="list-style-type: none"> <li>• The proposed ordinance would amend Chapter 10, Sections 10.177-2 and 10.177-3 of the San Francisco Administrative Code, to modify and extend the Assessor-Recorder's Office's Real Estate Watchdog Program.</li> </ul> <p><b>Key Points</b></p> <ul style="list-style-type: none"> <li>• On February 7, 2006, the Board of Supervisors approved the creation of the Assessor-Recorder's Office's Real Estate Watchdog Program (File 05-1759). The Real Estate Watchdog Program authorizes the Assessor-Recorder's Office to recommend rewards to individuals who provide the City with information related to the underpayment of Property Taxes owed to the City, when the underpayment results from a change in property ownership. The reward would be paid to the referrer from the General Fund if such a reward is authorized by the Board of Supervisors in separate legislation.</li> <li>• In five years of the Real Estate Watchdog Program, the Assessor-Recorder's Office has received 2 eligible referrals and 60 ineligible referrals of underpayment of Property Taxes, or a total of 62 referrals, resulting in the City collecting \$1,074,349 in outstanding Property Taxes and issuing one reward for \$66,600 from the City's General Fund.</li> <li>• The sections of the Administrative Code authorizing the Real Estate Watchdog Program expired on February 16, 2011.</li> <li>• The proposed ordinance would amend the Administrative Code to extend the Real Estate Watchdog Program for five years, beginning on the effective date of the proposed ordinance, streamline the program, and reduce the maximum allowable reward from \$500,000 to \$100,000.</li> </ul> <p><b>Fiscal Impacts</b></p> <ul style="list-style-type: none"> <li>• If a referral to the Real Estate Watchdog Program results in the collection of outstanding Property Taxes, the Assessor-Recorder's Office can recommend a reward up to an amount of 10 percent of the tax collected, with a modified maximum allowable reward of \$100,000. Any reward payable under the Real Estate Watchdog Program is subject to Board of Supervisors approval.</li> </ul> <p><b>Recommendation</b></p> <ul style="list-style-type: none"> <li>• Approve the proposed ordinance.</li> </ul>	

## MANDATE STATEMENT

Section 10.177-2 of the City's Administrative Code authorizes the Assessor-Recorder's Office to recommend a reward to be authorized by the Board of Supervisors payable from the General Fund for information leading to the detection of an underpayment of Property Taxes owed to the City and County of San Francisco when the underpayment results from a change of property ownership.

Section 10.177-3 of the City's Administrative Code requires the Controller to pay any reward authorized pursuant to Section 10.177-2 above, provided that (a) an application for such reward is filed in the Controller's Office, (b) the Assessor-Recorder's Office has recommended that the reward be paid on the application, and (c) the recommended reward amount is authorized by the Board of Supervisors.

## BACKGROUND

The California Constitution generally limits annual increases in the assessed taxable value of real property to two percent of the property's adjusted base year value, but requires that real property be reassessed at its full cash value when that real property undergoes a change in ownership. Because of difficulties in identifying changes of ownership, particularly in commercial and industrial properties, some properties may escape reassessment at full market value upon a change in ownership. In particular, the transfer of commercial properties may not always be properly reported to the City, and therefore may result in underpayments of Property Taxes. By contrast, the transfer of residential properties requires that a deed be recorded and therefore such residential properties are less likely to be subject to underpayments of Property Taxes.

On February 7, 2006, the Board of Supervisors approved, as a pilot program, the creation of the Assessor-Recorder's Office's Real Estate Watchdog Program, for the five-year period from February 16, 2006 to February 16, 2011, by amending Chapter 10, Sections 10.177-2 and 10.177-3 of the San Francisco Administrative Code to authorize the Assessor-Recorder's Office to recommend rewards for information related to the detection of underpayment of Property Taxes owed to the City and County of San Francisco, when the underpayment results from a change in property ownership (File 05-1759).

Under the Real Estate Watchdog Program, individuals who provide information to the Assessor-Recorder's Office that leads to the detection of an underpayment of Property Taxes owed to the City, when the underpayment results from a change in property ownership, are eligible for a reward to be paid from the City's General Fund if rewards are authorized by the Board of Supervisors in separate legislation. According to the Controller's Office, the rewards are paid from the General Fund Reserve.

Under Section 10.177-2(C) of the Administrative Code, an individual is eligible for rewards under the Real Estate Watchdog Program when:

1. The referrer files an application for reward along with supporting documentation in the Controller’s Office;
2. The Assessor certifies that the unreported change of property ownership will result in a reassessment leading to the actual collection of the Property Taxes or a lien or other device that is reasonably likely to result in the collection of the additional Property Taxes;
3. The referrer must not have participated in concealing the unreported transfer; and
4. The information furnished must be information previously unknown to the Assessor-Recorder.

The Assessor-Recorder’s Office makes a determination on each application filed with the Controller and transmitted by the Controller to the Assessor-Recorder’s Office. If the Assessor-Recorder’s Office determines that a reward is warranted, the Assessor-Recorder’s Office then submits such reward information to the Board of Supervisors for approval.

In accordance with Section 10.177-2 of the City’s Administrative Code, the amount of the reward cannot exceed ten percent of the amount of the underpayment of the Property Taxes collected by the City from the date of the unreported change in property ownership to the date the information is provided to the Assessor-Recorder’s Office, up to a maximum reward amount of \$500,000.

**Results of the Real Estate Watchdog Program, to Date**

Table 1 below summarizes the results of the Real Estate Watchdog Program, to date.

**Table 1: Results of the Real Estate Watchdog Program, Between February 17, 2006 and February 16, 2011**

Total years of the program	5
Number of referrals received	62
Referrals received prior to FY 2009-10	55
Referrals received in FY 2009-10	7
Referrals received in FY 2010-11	0
Number of ineligible referrals	60
Number of eligible referrals	2
Value of additional Property Tax Collections from the two eligible referrals	
Case #1	\$1,070,898
Case #2	<u>3,451</u>
<b>Total</b>	<b>\$1,074,349</b>

According to Mr. Mark McLean of the Assessor-Recorder's Office, the bulk of the 60 ineligible referrals were ineligible because those property transfers were already known to the Assessor-Recorder's Office.

The City has issued one reward under the Real Estate Watchdog Program. On October 28, 2008, the Board of Supervisors approved a reward in the amount of \$66,600 (File 08-1216) to the referrer of Case #1, as shown in Table 1 above. According to Mr. Mclean, "the referrer of Case #1 was eligible for a reward of up to \$83,251, which equaled ten percent of the increase in tax due from the date of the unreported change in ownership to the date the information was provided. The Assessor recommended that the referrer be awarded eighty percent of the maximum allowable which equals \$66,600." Mr. McLean noted that the referrer of Case #2, who was eligible for a reward of up to \$345, opted not to receive a reward, although the City received an additional \$3,451 in Property Taxes, based on the information provided.

### **Recommendations of the Controller and the Assessor-Recorder's Office**

Administrative Code Section 10-177-2(h) requires "Not later than six months prior to the expiration of the Assessor's authority ... the Controller and the Assessor shall confer and recommend to the Board of Supervisors whether the Assessor's authority to recommend rewards under this ordinance should continue for an additional period." According to Ms. Julie Van Nostern, Chief Counsel for the City Attorney's Office, in order for the Board of Supervisors to consider whether or not to extend the existing Real Estate Watchdog Program, which expired on February 16, 2011, the Controller's Office and Assessor-Recorder's Office must file a formal written recommendation for such extension of the program.

On February 15, 2011, the Assessor-Recorder and the Controller's Office submitted a memorandum to the Clerk of the Board of Supervisors recommending that the Board of Supervisors reauthorize and extend the Real Estate Watchdog Program.

## **DETAILS OF PROPOSED LEGISLATION**

The proposed ordinance would amend Chapter 10, Sections 10.177-2 and 10.177-3 of the San Francisco Administrative Code, to modify and extend the Assessor-Recorder's Real Estate Watchdog Program. Specifically, the proposed ordinance would (a) streamline the Program by having the Assessor-Recorder's Office assume responsibilities that are currently assigned to the Controller's Office, as summarized in Table 2, below, (b) reduce the maximum authorized reward amount from \$500,000 to \$100,000, which is payable to individuals who provide the City with information regarding underpayment of Property Taxes, if the City collects such additional Property Taxes as a result of information provided to the City regarding a change in property ownership, and (c) extend the Real Estate Watchdog Program by five years from the effective date of the proposed ordinance.

As noted in Table 1 above, for the five year period between February 16, 2006 and February 16, 2011, the City collected additional Property Taxes of \$1,074,349 under the existing Real Estate Watchdog Program.

The existing Assessor-Recorder's Office's Real Estate Watchdog Program expired on February 16, 2011. Ms. Angela D'Anna of the Assessor-Recorder's Office advises that the proposed ordinance would extend the Real Estate Watchdog Program by an additional five years, commencing on the effective date of the approval of the proposed ordinance.

As shown in Table 2 below, the five year extension of the Assessor-Recorder's Office's Real Estate Watchdog Program would also result in Assessor-Recorder's Office assuming the following duties now handled by the Controller's Office:

**Table 2: Streamlining of Responsibilities Under the Proposed Ordinance**

Tasks	Current Responsible Department	Responsible Department Under Proposed Ordinance
Receive Real Estate Watchdog Program referral application	Controller	Assessor-Recorder
Forward application to the Assessor-Recorder's Office	Controller	(this task would be eliminated)
Submit Annual Reports about the Real Estate Watchdog Program to the Board of Supervisors	Controller and Assessor-Recorder	Assessor-Recorder
Make formal recommendation to the Board of Supervisors whether the Real Estate Watchdog Program should be extended in the future	Controller and Assessor-Recorder	Assessor-Recorder

## FISCAL IMPACTS

As shown in Table 1 above, under the Assessor-Recorder's Office's Real Estate Watchdog Program, the City realized \$1,074,349 in additional Property Tax revenues between February 16, 2006 and February 16, 2011. Under the existing program, one reward, in the amount of \$66,600, was paid from the City's General Fund. Because the number and value of future potential referrals are unknown, the Assessor-Recorder's Office cannot estimate the potential future additional Property Tax revenues to be realized as a result of the proposed extension of the Real Estate Watchdog Program.

According to Mr. McLean, the Assessor-Recorder's Office does not have a precise projection of hours and the related costs required to administer the Real Estate Watchdog Program. However, the Assessor-Recorder's office estimates two hours of total staff time per referral would be needed, or an average of approximately 20 staff hours per year, based on an estimated 10 referrals per year. Both Mr. McLean and Ms. D'Anna note that the Real Estate Watchdog Program has not resulted in significant administrative costs to either the Assessor-Recorder's Office or the Controller's Office, both of which have administered the Program within existing staff resources. As summarized in Table 2 above, under the proposed ordinance, the Controller's

Office's current administrative responsibilities would either be transferred to the Assessor-Recorder's Office or eliminated. Ms. D'Anna estimates that the additional Assessor-Recorder's Office responsibilities can be absorbed with existing staff. Under the proposed ordinance, the Controller's Office would only have (a) general oversight responsibilities and (b) under Section 10.177-3 of the City's Administrative Code, the Controller's Office would continue to have the responsibility for paying any Real Estate Watchdog Program reward that is recommended by the Assessor-Recorder's Office and authorized by the Board of Supervisors.

As noted above, under the proposed ordinance, the maximum reward payable under the Assessor-Recorder's Real Estate Watchdog Program would be reduced from \$500,000 to \$100,000. In the February 15, 2011 memorandum to the Clerk of the Board, the Assessor and the Controller stated "It is our belief that a reward of up to \$100,000 will sufficiently incentivize watchdogs to report high-value commercial and residential property escapes."

As noted above, the one reward that has been paid by the City to date under the Real Estate Watchdog Program, was \$66,600, which is well below both the previous maximum reward amount of \$500,000 and the proposed maximum reward amount of \$100,000.

## **RECOMMENDATION**

Approve the proposed ordinance.

**Item 3**  
**File 11-0151**

**Departments:**  
Recreation and Park Department (RPD)

## EXECUTIVE SUMMARY

### Legislative Objective

- The proposed ordinance would appropriate a \$6,995,000 loan from the California Department of Boating and Waterways (DBW) to be used for the renovation of the West Harbor Project of the Recreation and Park Department (RPD) Marina Yacht Harbor.

### Key Points

- The West Harbor Renovation Project includes (a) demolition of 327 existing berths and construction of 325 reconfigured berths, (b) upgrading the electrical and water dock utilities, and (c) harbor dredging.
- On December 5, 2008, the Board of Supervisors approved a \$25,850,000 State loan, on a cost reimbursement basis, to complete the West Harbor Renovation Project. However, due to State budgetary issues, the State notified the RPD that the loan was reduced by \$2,355,000 to \$23,495,000.
- On April 2, 2009, the Board of Supervisors approved \$16,500,000 loan funds to the RPD, out of the total loan of \$23,495,000. On January 11, 2011, the State notified the RPD regarding the availability of the remaining loan amount of \$6,995,000 for the West Harbor Renovation Project.

### Fiscal Impacts

- Currently, the West Harbor Renovation Project's total estimated cost is \$24,810,000, which is \$1,315,000 more than the total available \$23,495,000 State loan. The RPD plans to allocate \$1,315,000 from the Marina Yacht Harbor Project Fund, which has a balance of \$4,000,000 as of February 2011, in FY 2010-2011 to the West Harbor Renovation Project.
- Repayment of the total State principal loan of \$23,495,000 plus \$20,305,000 interest (based on an interest rate of 4.5 percent per annum) will cost the RPD a total of \$43,800,000, or \$1,460,000 annually over 30 years. The RPD plans to repay the State loan funds from annual net income from the West Harbor operations, which accrue to the Marina Yacht Harbor Fund. Pursuant to the loan agreement between RPD and the State, the RPD must maintain a minimum debt coverage ratio of 1.25 of net income plus prior year's cumulative surplus to annual debt service.
- The RPD has allocated a ten percent construction contingency amount of \$1,875,598. If this contingency is not sufficient to cover potential construction cost overruns, the RPD plans to finance additional costs from the Marina Yacht Harbor Fund, which has a fund balance of \$4,000,000.
- However, the RPD assumes a 45 percent berth rental rate increase effective FY 2012-2013, rather than the approximately 37 percent rate increases that were previously approved by the Board of Supervisors, in order to meet the State's debt obligations under the proposed loan agreement.

### Recommendation

- Continue the proposed ordinance to the Call of the Chair in order to allow RPD to submit accompanying legislation to increase the West Harbor berth rental rates to fully meet the subject State loan obligations.

**MANDATE STATEMENT / BACKGROUND****Mandate Statement**

Charter Section 9.105 requires that amendments to the annual appropriation ordinance be approved by ordinance of the Board of Supervisors, and not be adopted unless the Controller certifies the availability of funds.

**Background**

The San Francisco Marina Yacht Harbor consists of two harbors, located approximately one-half mile east of the Golden Gate Bridge and west of Fort Mason: (a) the West Harbor, which consists of 327 berths, and (b) the East Harbor, which consists of 342 berths. The West Harbor Renovation Project would consist of the (a) demolition of 327 existing berths and construction of 325 reconfigured berths, (b) upgrading the electrical and water dock utilities, and (c) harbor dredging.

According to Ms. Mary Hobson, Project Director at the Recreation and Park Department (RPD) Capital Improvement Division, the East Harbor Renovation Project is currently unfunded, and there is no set schedule for its implementation. The project scope would consist of the (a) demolition of existing and construction of new docks, slips, gangways and gates, (b) upgrades to dockside utilities, (c) maintenance dredging, (d) installation of a new pump station, (e) installation of a new floating breakwater, (f) upgrade to the boat launch facility and adjacent dry boat storage yard, (g) renovation of the restrooms, and (h) construction of a new maintenance facility.

According to Ms. Hobson, the RPD applied to the California Department of Boating and Waterways (DBW) for State loan funding in 2002 in the amount of \$42,000,000 to renovate both the East Harbor and the West Harbor. Subsequently, the East Harbor Renovation Project and the West Harbor Renovation Project were divided into two separate projects. Ms. Hobson advises that the East Harbor Renovation Project loan funds from the State will be reconsidered for approval by the State at an undetermined date in the future.

On February 21, 2008, the RPD was awarded a State loan of \$25,850,000 from the DBW to fund the above-described West Harbor Renovation Project. On December 5, 2008, the Board of Supervisors approved the acceptance of the \$25,850,000 loan from the State for the West Harbor Renovation Project (Resolution No. 491-08, File No. 08-1329). According to Ms. Katharine Petrucione, Director of Administration and Finance for the RPD, this State loan is on a cost reimbursement basis, such that the RPD must first expend RPD funds and then submit claims to the State to get reimbursed for any expenditures on the West Harbor Renovation Project up to the maximum loan amount.

On March 16, 2009, the State notified the RPD that (a) due to State budget problems, the original loan amount of \$25,850,000 was being reduced to \$23,495,000, a reduction of

\$2,355,000, and (b).\$16,500,000 of loan funds were currently available for the RPD, out of the total loan of \$23,495,000, for the West Harbor Renovation Project. The \$16,500,000 was approved by the Board of Supervisors on April 2, 2009 (Ordinance No. 44-09, File 09-0131).

According to Ms. Hobson, the interest rate on the unpaid balance of the amended loan of \$23,495,000 is 4.5 percent per annum. Ms. Hobson advises that repayment of the total \$23,495,000 principal State loan plus interest costs of \$20,305,000 over 30 years will result in total loan repayments from the RPD to the State of \$43,800,000, which will be made by the RPD in 30 annual payments of \$1,460,000 each. The loan principal and interest repayments are not required to begin until FY 2012-2013, when the West Harbor Renovation Project is completed. Pursuant to the terms of the loan agreement between the RPD and the State, the RPD is required to maintain a minimum debt coverage ratio of 1.25 of net income plus prior year's cumulative surplus to annual debt service.

According to Ms. Petrucione, the State has required the RPD to begin making interest only payments in August 2010, on State loan funds already reimbursed by the State to the RPD for costs incurred for the West Harbor Renovation Project. As of February 2011, Ms. Petrucione advises that the RPD has received total reimbursements of \$1,480,000 from the State, such that to date, the RPD has repaid the State a total of \$20,085 in interest expenses. Ms. Petrucione advises that the State is not requiring the RPD to demonstrate a minimum debt service ratio until the West Harbor Renovation Project is completed and the State fully reimburses the RPD for all expenditures. Ms. Petrucione advises that the RPD is making the interest only payments to the State from annual net income from the West Harbor operations revenues, which accrue to the Marina Yacht Harbor Fund, a special revenue fund administered by the RPD. The Marina Yacht Harbor's revenues are recovered from berth rental fees and concession revenues. Such revenues are also used to pay for operating expenses, as well as facilities maintenance and capital repairs to the existing Marina Yacht Harbor facilities.

Ms. Hobson advises that, based on a competitive Request for Proposal (RFP) process, preliminary design and technical investigations of the West Harbor Renovation Project was completed by the firm, Winzler & Kelly, on December 31, 2009 for a total cost of \$1,966,410. Ms. Hobson also advises that the RPD entered into an emergency sole source agreement with Salt River Inc. in 2009 at a cost of \$198,900 to perform urgent dredging<sup>1</sup> activities. Ms Hobson advises that a number of factors led to the emergency agreement: (a) a different firm that was previously secured by the RPD through a competitive bid process withdrew from the agreement, (b) the window of opportunity to dredge was going to lapse because the RPD could only dredge during six months of the year, and (c) sand was accumulating in the water, such that boats would not be able to enter and exit the West Harbor. Ms. Hobson adds that the RPD also entered into a

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<sup>1</sup> Ms. Hobson advises that dredging excavates valueless underwater bottom sediments and disposes of them at a different location.

competitively bid agreement with Vortex Marine Inc. at a cost of \$403,704 in 2010 to complete a needed sandmining<sup>2</sup> project in the West Harbor.

Ms. Hobson advises that, on September 21, 2010 and November 4, 2010, the RPD secured two of the three required construction permits from the California Regional Water Quality Control Board and the San Francisco Bay Conservation and Development Commission, respectively, in order to begin the construction project phase of the West Harbor Renovation Project. According to Ms. Hobson, the third required permit is being secured from the Army Corps of Engineers and is expected to be obtained in March 2011.

On October 8, 2010, the RPD issued a competitive bid for the construction of the West Harbor Renovation Project. On December 15, 2010, the RPD received two bids from four qualified firms. Based on the two bids received, the RPD awarded a construction agreement on January 20, 2011 to the lowest-bidder firm, Dutra Construction Inc., in the amount of \$18,755,348. Under this \$18,755,348 construction agreement, Dutra Construction Inc. will provide (a) maintenance dredging, (b) seawall repairs, (c) hazardous material handling, (d) site landscaping, (e) breakwater repairs, and (f) utility infrastructure work. Construction is expected to begin the first week of April 2011. In accordance with Section 9.118 of the City's Charter, construction agreements are not subject to the Board of Supervisors approval.

The reduced State total loan award of \$23,495,000, less the previously allotted State loan funds to RPD of \$16,500,000 resulted in a remaining balance of State loan funds of \$6,995,000. On January 11, 2011, the State notified the RPD as to the availability of the remaining loan funds of \$6,995,000 (\$23,495,000 less \$16,500,000) to be used for the construction project phase of the West Harbor Renovation Project.

## **DETAILS OF PROPOSED LEGISLATION**

The proposed ordinance would appropriate State loan proceeds of \$6,995,000, which is the remaining loan installment from the total State loan amount of \$23,495,000, for the Marina Yacht Harbor's West Harbor Renovation Project.

The proposed appropriation of \$6,995,000 in State loan proceeds would be used by the RPD to partially fund the West Harbor Renovation Project's construction agreement of \$18,755,348 with Dutra Construction Inc.

## **FISCAL IMPACTS**

Currently, the West Harbor Renovation Project is estimated to cost a total of \$24,810,000, which is \$1,315,000 more than the total reduced State loan amount of \$23,495,000. According to Ms. Petrucione, the RPD will allocate \$1,315,000

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<sup>2</sup> Ms. Hobson advises that sandmining operations result in the excavation and sale of underwater bottom sediments with value, such as sand and other mineral deposits, which are then sold at market value.

(\$24,810,000 less \$23,495,000) from the RPD's Marina Yacht Harbor Project Fund, to fund the difference between the costs to complete the West Harbor Renovation Project and available State loans. According to Ms. Petrucione, the Marina Yacht Harbor Project Fund's balance is approximately \$4,000,000 as of February 2011.

Attachment I, provided by Ms. Hobson, provides a budget for the West Harbor Renovation Project. As shown in Attachment I, the budget of \$24,810,000 is divided into two major categories: (a) \$3,576,451 for Design and Engineering, Construction Services and Regulatory Agency Approval expenditures, and (b) \$21,233,550 for Construction expenditures. According to Ms. Petrucione, a total of approximately \$2,569,014 of the total estimated project cost of \$24,810,000 has been expended to date, including (a) \$1,966,410 for design and engineering, (b) \$198,900 for emergency dredging, and (c) \$403,704 for other dredging activities. Ms. Petrucione advises that, to date, the State has reimbursed \$1,480,000 in State loan funds to the RPD.

According to Ms. Hobson, the subject \$6,995,000 loan amount from the State is subject to the same loan terms as the initial loan amount of \$16,500,000, including an annual interest rate of 4.5 percent on the unpaid loan balance. As noted above, the City must first incur the costs and then submit claims to the State for reimbursement up to the maximum \$23,495,000 State loan. Repayment of the entire \$23,495,000 State loan plus \$20,305,000 of interest expense at a rate of 4.5 percent per year over 30 years will result in the RPD incurring total costs of \$43,800,000, which will be made in 30 annual payments of approximately \$1,460,000 each, beginning in FY 2012-2013.

According to Ms. Hobson, the RPD plans to repay the entire \$43,800,000 State loan and interest expenses from increased annual net income<sup>3</sup> from the West Harbor operations. Ms. Petrucione advises that annual revenues, including berth rental fees, and concession revenues from the West Harbor operations, accrue to the Marina Yacht Harbor Fund. The estimated revenues from the berth rental fees, concession revenues and the associated cash flow projections and debt coverage ratios from FY 2009-2010 through FY 2041-2042 are shown in Attachment II, provided by Ms. Petrucione.

Ms. Petrucione notes that the Board of Supervisors previously approved increases to the berth rental rates of approximately 37 percent in FY 2012-2013 to cover the total \$23,495,000 State loan. However, the Budget and Legislative Analyst notes that the projected revenues shown in Attachment II assume an increase of 45 percent in berth rental rates beginning in FY 2012-2013. According to Ms. Petrucione, the terms of the subject \$6,995,000 State loan requires that the RPD create a separate Escrow Account, funded over ten-years after completion of the West Harbor Renovation Project, to provide two years of set-aside loan payments, or approximately \$2,920,000 (\$1,460,000 times two years) as additional security to the State for repayment of the State loan. As

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<sup>3</sup> On November 19, 2008, the Board of Supervisors approved Ordinance No. 0307-08 (File No. 08-1328), which authorized the RPD to increase the West Harbor berth rental fees by approximately 37 percent per berth in FY 2012-2013, or upon completion of the West Harbor Renovation Project in order to offset the costs of the anticipated renovation of the West Harbor, to be funded with the total State loan fund proceeds of \$23,495,000.

shown in Attachment II, RPD anticipates contributing approximately \$285,000 annually for ten years from FY 2012-2013 through FY 2021-2022 to provide approximately \$2,850,000 into this Escrow Account Set Aside.

As noted above, pursuant to the terms of the loan agreement between the RPD and the State, the RPD is required to maintain, at a minimum, a debt coverage ratio of 1.25 of net income plus prior year's cumulative surplus to annual debt service. As shown in Attachment II, the total Marina Yacht Harbor revenues, including the berth rental fees, will result in estimated debt coverage ratios ranging from 1.81 in FY 2012-2013 to 22.54 in FY 2041-2042, which exceeds the State's required minimum debt coverage ratio of 1.25. However, as noted above, this assumes an increase in berth rental rates of 45 percent in FY 2012-2013, although the Board of Supervisors has only approved 37 percent (see Policy Consideration Section below).

Additionally, as shown in Attachment II, the estimated revenues from berth rental fee increases, beginning in FY 2012-2013, are projected to result in a cumulative surplus, of approximately \$32,144,000 for the West Harbor by FY 2041-2042. The berth rental fee increases, as previously approved by the Board of Supervisors, will assist in enabling the RPD to (a) pay debt service during FY 2012-2013 through FY 2015-2016 when the annual surplus is negative, and (b) fund ongoing capital and maintenance repairs needed by the West Harbor.

According to Ms. Petrucione and as shown in Attachment I, the RPD has allocated a contingency amount of \$1,875,598, or ten percent of the \$18,755,348 in the construction budget in the event that construction costs exceed available funding. If this contingency fund is not sufficient to cover potential cost overruns, the RPD plans to finance the additional costs through the Marina Yacht Harbor Fund, which, as noted above, has a fund balance of \$4,000,000 as of February 2011.

## **POLICY CONSIDERATION**

As discussed above, the Budget and Legislative Analyst notes that RPD is assuming berth rental rates will increase approximately 45 percent in FY 2012-2013, when the West Harbor Renovation Project is completed, in order to repay the State for the subject loan funds, create the State-required Escrow Account Set-Aside of approximately \$2,850,000, and meet the State's required 1.25 percent debt coverage ratio. However, to date, the Board of Supervisors has only approved approximately 37 percent in berth rental rate increases, not 45 percent with respect to the West Harbor berth rental rates. As of the writing of this report, the Budget and Legislative Analyst working with the RPD estimates that an approximate 40 percent increase in the West Harbor berth rental rates, instead of a 45 percent increase, would still enable the RPD to (a) make the annual \$1,460,000 debt service payments on the loan to the State, (b) fully fund the State-required Escrow Account Set-Aside over a ten-year period, and (c) meet the State-required debt coverage ratio of 1.25 percent.

Therefore, the Budget and Legislative Analyst recommends that the proposed ordinance be continued to the Call of the Chair to enable the Recreation and Park Department to submit accompanying legislation to increase the West Harbor berth rental rates to the required amounts in order to allow the RPD to fully meet the subject loan obligations.

## **RECOMMENDATION**

Continue the proposed ordinance to the Call of the Chair in order to allow RPD to submit accompanying legislation to increase the West Harbor berth rental rates to fully meet the subject State loan obligations.

	DBW CONTRACT ALLOWANCES	CURRENT BUDGET
<b>Principal Construction</b>		
D/B Phase 1 - Dutra Construction		\$12,528,506.00
D/B Phase 2 - Dutra Construction		\$6,226,842.00
Construction Contingency (10%)		\$1,875,535.00
<b>Misc/Other Construction</b>		
Dredging Contract - 2009, Salt River		\$198,900.00
Dredging Contract - 2010, Vortex Marine		\$403,704.00
<b>CONSTRUCTION BUDGET</b>	<b>\$18,796,000.00</b>	<b>\$21,233,487.00</b>
<b>Design &amp; Engineering</b>		
Desing/Engineering: Winzler & Kelly		\$1,966,410.00
HM Sampling & Testing: AGS/Kennetic		\$71,775.00
HM Assessment: Winzler & Kelly		\$16,292.00
Phase I Environmental Assessment: Baseline		\$9,740.00
Historic Resources Rpt: Carey/Furgo		\$9,400.00
Haz Mat Testing: North Tower Environmental		\$3,301.88
	\$2,819,400.00	\$2,076,918.88
<b>Construction Services</b>		
Construction Management		\$700,000.00
Materials Testing/Special Inspections		\$100,000.00
OLSE		\$8,000.00
	\$1,174,750.00	\$808,000.00
<b>Regulatory Agency Approvals</b>		
City Planning EIR Ammendment		\$11,945.72
Regional Water Quality Board		\$640.00
Bay Conservation & Development Commission		\$39,950.00
	\$704,850.00	\$52,535.72
<b>ENGINEERING &amp; PERMITS</b>	<b>\$4,699,000.00</b>	<b>\$2,937,454.60</b>
<b>Project Management</b>		
RPD PM		\$500,000.00
BOE PM		\$75,000.00
<b>Administration</b>		
BCM Contract Admin (Baseline)		\$1,220.00
BCM Contract Admin (Carey)		\$1,220.00
BCM Contract Admin (AGS/Kinnetic)		\$7,177.50
BCM Contract Admin (WK)		\$1,629.20
BCM Contract Admin (North Tower)		\$910.00
BOE Contract Prep		\$29,250.00
MOD - ADA Review		\$12,850.00
<b>Misc.</b>		
Elite / BPS / Other		\$9,740.00
<b>MANAGEMENT &amp; ADMINISTRATION</b>		<b>\$638,996.70</b>
<b>PROJECT CONTINGENCY (UNALLOCATED)</b>		
	<b>\$23,495,000.00</b>	<b>\$24,809,938.30</b>

TOTAL PROJECT COSTS Rounded to \$24,810,000



**Item 4**  
**File 11-0154**

**Department:**  
Department of Public Works; City Attorney's Office

## EXECUTIVE SUMMARY

### Legislative Objective

- The proposed ordinance would appropriate \$2,809,000 from the General Fund Reserve to the Department of Public Works (DPW) for litigation expenses related to Mitchell Engineering/Obayashi Corporation v. City and County of San Francisco, for the Fourth Street Bridge Project, including (a) \$300,000 for DPW's staff to assist the City Attorney's Office with litigation, and (b) a \$2,509,000 DPW work order with the City Attorney's Office for the provision of legal services.

### Key Points

- On March 10, 2003, after a competitive bid process, DPW awarded a \$16,978,570 construction agreement to Mitchell Engineering and the Obayashi Corporation (MEOC), a Joint Venture, for MEOC to construct the Fourth Street Bridge Project. Subsequent change orders by DPW increased the construction agreement to \$21,682,307. MEOC did not complete construction until May 1, 2006, which was 555 days subsequent to the required completion date of October 23, 2004.
- On February 28, 2008, MEOC filed a lawsuit against the City for an amount not less than \$20,000,000 to recover additional costs that MEOC alleges to have incurred to complete the Fourth Street Bridge Project. Subsequently, the City Attorney filed a cross-complaint against MEOC and Arch Insurance Company, MEOC's surety bond provider, for breach of contract and the recovery of liquidated damages totaling \$14,115,000 for the delay in completing the Fourth Street Bridge Project. All attempts at mediation and settlement have been unsuccessful.

### Fiscal Impacts

- If approved, this supplemental appropriation request of \$2,809,000 would reduce the City's General Fund Reserve, from the original FY 2010-2011 funding level of \$25,000,000 to \$22,191,000.
- A combined total of approximately \$319,740, or 11.4 percent of the requested \$2,809,000 is projected to be expended by the City Attorney (\$250,000) and DPW (\$69,740) retroactive from December 1, 2010 through March 8, 2011, such that the proposed ordinance should be amended to provide for retroactivity.
- Although the City Attorney considers the expenditures of the trial preparation and the forthcoming trial by the City Attorney's Office and DPW to be privileged and confidential, the City Attorney and DPW will provide such details to the Budget and Finance Committee on a confidential basis, if requested.

### Recommendations

- Amend the proposed ordinance to provide for retroactivity.
- Approval of the proposed ordinance, as amended, is a policy decision for the Board of Supervisors.

## MANDATE STATEMENT / BACKGROUND

### Mandate Statement

In accordance with Section 9.105 of the City Charter, subject to the Controller's certification of the availability of funds, the Board of Supervisors or the Mayor may initiate amendments to the annual appropriations ordinance, which must be subsequently approved by the Board of Supervisors.

### Background

The Board of Supervisors appropriated a total of \$42,056,978 from Federal, State, and local funding sources for the Department of Public Works (DPW) to construct the Fourth Street Bridge Project, in six previous DPW annual budgets (FYs 1999-2000, 2000-2001, 2004-2005, 2005-2006, 2006-2007, and 2007-2008), and seven previously approved legislative items (Resolutions 453-02, 132-01, 1158-99, 0096-03, 070-03; Ordinances 50-06 and 60-05).

Work on the Fourth Street Bridge Project, located on Fourth Street between Channel Street and Berry Street, includes (1) seismic retrofitting, (2) installing a redesigned counterweight<sup>1</sup>, (3) integrating rails for the Third Street Light Rail Project, to provide light rail service between Downtown and the Third Street Corridor, (4) refurbishing the Bridge's watchman and operator houses, (5) upgrading the mechanical, electrical, and control systems, (6) replacing the steel deck, and (7) repaving the approach spans and surrounding areas of the Fourth Street Bridge.

On March 10, 2003, subsequent to a competitive bid process, DPW awarded an initial \$16,978,570 construction agreement<sup>2</sup> to Mitchell Engineering and the Obayashi Corporation (MEOC), a Joint Venture, for MEOC to construct the Fourth Street Bridge Project. DPW added change orders totaling \$4,703,737 to the MEOC construction agreement, which increased the total construction agreement to \$21,682,307, in order to provide additional steel rehabilitation, a heavier-weight counterweight, the removal of timber piles<sup>3</sup>, and the reconstruction of the abutment<sup>4</sup> supporting the south end of the Fourth Street Bridge. Approval of the original \$16,978,570 construction agreement was not required by the Board of Supervisors because pursuant to Section 9.118(b) of the City Charter, construction agreements are not subject to Board of Supervisors approval. Approval of the \$4,703,737 in change orders, in accordance with Section 6.22(H) of the City's Administrative Code was subject to approval by the Mayor and the Controller. All funds for the Fourth Street Bridge Project were subject to appropriation approval by the Board of Supervisors.

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<sup>1</sup> The Fourth Street Bridge is a drawbridge that uses a counterweight to raise and lower the drawbridge.

<sup>2</sup> In addition to the initial \$16,978,570 construction agreement, DPW budgeted a ten percent construction contingency of \$1,697,857 for the Fourth Street Bridge Project. A total of \$4,703,737 in change orders, which included the \$1,697,857 construction contingency, was added to the MEOC construction agreement, increasing the total construction agreement to \$21,682,307.

<sup>3</sup> Timber piles are cylindrical timber columns driven into the channel bottom (bay mud and bedrock) to support the vertical load of the Bridge.

<sup>4</sup> An abutment supports the end of the bridge, such that the bridge loads are transferred to the foundation.

Construction of the Fourth Street Bridge Project commenced on April 28, 2003 and was completed on May 1, 2006, approximately three years later, which was 555 days subsequent to the required completion date of October 23, 2004.

The Fourth Street Bridge re-opened to traffic on September 1, 2006. Ms. Peg Divine, Deputy Manager of the Bureau of Engineering at DPW, states that because MEOC could not provide bridge operations training to DPW's bridge operators until after 60 days of completing construction, the Fourth Street Bridge re-opening was delayed until September 1, 2006.

As a result of construction delays, MEOC claimed that it incurred costs of \$21,470,436 in excess of the \$21,682,307 which was previously paid by DPW to MEOC under the construction agreement. In March and May of 2006, MEOC and DPW entered into two separate mediations to resolve MEOC's claims. According to Ms. Louise Simpson of the City Attorney's Office, MEOC's and DPW's attempts to mediate the dispute were unsuccessful.

Subsequently, on February 29, 2008, MEOC filed a lawsuit against the City in an amount not less than \$20,000,000, to recover its additional costs of \$21,470,436 that MEOC alleges it incurred and was not paid by the City, plus penalties and interest. Subsequently, the City Attorney's Office filed a cross-complaint against MEOC and Arch Insurance Company, MEOC's surety bond provider<sup>5</sup>, for breach of contract and the recovery of liquidated damages totaling \$14,115,000 because of the 555-day delay caused by MEOC in completing the Fourth Street Bridge Project.

After continued unsuccessful attempts to settle the City's and MEOC's claims, MEOC proceeded with its lawsuit against the City. As a result, Ms. Simpson states that the City Attorney and DPW are requesting \$2,809,000 of additional General Fund monies at this time in order to provide legal services to defend the City in this case.

On January 28, 2011, the Santa Clara Superior Court<sup>6</sup> cancelled the original trial date of May 31, 2011 and scheduled a trial setting conference on March 11, 2011 to set a new trial date. Ms. Simpson advises that while the trial may commence as early as June 2011 and end in August 2011, based on an anticipated trial length of 12 weeks, the trial is more likely to occur in the fall of 2011, during FY 2011-2012.

## DETAILS OF PROPOSED LEGISLATION

The proposed ordinance would appropriate \$2,809,000 from the City's General Fund Reserve to DPW for litigation expenses related to the Santa Clara Superior Court case, Mitchell Engineering/Obayashi Corporation v. City and County of San Francisco, pertaining to the Fourth Street Bridge Project. Of the total requested \$2,809,000 supplemental appropriation, (a) \$300,000 would pay for DPW's staff to assist the City Attorney's Office, including providing

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<sup>5</sup> Arch Insurance Company provided the City's required surety bonds for the Fourth Street Bridge Project. The surety bonds required Arch Insurance to guarantee completion of the Project and payment of the subcontractors and vendors, in the event that MEOC failed to complete the Project.

<sup>6</sup> Bay Area Reinforcing, Inc., MEOC's subcontractor, originally filed a lawsuit in the Superior Court of San Mateo County against MEOC because Obayashi Corporation, a joint venture partner, had its principal place of business in San Mateo County. MEOC then filed a cross-complaint against the City in San Mateo County. The City subsequently filed a cross-complaint against MEOC and Arch Insurance, and filed a motion to change the venue to a neutral location, which was granted, and the Superior Court of San Mateo County moved the trial to Santa Clara County.

information for (i) discovery responses, (ii) deposition preparation, and (iii) other trial preparation, and (b) the remaining \$2,509,000 would pay for a DPW work order with the City Attorney's Office for the City Attorney's costs, including (i) City Attorney staff, (ii) written discovery, (iii) document scanning, coding, and production, (iv) witness depositions, (v) trial motions, (vi) trial audio/visual preparation, (vii) travel costs, and (viii) trial (expected 12 week length).

According to Ms. Simpson, the City Attorney considers the detailed plans for the trial preparation and trial by the City Attorney's Office and DPW, and the related expenditures, to be privileged and confidential. As such, Ms. Simpson provided the Budget and Legislative Analyst, on a confidential basis, with a budget for the subject requested \$2,809,000 supplemental appropriation. Ms. Simpson advises that the City Attorney would also provide such budget details to the Budget and Finance Committee on a confidential basis, if the Budget and Finance Committee makes such a request.

In December of 2010, the Santa Clara Superior Court set an original trial date for May 31, 2011. The City Attorney and DPW began trial preparation for the case on approximately December 1, 2010, subsequent to continued unsuccessful attempts to settle the City's and MEOC's claims. Subsequently, MEOC proceeded with its lawsuit against the City. As a result, the City will expend an estimated \$319,740, or 11.4 percent of the requested \$2,809,000, including an estimated \$250,000 by the City Attorney's Office and an estimated \$69,740 by DPW, for the period retroactive to December 1, 2010 through March 8, 2011 for costs related to the litigation.

Therefore, the proposed supplemental appropriation ordinance should be amended to provide for retroactive authorization of expenditures.

## **FISCAL IMPACTS**

The proposed supplemental appropriation request of \$2,809,000 would be funded with monies from the City's \$25,000,000 General Fund Reserve. If the proposed \$2,809,000 supplemental appropriation request is approved, the City's \$25,000,000 General Fund Reserve would be reduced to \$22,191,000.

In response to inquiries by the Budget and Legislative Analyst regarding the use of alternative funding sources other than the General Fund Reserve for the subject supplemental appropriation, according to Ms. Divine, although Federal, State, and local sources funded the Fourth Street Bridge Project, such funds cannot be expended on the subject litigation expenses because (1) the use of the Federal and State funds is limited by Federal and State regulations and (2) the remaining local funds of an estimated \$85,000, all City General Fund monies, cannot be expended because the California State Department of Transportation (Caltrans) has not conducted its audit of the Fourth Street Bridge Project and may find some Project expenditures ineligible for Federal and State Highway funding. Furthermore, Ms. Monique Zmuda, Deputy City Controller, states that the City's FY 2010-2011 \$11,000,000 General Fund Litigation Reserve is not being proposed to fund the subject supplemental appropriation because the Litigation Reserve is generally used to pay for judgments, claims, and settlements. According to Mr. Leo Levenson, the Controller's Director of Budget, Analysis, and Reconciliation, as of the writing of this report, the Litigation Reserve has a FY 2010-2011 balance of \$2,800,000.

The Budget and Legislative Analyst notes that given that the anticipated trial is not scheduled to begin until June of 2011, and possibly later, a portion of the unexpended amount of \$2,489,260 (\$2,809,000 requested less \$319,740 to be expended through March 8, 2011) will likely be expended in FY 2011-2012. Mr. Levenson advises that any unexpended funds, as of June 30, 2011, from the requested \$2,809,000 supplemental appropriation would automatically carry-forward from FY 2010-2011 to FY 2011-2012. In the event that there are unexpended funds at the conclusion of litigation, Mr. Levenson states that such funds would be returned to the City's General Fund.

The City Attorney's Office and DPW also advise that, in addition to this subject request of \$2,809,000, an estimated additional \$1,236,991 in General Fund monies, including \$1,075,000 for the City Attorney's Office and \$161,991 for DPW, associated with the subject litigation, will be requested in the City's FY 2011-2012 annual budget.

According to Ms. Divine, pursuant to the grant agreements that the City has with the various Federal, State, and local entities that funded the Fourth Street Bridge Project, any monies that the City might recover from the subject litigation would be distributed to the various Federal, State, and local entities<sup>7</sup>, depending on the proportion of funding each source contributed to the Fourth Street Bridge Project. To the extent that monies are returned to the City, such monies could potentially reimburse the City's General Fund<sup>8</sup> up to the subject requested \$2,809,000. However, according to Ms. Simpson, the construction agreement between MEOC and DPW did not include a provision entitling the prevailing party, in a breach of contract dispute, to recover attorney's fees. Therefore, the City has no legal basis to seek recovery of its attorney's fees from MEOC in this case.

Ms. Simpson states that if the City reaches a settlement agreement or does not prevail in the subject litigation, the City will request funds from Caltrans, which administers Federal funds, up to a maximum of 80 percent, to pay any settlement or judgment amounts resulting from the subject litigation, with the remaining balance of at least 20 percent to be paid by the City, subject to appropriation approval by the Board of Supervisors.

## RECOMMENDATIONS

1. Amend the proposed ordinance to provide for retroactivity.
2. Approval of the proposed ordinance, as amended, is a policy decision for the Board of Supervisors.

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<sup>7</sup> Local funding sources for the Fourth Street Bridge Project included City General Funds, San Francisco County Transportation Authority ½ cent Sales Taxes, Earthquake Safety Bonds, and Street Improvement Bonds.

<sup>8</sup> An estimated \$3,636,750 of General Fund revenues were used to fund the Fourth Street Bridge Project.



Harvey M. Rose

cc: Supervisor Chu  
Supervisor Mirkarimi  
Supervisor Kim  
Supervisor Wiener  
President Chiu  
Supervisor Avalos  
Supervisor Campos  
Supervisor Cohen  
Supervisor Elsbernd  
Supervisor Farrell  
Supervisor Mar  
Clerk of the Board  
Cheryl Adams  
Controller  
Greg Wagner