

SDCTA Backgrounder on Lease-Leaseback Procurement Method and Recommended Best Practices

Procurement delivery methods can be complex agreements between government agencies and contractors tasked with building a specific project. While other methods have clear and concise requirements, the Lease-Leaseback Procurement method has flexibility allotted to school districts and contractors. This flexibility allows districts to select capable contractors on the basis of their demonstrated experience and qualifications, to experience construction cost savings, and to ensure timely completion of quality construction work. To promote fair and open competition, the San Diego County Taxpayers Association (SDCTA) wants to ensure school districts are transparent and operate under best practices as set forth below.

What is Lease-Leaseback?

A lease-leaseback (LLB) contract is authorized by Education Code §17406 et seq. The relationship and contract terms between the district and project contractor (contractor) are considerably different than with other project delivery methods. A general outline of the steps within the LLB process can found in the nearby figure. An April 2011 study by the San Diego Taxpayers Educational Foundation found that the use of LLB contracts has, “produced promising results for

school districts and can be advantageous when used in the appropriate circumstances.”

Lease-Leaseback Contract Terms

The relationship and contract terms between the district and contractor are considerably different than with other project delivery methods. After selecting a contractor, the school district negotiates two concurrent leases: a site lease (an agreement in which the school district leases a parcel of property which it owns so that the firm can construct, renovate, or modernize school facilities on the premises), and a facilities lease (an agreement in which the firm leases the newly constructed facilities back to the school district). The lease term can be no longer than 40 years, at which time the school district assumes ownership of the parcel and school facilities. The facilities lease sets the fixed price to be paid by the district for the completion of the project. It is through the lease payments of the facilities lease that the builder will be paid, similar to traditional “progress payments.”

The construction provisions, which in turn will reference the plans and specifications to be completed by the architect, with input by the builder on constructability or potential avenues for cost savings, will direct the contractor to construct the project pursuant to such plans and specifications. The construction provisions will also include legal requirements associated with public works projects,

Lease-Leaseback Steps



such as certain labor requirements, payment of prevailing wage, requirements regarding payment and performance bonds, as well as pertinent construction contract provisions such as indemnity and insurance language.

Lease-Leaseback Bidding Processes

While by law the selection of a project contractor under LLB need not follow a competitive bidding process, SDCTA requires the commitment of school districts to use an open and transparent competitive selection process to select a contractor. SDCTA has developed a series of transparency best practices to ensure all procurement policies undertaken by school districts are fair and transparent, and in the best interest of taxpayers.

Agreements pursuant to LLBs typically include a Guaranteed Maximum Price (GMP) provision. GMP limits the total sum of payments that a school district is obligated to make to a general contractor for the completion of a project. Aside from legally and/or contractually-mandated exceptions, the general contractor is generally liable for all project costs incurred beyond this price limit.

Recommended SDCTA LLB Process to be Adopted by School Districts

While SDCTA has adopted a set of best practices when districts pursue a LLB contract, SDCTA recommends substituting the adopted best practices document and asking each district to adopt a formal guiding process for LLB contracting that includes the following steps to be accomplished prior to the governing board approval of a LLB contract. SDCTA still contends that one particular delivery method should not be used for all projects, but rather, each delivery method, including LLB, should be considered to determine which method is best-suited to ensure a project's success. Toward this end, each district should adopt a policy by which project delivery methods should be evaluated and considered for each project.

Step 1

- Preparation of design and initial cost estimates for the project by district (can be through a program manager) and architect(s).

- Prepare and submit Request for Qualifications (RFQ) to prospective LLB contractors.
- Forming of Selection Panel and its Chairperson to review all LLB contractor proposals. Governing Board members should not participate on this panel. The Panel should include a member of the Bond Oversight Committee, when feasible.
- Review of RFQ submissions and shortening of LLB contractor list to a minimum of three qualified firms.

It is important a district begin the necessary planning for each project in which they intend to bid as a LLB project. Each district intending to use LLB **shall** use a competitive selection process to select the LLB contractor. Proper planning will allow the selection panel and district team that will oversee the project have a clear understanding of the details of the contract and have adopted proper and fair criteria to select a contractor. SDCTA recommends including within the criteria a review of a contractor's proposed general conditions, general requirements and allowances. Additionally (not in lieu of), districts should ask firms to consider submitting improvements that may be made to the approach and methodology of the project. Consideration may be given to firms that may not have direct LLB experience but have experience in school facility construction. The initial design and cost estimates developed by the district and its architect will serve a basis for determining final plans and cost estimates during the preconstruction phase.

Step 2

- Review and selection of project contractor by Selection Panel.
- Execution and board approval of a preconstruction services agreement with the selected contractor including requirement to perform, in conjunction with the project architect, constructability review, evaluate value engineering options, prepare preliminary cost estimates and project schedule and prepare subcontractor bid packages and outreach plan to ensure bidding by a minimum of 5 subcontractors for each trade, if feasible.

The review and scoring of qualifications proposals should follow the criteria previously agreed to ensure a fair and transparent process. The selected proposal will move forward to the governing board for final approval, with an executed contract to follow. Following the Selection Panel's recommendation, the District governing board should approve a pre-construction services contract with the contractor that includes a constructability review clause. This clause should include a requirement that, subject to the limitations of Public Contract Code section 1104, there shall be no adjustment to the Final GMP for errors and omissions made by the architect and its consultants, or any later discovered conditions related thereto, that could have or should have reasonably been identified by the contractor (in its capacity as a building contractor and not as an architect, engineer or other design professional) during the performance of the contractor's preconstruction scope of services. SDCTA recommends the contractor prepare subcontractor bid packages from a minimum of 5 subcontractors, if feasible, for each trade as a means to reduce costs to taxpayers.

Step 3

- Receipt of project approval by DSA.
- Receive and evaluate subcontractor bids by the contractor in an "open-book" process with the District at a District designated facility.
- District governing board adopts finalized GMP.
- Execution of LLB agreements.

Any addenda to the project and proposals should be submitted with eventual final DSA approval. Following the development of the GMP, the final GMP **shall** be approved by the district's governing board at an open meeting. At that time, any discrepancies between the proposed GMP and original estimates developed by the district and architect will be disclosed to the governing board. The selected contractor will deliver the project under the agreed upon GMP, and no additional dollars should be allocated to the project by the district, absent force majeure or other causes for which additional compensation is required by the contract or applicable law, including additional scope, unforeseen conditions, delay not caused by the contractor or errors or omissions in the project design.

Step 4

- Monitoring of project by bond oversight committee.
- All deductive change orders and material substitutions presented to bond oversight committee for review and governing board for approval.
- Final project budget vs. actual presented to bond oversight committee and governing board presented on regular basis.

Following the approval of the contract, the district's bond oversight committee and governing board should be notified of the progress of the project. This includes continuous review of actual expenditures vs. budgeted and the timeline to completion. Additionally, any deductive change orders and material substitutions instigated by the contractor should be presented to the bond oversight committee for review and approved by the governing board.