

PIEDMONT HILLS UNDERGROUND ASSESSMENT DISTRICT

DRAFT REPORT OF AUDIT SUB-COMMITTEE

BY: DEAN E. BARBIERI, MAYOR AND MEMBER OF PIEDMONT AUDIT SUB-COMMITTEE

INTRODUCTION:

The Audit Sub-Committee of the Piedmont Audit Committee (the "Sub-Committee") was formed specifically to investigate certain aspects of the Piedmont Hills Underground Assessment District (the "District") related to the construction problems encountered and resulting cost overruns which exceeded \$2 million. The Sub-Committee is comprised of the Mayor of Piedmont, Dean Barbieri, the Vice-Mayor of Piedmont, John Chiang, and a Piedmont resident and retired Alameda County Superior Court Judge, Ken Kawaichi.

The City of Piedmont has initiated litigation against various parties associated with the construction of the District, and that litigation is currently pending. As a result of that pending litigation, and under the advice and direction of Piedmont's legal counsel, the Sub-Committee has been restricted in discussing certain topics during the open meeting sessions already conducted, and is restricted in this and other reports from discussing those topics so as not to violate the applicable attorney client and attorney work product privileges. It is acknowledged that the City of Piedmont is aggressively pursuing the parties that it feels contributed to the construction problems associated with the District, and that the Sub-Committee must not take steps that would compromise the legal case of the City of Piedmont against those adverse parties.

To date, there have been four open meetings attended by all of the Sub-Committee members. Those four meetings occurred on March 31, 2010, May 13, 2010, July 8, 2010 and July 21, 2010. During each of those meetings there have also been a number of concerned citizens in attendance. Minutes of each of those meetings have been kept and published. Another meeting is scheduled for January 26, 2011. At the January 26, 2011 meeting the draft reports prepared and submitted by each of the three Sub-Committee members will be considered and a final, consolidated report will be produced taking into consideration all of the facts and findings of the three individual reports.

During the first meeting on March 31, 2010, the scope of work for the Sub-Committee's evaluation process was discussed and established (the "Scope of Work"). The proposed Scope of Work was based upon input received from the Mayor, Vice-Mayor and members of the general public. The Scope of Work is included in the minutes of the March 31, 2010 Sub-Committee meeting, and thus it is not necessary to include in this report. At the public meetings of the Sub-Committee it was discussed and decided that the most efficient means of conducting the investigatory work of the Sub-Committee was to assign different aspects of the Scope of Work individually to the members of the Sub-Committee who could then investigate those specific matters in greater detail, and report to the entire Sub-Committee during the

public meetings. Given the limitations of the Brown Act it was recognized that the Sub-Committee could not maintain discussions except during the public meetings.

The specific areas of the Scope of Work assigned to Mayor Barbieri were items identified as follows:

1. b. Review of existing City Council policy for underground utility assessment districts (20B) and investigate the role of Piedmont staff.

1. g. Review of existing City Council policy for underground utility assessment districts (20B) and investigate the past experience with undergrounding projects.

2. d. Application of City policy to the Piedmont Hills Underground Assessment District and investigate the timeline for seeking legal counsel (notification of the City Council and notification of the public).

REVIEW OF EXISTING CITY COUNCIL POLICY FOR UNDERGROUND UTILITY ASSESSMENT DISTRICTS (20B) AND INVESTIGATE ROLE OF PIEDMONT STAFF and PAST EXPERIENCE WITH UNDERGROUNDING PROJECTS:

The Scope of Work outline sets forth two separate items, 1. b. and 1. g. relating to the “role of Piedmont staff” and the “past experience with undergrounding projects”, respectively. As these two topics are interconnected they have been combined for discussion herein.

The roles of City staff in 20B underground utility assessment districts have varied from district to district, starting with the Dudley Blair district. In the Dudley Blair district, the roles of City staff were overall far less than the roles of City staff in the Wildwood Crocker, Central Piedmont, Hampton Sea View and Piedmont Hills districts. Districts and projects before the Dudley Blair district, including King Avenue and Richardson Way, were not reviewed.

In the Dudley Blair district the entire project was organized as if it were a private project. The City staff only got involved after the district progressed toward the final legally required approval process. This included consultation with outside bond counsel, Sam Sperry, and preparation of the necessary resolutions and contracts. The residents of the district, and in particular the main proponent of the district, Mr. Mason Willrich, oversaw the formation of the district and fundraising. The City staff oversaw the construction of the project. The Director of Public Works, Larry Rosenberg, was in charge of the construction. Except for regular and usual City business related to all construction projects, and the administration/disbursement of bond proceeds, very little specific work was performed on this district by any other City staff including City Administrator Geoff Grote, City Clerk Ann Swift, Finance Director Mark Bischel, City Attorney George Payton, or any other senior level or mid level management personnel of the City.

The past experience with this district was good. The construction was completed without encountering any significant geologically related financial issues. Some significant

construction issues did arise, and it was necessary that private funds be raised and deposited with the City as a contingency. In particular, the light poles needed replacement as they were not correctly specified. Otherwise this was a very successful undergrounding district. No City general funds were used.

In the Wildwood Crocker district the City staff role developed as the district developed. The role of the City Clerk, Ann Swift, increased as the district evolved. City Council resolutions were passed through the process and those resolutions set forth the different aspects of the district which would be the responsibility of the City Clerk and other City staff. Once formed, the oversight of the construction phase was the responsibility of the Director of Public Works. The Finance Director had little day to day involvement. The City Administrator supervised the senior management but had little day to day involvement with the project, and the City Attorney reviewed the legal process and documentation and worked with bond counsel throughout the period.

As with the Dudley Blair district, the experience with the Wildwood Crocker district was very good. The construction was completed timely and within budget. Although some rock was encountered during the trenching phase, the contingency funds were more than sufficient to cover those extra expenses, and no Piedmont general funds were used for this project except for those that related to City owned land within the district.

In the Central Piedmont district, at City Council direction the City staff became even more involved as a result of many factors including, but not limited to, the size of the district and the number of households involved, the rising costs of construction, the need for multiple ballots and the divided resident support for this district as compared to either the Dudley Blair or Wildwood Crocker districts. The role and workload of the City Clerk on this district increased due to the fact that there was a resident vote to approve the district before an actual construction bid was obtained. The vote was based upon a cost estimate rather than an actual bid. Given the construction industry bidding climate at the time, by the time the first vote approving the district occurred and the project was sent out for an actual bid, the construction costs for the district increased dramatically over the projected estimate resulting in a need to conduct a second vote by the residents. Given the large difference in construction costs between the estimate and the actual bid, the second vote resulted in far less resident support for the district, and the City Council voted not to approve the district. No construction ever occurred within this district and no City general funds were expended on construction within this district.

In the Piedmont Hills district, the City staff and the residents of the district learned from the experiences of the Central Piedmont district, and did not vote on the project until actual construction bids were obtained. As had been the case with previous districts, the City Clerk worked with the steering committee and other residents within the district to assist them in the early stages of formation and throughout the balloting process. The main difference which occurred with the Piedmont Hills district as compared with the prior districts was the City Clerk's level of interaction during the bidding and construction phase of this district. In the prior district's above described, the construction phase was handled almost exclusively by the

Director of Public Works, and others in his department. In the Piedmont Hills district, more direct contact occurred between the City Clerk and the construction entities, including the engineers and contractors, and there was more of a blurring of lines between the roles of the Director of Public Works and the City Clerk until January 2010. In January 2010 the City Administrator assigned responsibility for the construction aspects of the district to Chester Nakahara, and assigned responsibility for the financial aspects of the district to Mark Bischel.

The experience with the Piedmont Hills district is well documented, and will certainly be the subject of further and more detailed description in the reports of my other Sub-Committee members. In essence, the district encountered significant cost overruns due to certain factors which are the subject of the above described litigation. The two primary causes of those cost overruns are the costs associated with the substantial rock discovery which resulted in greater time, energy and expense being expended during the trenching phase. Another cause of the cost overrun was the linear feet miscalculations which were present in the bid documents prepared by the engineers hired to prepare the specifications. Those significant miscalculations resulted in the construction bid being much below what it otherwise would have been had the contractor been bidding on correct calculations. It was not until well into the completion of the project that the contractor and the City realized that the engineer specifications were wrong and that the linear foot specifications needed to be re-calculated.

To avoid similar problems for any future City significant construction projects, the roles of the City staff must be certain and established at the outset of such projects. The responsibilities for the financial, administrative and supervisory aspects of the project must be known and accepted by all of the staff involved. The responsibilities must be assigned based on knowledge and time availability. If necessary and appropriate a dedicated project manager should be named to oversee any such project, and in particular all of the technical construction phases. If necessary, the City should hire such a dedicated project manager as opposed to just using City staff. The financial oversight must be accurate and reviewed daily if necessary, and the City Administrator and City Council must be informed immediately of any unexpected significant circumstance which could impact the City and its resources. Equally important an experienced project manager must have experience in the type of project undertaken to assess the implications of issues that are identified at early stages.

APPLICATION OF CITY POLICY TO THE PIEDMONT HILLS UNDERGROUND ASSESSMENT DISTRICT AND INVESTIGATE THE TIMELINE FOR SEEKING LEGAL COUNSEL (NOTIFICATION OF THE CITY COUNCIL AND NOTIFICATION OF THE PUBLIC):

Once it became apparent that there were significant problems with the Piedmont Hills district, and that there was potential for legal causes of action and liability by and among different parties, the City Administrator Geoff Grote notified Mayor Abe Friedman in October 2009. The City Administrator then immediately contacted the law firm of Lombardi, Loper & Conant to discuss all aspects of the matter relating to the engineering and construction phase of the district. Of course, given the pending litigation and the need to preserve the attorney client

and attorney work product privileges, the specifics of those discussions cannot be detailed in this report.

Following the initial consultation with Lombardi, Loper & Conant, the City Council was briefed during the closed session portion of the first meeting in November 2009, on November 2, 2009. A representative of Lombardi, Loper & Conant was present and discussed the potential rights, liabilities and remedies facing the City. Lombardi, Loper & Conant has been representing the City on all aspects of this legal matter since, and litigation has been initiated. By contract, a mediation had to be conducted to attempt a resolution of the matter without further litigation and to date one mediation session has occurred and another mediation session is planned.

In addition to the consultation and advice being provided by the litigation counsel, Lombardi, Loper & Conant, regarding the matters associated with the engineering and construction aspects of the district, the City also consulted with Sam Sperry, the City's bond counsel for the district. Mr. Sperry appeared before the City Council in closed session on November 16, 2009 to discuss the options the City had with regard to completion of the construction project, including whether to continue or terminate the daily construction. Included in Mr. Sperry's discussion were impacts on the bond obligations facing the City, continuing liability under the contracts entered into by the City with the contractors among others, and the potential liability related to unfinished trenches throughout the district.

In conclusion, City Administrator Grote followed City policy and procedures and sought the advice of legal counsel as soon as it became evident that there was a need for legal representation for the City both on the litigation aspects of the matter, as well as on the potential obligations under the bonds that were issued in connection with the district.