



OFFICE OF THE PRESIDENT

Robert C. Dynes
President

1111 Franklin Street
Oakland, California 94607-5200
Phone: (510) 987-9074
Fax: (510) 987-9086
<http://www.ucop.edu>

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MEMBERS OF THE REGENTS' COMMITTEE ON GROUNDS AND BUILDINGS

Enclosed for your information is the Major Capital Projects Implementation Report for fiscal year 2004-05. This report describes the aggregate status of major capital projects underway at the end of the 2004-05 fiscal year and summarizes management initiatives and market conditions affecting project implementation.

If you have any questions about the report, please get in touch with Senior Vice President Mullinix.

Sincerely,

A handwritten signature in cursive script that reads "Bob".

Robert C. Dynes

Enclosure

cc: All Regents
Chancellors

TO MEMBERS OF THE COMMITTEE ON GROUNDS AND BUILDINGS:

INFORMATION ITEM

MAJOR CAPITAL PROJECTS IMPLEMENTATION REPORT, 2004-05 FISCAL YEAR

EXECUTIVE SUMMARY

The dollar value of active University projects in 2004-05 was approximately the same as the previous year with a net increase of \$104 million for a total capital program of approximately \$8 billion. The percentage of projects with schedule changes decreased from 53.3 in 2003-04 percent to 47.7 percent in 2004-05. The percentage of net budget augmentations increased from 2.9 percent in 2003-04 to 4.1 percent this past year.

During fiscal year 2004-05, the University continued to experience a significant increase in construction inflation initiated by the rapid cost escalation of key building materials which began in 2003-04. This inflationary cycle was intensified by strong competition from foreign markets for building materials, a dramatic increase in energy costs, a record high volume in the construction market, and recently, by the damage and destruction caused by the hurricanes in the Gulf Coast. The known and unknown cost implications of these influences, coupled with the very tight labor market and reduced competition among contractors and subcontractors, have led to a high volatility in construction bids during the past year and at the time of this report is expected to continue in 2005-06.

Campus financial and staff resources continue to be challenged by the scale and complexity of a capital program that has increased from \$1.9 billion in 1996-97 to \$8 billion in 2004-05. Meeting this challenge requires continuous development of the University's project management capability to effectively manage complex University projects in this challenging market environment.

Introduction

The Major Capital Projects Implementation Report, first presented in 1991, measures project delivery performance and identifies trends. This Report describes the aggregate status of major capital projects underway at the end of fiscal year 2004-05 and summarizes management initiatives and market conditions affecting project implementation.

The University's ability to successfully implement its capital program depends on many factors. Factors within University control include project management and delivery strategies, academic program changes, and budgeting/funding strategies. Factors beyond University control include the construction industry bid climate and market conditions, code changes, requirements of State and other funding sources, and weather delays.

It is important to note that some project budget and schedule changes are driven by circumstances intentional, necessary, and beneficial to the University's interests (for example, program changes, the logistics of multiple project phasing, and incorporation of new funding

opportunities). Because this mix of factors affects project delivery, simple indicators do not fully represent the complexity of factors affecting University capital project implementation. Nonetheless, to assess the general condition of the program, to identify trends, and to develop initiatives to improve project delivery, two indicators are monitored in this annual report: 1) project budget changes and 2) project schedule changes.

Status of the Capital Program

Major University capital project activity for fiscal year 2004-05 is shown in the summary table that follows. The compilation deals only with major capital projects, those with a project cost of over \$400,000. All figures referring to either budget or schedule changes represent the cumulative change over a project's duration (normally averaging four years).

**Summary of Major Capital Project Activity at Fiscal Year End
2004-2005**

1. Total active projects.....	344
2. Total amount of original budgets.....	\$7,659,516,000
3. Cumulative approved budget changes (adj for inflation for 2004-05).....	\$313,817,000
4. Total year-end budget, (adj. for inflation).....	\$7,973,333,000
5. Percent Change from Original Budget.....	4.1%
6. Total year-end budget (including inflation).....	\$7,979,159,000
7. Projects with budget changes.....	101
8. Projects with schedule changes.....	164

Table 1 following this item provides campus-level detail for the above categories. Attached Figures 1, 2 and 3 display trends for the year-end budget totals, and for the number of active projects for each fiscal year; the percent change in project budgets (net changes divided by total amount of original budgets); and the percentage of projects with schedule changes.

From fiscal year 2003-04 to fiscal year 2004-05, the net number of active projects decreased, by 3, from 347 to 344. During fiscal year 2004-05, 112 projects with budgets totaling \$866 million filed Notices of Completion. With the addition of new projects and augmentations to previously approved projects, the total value of projects in design and construction (approved budgets) increased by a net of \$104 million, from \$7.869 billion to \$7.973 billion (Figure 1). Projects related to enrollment growth, including housing, continue to be the majority of projects in the program. Seismic improvements and renovation projects continue to represent a substantial component of the State funded capital program. In addition, replacement hospitals and seismic improvements to existing medical center buildings that are needed to meet statutory deadlines under SB 1953 represent a significant component of the non-State funded capital program.

The fourteen-year trend in the percentage of net project budget augmentations shows an overall reduction from a high of 6.0 percent in fiscal year 1990-91 to 4.1 percent in fiscal year 2004-05 (Figure 2). From fiscal year 2003-04 to fiscal year 2004-05 the percentage of net project budget augmentations increased from 2.9 percent to 4.1 percent. The percentage of projects with schedule changes decreased from 53.3 percent to 47.7 percent between 2003-04 and 2004-05 (Figure 3).

Conditions in the Construction Market place

As discussed at the January 2005 Regents meeting, the volatile conditions in the construction

marketplace continue to be an important factor that impacted University projects since early 2004, and is a trend that is anticipated to continue at least through the remainder of this fiscal year.

From 2002 through 2003 the economy was rebounding from a short recession and construction material costs as a whole were quite flat, with few materials making any pricing gains, and the cost of many materials actually falling. During this period both the public sector and housing construction markets were strong, but the commercial construction markets were weak. Contractor margins were very low during this period.

At the end of 2003, significant events occurred simultaneously that had a substantial cumulative impact on the construction industry. Volume in the commercial construction market sector finally rebounded, which initiated an increase to contractor margins from previously depressed levels. Lumber prices continued to go up and global demand in the steel market created a shortage in “scrap” metal (a component in the manufacturing of structural steel), resulting in a shortage of structural steel and a significant increase in pricing. Shortages in cement were seen in the market place, resulting in further price increases in that commodity.

The year 2004 started with an annual construction inflation rate of approximately 3 percent. This rate quickly changed during the course of the year, peaking in the third quarter of 2004 to a rate of approximately 10 percent. This significant increase was due in part to a shortage of skilled labor, the overall construction volume, and significant material price increases resulting from a variety of market conditions, including a changing global construction market. During 2004 the construction industry effectively shifted from a “buyers” (owner’s) market, to a “sellers” (contractor’s) market. By late 2004, it was anticipated that the annual rate of inflation during 2005 would fall back to a level around 3.5 percent. This forecast was attributed to: 1) high construction activity in the following sectors: multifamily housing, office, hotels, manufacturing, education, and healthcare; 2) anticipated softening of prices of several construction materials that had increased significantly during 2004; and 3) the prediction that construction spending in 2005 would increase by 2 percent. Recent reports now estimate construction inflation in 2005 at 8 percent nationally and 10 percent in the West. The California Construction Cost Index (CCCI) increase for calendar year 2005 was 6.4 percent.

Even though the year 2005 started out with encouraging signs that the construction material market was finally stabilizing (oil prices had seemed to peak and steel prices had started to fall), as the year progressed the construction economy once again became very uncertain. Oil prices rebounded higher, construction volume continued to climb to all time highs, and some construction material prices started rising again. Then in the late summer and early fall of 2005 fear and uncertainty re-entered the construction economy with the destruction caused by the hurricanes which hit the Gulf Coast.

Expert opinion has varied widely on what the exact impact will be to the national construction economy due to hurricane Katrina (and several other major hurricanes). Many experts feel that the effect of these events will be softened by the fact that the required massive rebuilding effort in the impacted areas will likely occur over an extended period of time. Two key construction materials, cement and lumber, experienced price increases resulting from demand generated by these events and from the demand already existing from the record high volume of the national

construction economy. Some experts voiced confidence that these specific material price increases could be alleviated or kept in check through government actions reducing existing tariffs on foreign products from Mexico (cement) and Canada (lumber), allowing more supply of these materials into the U.S. market.

The market instability has led to higher incidence of University's capital projects bidding higher than originally budgeted. Many projects going to bid in fiscal year 2004-05 were budgeted a year or more before the construction market began its upward trend and before rapidly increasing volume and natural disasters had destabilized the construction market. In fiscal year 2004-05, 72 percent of projects with budgets greater than \$5 million bid over their original budgets; the aggregate overage was 20.0 percent greater than the budgeted total. In comparison, the aggregate overage in fiscal year 2003-04 was approximately 5.0 percent; and in fiscal year 2002-03, bids were slightly less than budgeted.

The exact impact of the Gulf Coast hurricanes will not begin to be known until about the middle of 2006 and until then this uncertainty will add to the volatility of the construction market. The residential market may slow somewhat nationwide, but any market savings here will probably be taken up in increased housing construction on the Gulf Coast. Construction cost inflation estimates by experts fluctuate widely (between 5.0 and 20.0 percent annually for the first two quarters of 2006) with consensus that inflation should stabilize in the range of 5 percent to 7 percent by the fourth quarter. Finally, the construction volume will continue at record levels (going on six years) which will continue to put pressure on the shortage of skilled labor and drive up labor cost. The continued high volume of construction and resulting lack of contractor competition means that the bidding for UC projects remains extraordinarily volatile and unpredictable.

Initiatives Related to Cost Management and Project Delivery

As the University works to continue providing the capital assets necessary for continued enrollment increases within this difficult construction market, it is pursuing several cost management and project delivery initiatives.

During the past year the Board of Regents, through its Committee on Grounds and Buildings, commenced an investigation of current practices and policies to determine more effective approaches for designing and constructing projects. To conduct the investigation, a committee of six outside experts was commissioned and it identified six primary areas of change in a report entitled, "Transforming Capital Asset Utilization and Delivery". At this time these suggestions are in the process of being implemented by the University with implementation anticipated by the latter part of 2006.

Meanwhile, the University is working to implement immediate system wide and project-specific responses to current market volatility. These include such project-specific measures as establishing a Capital Bid Response Team, modifying the bid process to make it more attractive to the construction community, simplifying designs and utilizing cost benchmarking, and "add" alternates for projects early in design. Measures such as these will address University projects at various stages of implementation from projects currently out to bid, to projects currently in design, to projects now being budgeted.

The Regents Committee on Grounds and Buildings continues to focus its attention on long-term planning, urban design, and development issues. During fiscal year 2004-05, the Long Range Development Plans for two campuses were approved and three campuses made presentations on their urban design vision.

The Regents' policy on sustainability is now applicable to all new University building projects. Campuses have submitted and have had approved Green Building Baselines and are now incorporating sustainability design techniques into all building projects to make sure they meet UC sustainability standards.

The University of California at Merced campus is now open and construction continues on the campus to help meet the University's continuing enrollment expansion.

In addition, during 2004-2005 the University:

- Continued to address a shortage of student housing through expansion of housing bed count, adding approximately 1,300 beds and bedrooms by fall 2005.
- Continued to support the development of campus project management capabilities by expanding the range, scope, and frequency of training programs and courses for campus personnel through the UC Project Management Institute, which served 476 UC and CSU attendees with 18 programs (with repeat offerings at different locations in California). The range of topics has been expanded to include specialty forums on current challenges (campus building official responsibilities, market cost overruns and proposed contractor rating systems) and training for project managers on energy efficiency and sustainable building designs.
- Expanded the use of alternative project delivery methods such as Construction Management at Risk and Design/Build during FY 2004-05.
- Sought legislative initiative to modify the Stull Act to allow "best value" selection for all project delivery methods.
- Continued to review contract documents with regard to risk allocation.
- Reviewed administrative processes on campuses with the objective of improving contractor relations.

Attachments

Table 1

Figures 1, 2, 3

Table 1

Attachment

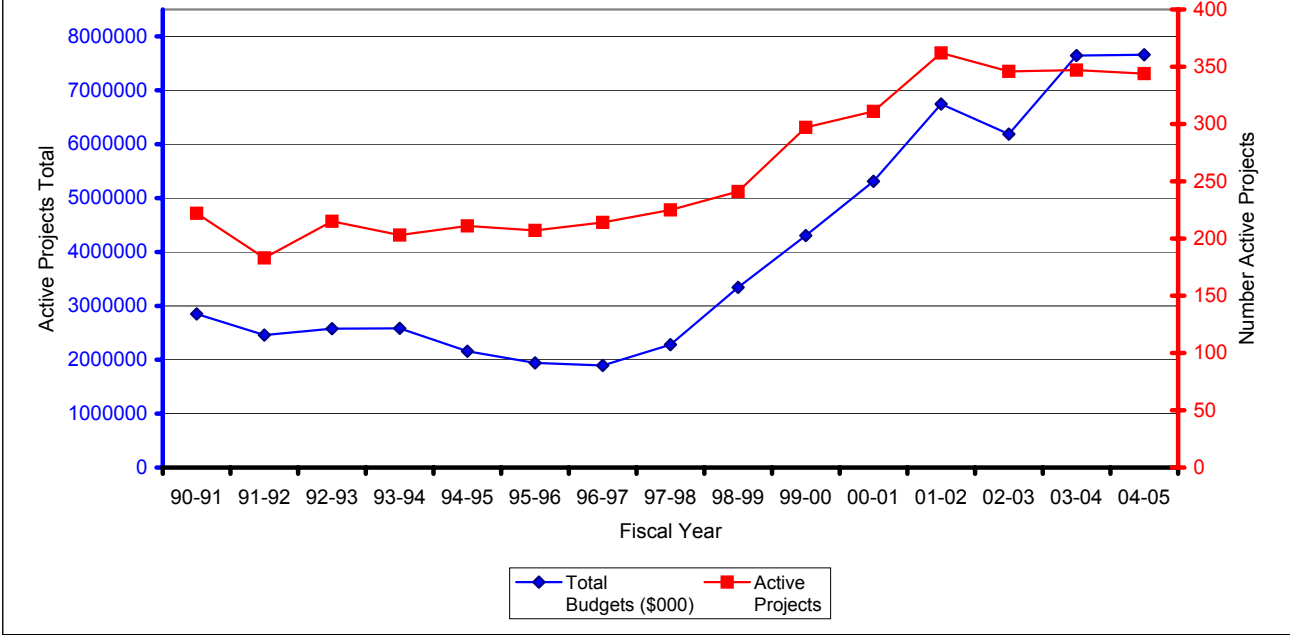
UNIVERSITY OF CALIFORNIA
MAJOR CAPITAL PROJECT SUMMARY
2004-05

CUMULATIVE CHANGES TO BUDGET AND SCHEDULE SINCE PROJECT APPROVAL BY REGENTS

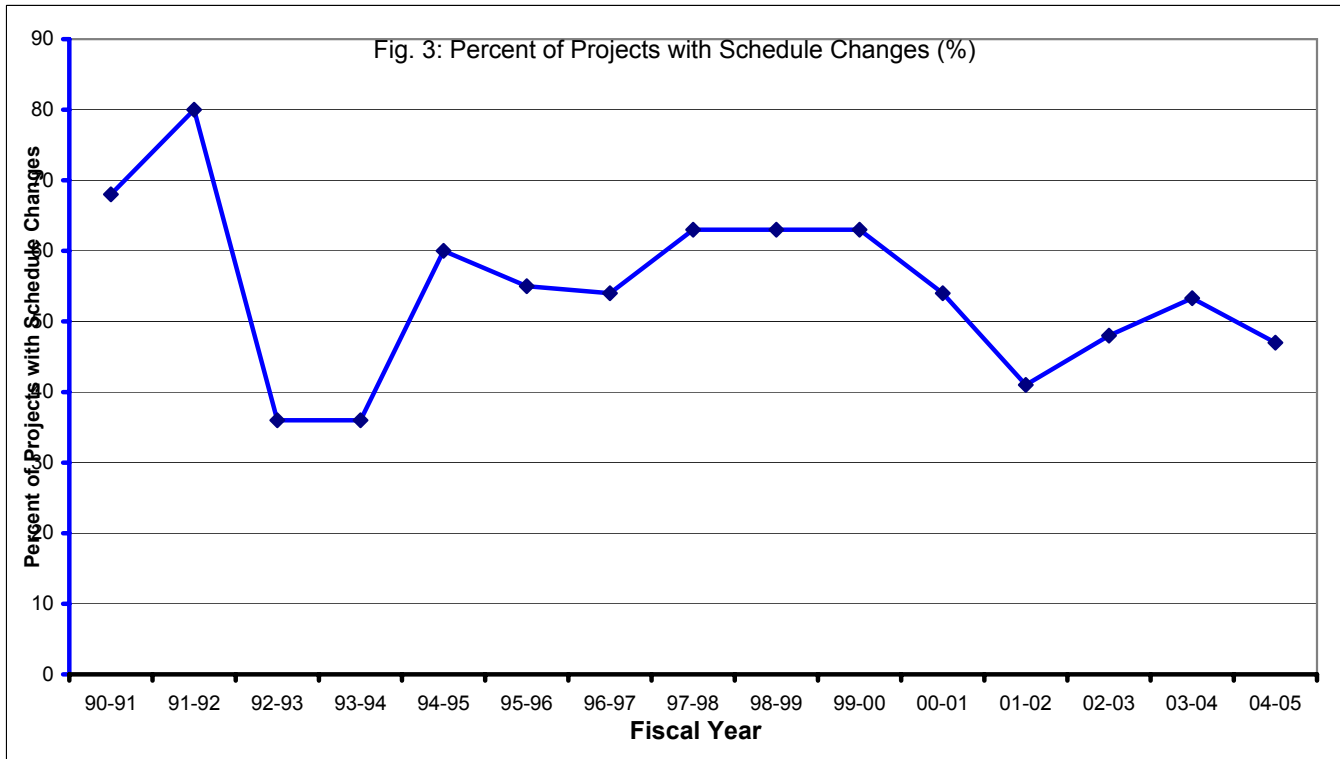
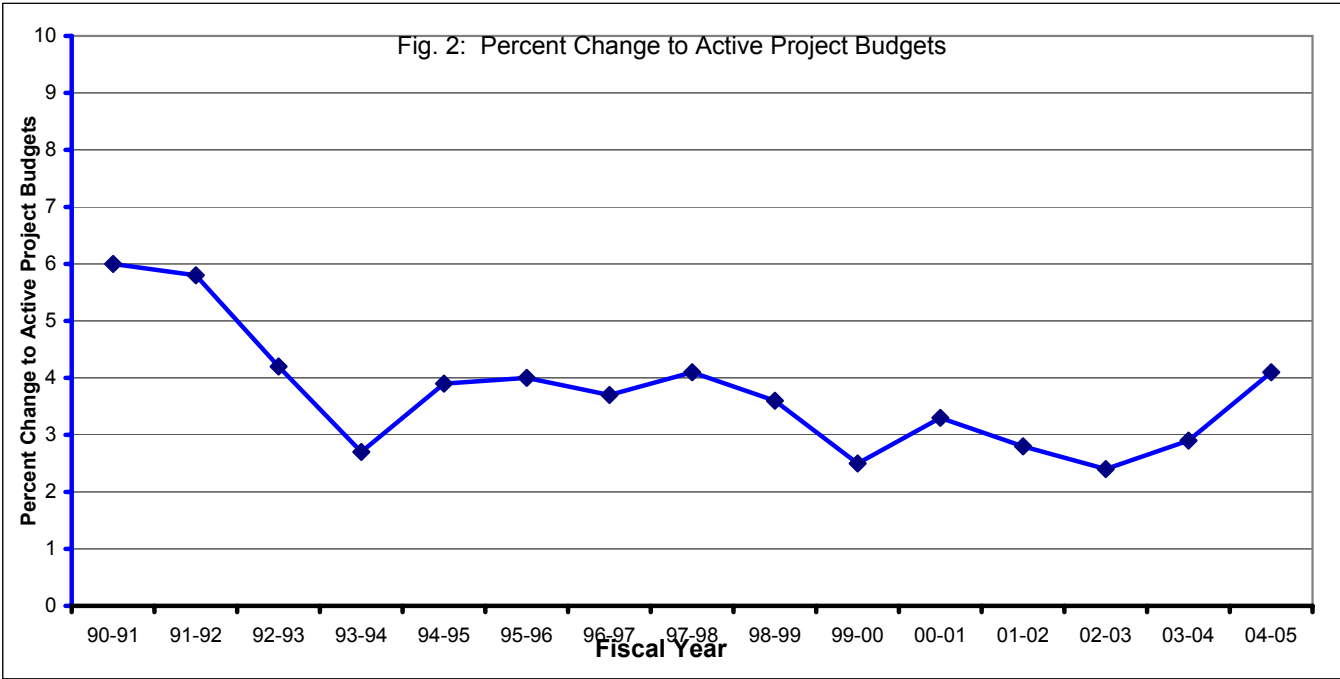
	1	2	3	4	5	6	7	8	9
	Active Projects	Original Budget (\$000's)	Budget at End of 04-05 (\$000's)	Inflation Adjusted Budget 04-05 (\$000's)	Total # with Budget Changes	Changes to Original Budget (\$000's)	% Change from Original Budget	# with Schedule Changes	% with Schedule Change
BERKELEY	43	724,550	738,047	737,444	8	12,894	1.8%	18	41.9%
DAVIS	47	980,312	1,003,378	1,000,140	14	19,828	2.0%	20	42.6%
IRVINE	18	853,488	938,865	938,865	7	85,377	10.0%	6	33.3%
LOS ANGELES	53	2,161,144	2,244,049	2,243,622	27	82,478	3.8%	35	66.0%
MERCED	11	308,402	314,777	314,777	5	6,375	2.1%	8	72.7%
RIVERSIDE	13	301,216	302,184	302,184	1	968	0.3%	4	30.8%
SAN DIEGO	59	804,768	846,586	845,028	15	40,260	5.0%	26	44.1%
SAN FRANCISCO	47	753,191	768,226	768,226	11	15,035	2.0%	25	53.2%
SANTA BARBARA	29	517,361	558,447	558,447	7	41,086	7.9%	14	48.3%
SANTA CRUZ	23	254,321	263,837	263,837	6	9,516	3.7%	8	34.8%
DANR	1	763	763	763	0	0	0.0%	0	0.0%
OP	0	0	0	0	0	0	0.0%	0	0.0%
	344	7,659,516	7,979,159	7,973,333	101	313,817	4.1%	164	47.7%
			<i>Inflation Adjustments:</i>	<i>5,826</i>					
<u>BUDGET CHANGES</u>									
Reduced					21	(74,469)			
Increased					80	388,286			
<u>SCHEDULE</u>									
On schedule								180	
Schedule Changed								164	
STATE	84	3,830,511	3,980,260	3,974,434					
NON-STATE	260	3,829,005	3,998,899	3,998,899					
TOTALS	344	7,659,516	7,979,159	7,973,333	101	313,817	4.1%	164	47.7%

- (1) Active Projects: Projects with budgets exceeding \$400,000 on which funds were expended in 2004-2005 and had not been completed by June 30, 2005.
- (2) Original Budget: The sum of the original budgets for the active projects approved by The Regents.
- (3) Budget at End of 2004-2005: The sum of the project budgets at year end. This figure includes all increases and decreases made to the original budget since its approval.
- (4) Budget with inflation removed for state funded projects. *Value of inflation adjustments shown in italics.*
- (5) Total # with Budget Changes: How many of the active projects have had budget changes (increases or decreases) over the life of the project to date?
- (6) Changes to Original Budget: This is a net dollar amount of augmentations and decreases. State funded project budgets are adjusted to the original cost index for the project so that inflationary changes are not reflected as budget augmentations.
- (7) % Change Original Budget: The budget changes represent what percent change from the original budget, due to revised program scope or market conditions?
- (8) # with Schedule Changes: How many projects have had changes in their schedule since original approval?
- (9) % with Schedule Changes: The number of projects with schedule changes represents what percentage of the total campus projects?

Fig. 1: Total Budget and Number of Projects



Projects: All active projects with budgets exceeding \$400,000 for which funds were expended in 2004-05 and had not been completed (no Notice Of Completion filed) by June 30, 2005.
 Dollars: This is the sum of all project budgets at end of 2004-05. The figure includes all increases and decreases adjusted to remove inflation made to the original budget since its initial approval.



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