DRAFT
FINANCE AND AUDIT SUBCOMMITTEE MEETING MINUTES
February 16, 2016

Sacramento County Board of Supervisors
700 H Street
Hearing Room 1
Sacramento, CA 95814

The Finance and Audit Subcommittee of the California High-Speed Rail Authority (Authority) Board met on February 16, 2016 at 8:30am.

Committee Board Members Present:
  Mr. Tom Richards

Committee Board Members on Conference Call:
  Mr. Michael Rossi, Chair lead

Board Members Present:
  Ms. Lynn Schenk
  Ms. Bonnie Lowenthal

Authority Staff Present:
  Mr. Jeff Morales, CEO
  Mr. Tom Fellenz, Chief Counsel
  Mr. Russell Fong, CFO
  Mr. Jon Tapping, Director of Risk Management and Project Controls
  Mr. Scott Jarvis, Chief Engineer
  Ms. Paula Rivera, Chief Auditor
  Mr. Alan Glen, Director of Real Property
  Mr. Mark McLoughlin, Director of Environmental Services
  Mr. Paul Engstrom, Third Party Manager

Rail Delivery Partner Staff Present:
  Mr. Gary Griggs, Program Director

Minutes prepared in the order items were presented during the meeting

Agenda Item – January 2016 Meeting Minutes

- Mr. Rossi asked about page 2 under the Capital Outlay Report, "what the procedure is, how it happens without it coming here, and what's the process before it gets here" regarding going over budget. Mr.

Fong replied that the over spend in the budget occurred in 2014. At that point in time we were managing the budget at a higher level. Now that we have broken the budget down to environmental sections we do have processes in place over the last year or two to ensure that if there are any budget changes it will be notified and flagged earlier. We have the change control process for approval and would bring items to the Finance and Audit Committee if we have a budget change. The processes are in place to ensure that we will not over spend our budget without proper approval. Mr. Rossi asked about page 2 under the Contracts and Expenditures Report, regarding when a contract is dead. Mr. Fong replied that he and Mr. Richards spoke regarding a couple of questions. All of the active contracts are included in the budget and appear on this report. We do manage our cash flow. We have a 36 month look ahead report that helps us manage our cash. There's a question on contract expenditures and what's the assumption. Actual expenditures reflect approved invoices received and paid. Forecast expenditures are updated by the contract manager. Those are the two differences between the two columns. For the question why do we keep contracts active when the forecast and expenditures are equal. A vast majority of the High-Speed Rail contracts are not to exceed the ceiling of each contract. When you see a forecast equaling expenditures it means the contract manager doesn't have expenditures but they do want to keep the contract open. It is a lengthy process to reprocure contracts and some of these are being amended, which takes approximately 3 or 4 months. It's a combination of the two so we do not necessarily close a contract if we anticipate there could be future needs for a particular task. Mr. Rossi asked if the contract goes on perpetuity. Mr. Fong replied that each contract does have an expiration date. If you see on a report the forecast equal the actual expenditure, the contract manager wants to keep the contract active based on future needs for that particular task or it is going through an amendment. Mr. Richards commented that now on the contract expenditures provided we show a start and an end date. Mr. Fong responded correct. Mr. Rossi asked about page 3 under the Operations Report, "The information hasn't flowed quite to the extent we would like it to" regarding to getting the second tier priority parcels from the design builder. Mr. Jarvis replied that the communication from the design build teams and the Authority's ROW team is improving. Mr. Jarvis stated that the design-build and ROW teams are putting together longer range ROW acquisition plans. Mr. Rossi asked about page 4 with third parties being in a separate budget. Have we now consolidated all the budgets for the construction pages so we are now looking at one budget? Mr. Jarvis replied yes. We are in the process for CP1 of transferring those funds into the CP1 project account. CP2-3 and CP4 and beyond all of the funds dealing with construction and provisional sums related to utilities are part of that overall contract budget.

Agenda Item – Action Items from Previous Finance and Audit Committee Meeting

- None.

Agenda Item - Financial Reports – Russell Fong

Questions asked and answered. Issues discussed included:

- **Executive Summary Report –** Mr. Rossi asked on page 4 of the Executive Summary "the January-2016 Cap and Trade cash balance was $330M" and page 54 of the Operations Report where it talks that we have spent all of the Cap and Trade. Mr. Fong responded that page 54 only displays the first construction site whereas the Cash Management Report reflects all of the cash. Mr. Rossi asked on page 4 why "Tapered Federal Funds increased from $552M for January-2016 to $582M for February-2016" is an issue. Mr. Fong responded that it is not an issue. It is a display of how much in federal funds and how much in state funds is liable to match. Mr. Rossi responded that is not an issue. The issue is whether we will be able to meet the ARRA spend date of June 2017. Mr. Fong responded that is correct and we may want to rethink the title "issue". Mr. Rossi asked on page 5 "Financial System update (currently on hold)" why is that and don't we need that system. Mr. Fong replied as reported in previous Finance and Audit Committee meetings we are still working on our FI$CAL system which is the state's budget and accounting system. We need to figure out what that system will do for us before we do our gap analysis on what the High-Speed Rail needs versus what FI$CAL can actually deliver. We anticipate it is going to be a few more months before FI$CAL is functioning for the High-Speed Rail. Mr. Richards asked for an explanation on what the Authority and the RDP is contemplating with regards to the implementation of the financial system. Mr. Fong replied that we are working closely with the RDP and we do understand there is an immediate need to display our budget and accounting using a financial system versus the current manual system. We are trying to do two things at the same time, finish FI$CAL and be prepared to implement a new financial system once FI$CAL is running.

- **Summary of YTD Budget & Expenditures –** Mr. Rossi asked if we are going to be under budget for expenditures or is it a timing issue. Mr. Fong replied at this point it is hard to tell being at the 50% mark. We are under budget and at the pace we will be below budget at the end of the year. With only 50% of the year complete, things can change. Historically expenditures do ramp up in the fourth quarter. Mr. Richards asked if historically we have been under budget. Mr. Fong replied that is correct. **Operations Report –** Mr. Rossi asked on page 3 the third bullet point the re-baselining plan. Mr. Glen responded that we have reported at the last several Finance and Audit Committee meetings that we are anticipating a full re-baselining of CP2-3. In recent discussions with the construction oversight manager there are approximately 80 parcels that actually have changed ROW from the total 542 parcels. We are going to be going through a re-baselining for those 80 parcels. Once they finalize the ROW requirements and complete the environmental documentation that is required by the contract, we will then set the new delivery dates for those parcels. Mr. Rossi asked on page 9 page if we are going to change where it shows actual and planned as the same. Mr. Glen responded that the actual and planned in this section of the "Plan" line is similar because the Plan line represents a Rebaselining with TPZP that occurred in December 2014. However, in order to increase our transparency, we will add the original contract schedule to the graph which is referred to as Addendum 9 from this point forward. This way everyone will be able to see all of the history as we continue to deliver parcels. We continue to be focused on trying to deliver based on the early forecast. Mr. Rossi commented that on pages 15 and 16 for CP2-3 the plan has been adjusted. The December performance was not going to happen. Mr. Glen responded that the original forecast of 120 parcels in December was unrealistic. We were able to achieve the overall delivery at that point because we had a head start on it in the early months before the contract was executed. Mr. Rossi asked on pages 27 why the box "complete 100%" is in red. Mr. McLoughlin replied that is an error with no reason to be in red. Mr. Rossi asked on pages 26 why are we going to spend that much on the Program Level Budget. Mr. McLoughlin replied we are having meetings on each project section for schedule, budget, with each contract with each AWP of what we need to get to our target of the RODs. These numbers are what we are today. I'm looking at each contract again and each schedule and seeing what the cost and the level of effort it will take to get to those dates. I don't think that numbers should roll up but they could potentially. We may have costs that have not been day lighted to you yet. Now that the contracts have come back to the environmental departments we are relooking at those with the RDP. Mr. Rossi asked when this will get done. Mr. McLoughlin replied that today is the first meeting of the F Street. The next two weeks will be to get thru each section. That includes critical path for each schedule. In the next two weeks we should have some indication of what direction we will head for each one. Mr. Rossi asked on page 28 numbers 7 through 10 continue to slide further out, at what state do we change the dates. Mr. McLoughlin replied that we are monitoring the dates. We are going to have meetings this week to see how hard they are and where they move. For the Southern California ones the next month or so are important as it relates to the SAAs that are going to come for those that will set us forward, further more defining as we get into the draft documents to get into the check points. Those items are critical that will be coming to here or the Board in the next month. Mr. Rossi asked as they get reevaluated, if there continues to be delays, if the target date will be adjusted. Mr. McLoughlin replied yes. Mr. Rossi asked on page 39 what the due date means. Mr. McLoughlin replied that is when it is due internally to us to start looking ahead in preparation of an item that may be brought to the Board. It's an internal date that we target internally and the FRA is also part of that review. Mr. Richards asked if we are still on schedule for being under construction on the seven early key construction sites by the middle of March. Is that still a viable date? Mr. Jarvis replied yes. We are under construction on five sites right now on CP1: the Fresno River Viaduct, Tuolumne Bridge, Fresno Trench, Downtown Fresno Viaduct, and the Caltrans State Route 99 project is the fifth location. We expect State Route 180 to be in construction in March as well as the San Joaquin River Viaduct. At Avenue 12 we need one more parcel to start construction. That would make a total of 8 locations. Mr. Rossi asked on page 6 on re-baselining the budget and forecasting the coming months, mitigation measures and an analysis that is currently being used to identify the ARRA funds. What is the status of that report? Mr. Fong replied that we anticipate that to wrap up this week. Mr. Rossi commented on pages 4, 6, 44, 46, 55, 61, 69 and page 4 of 10 on the Capital Outlay and Expenditure Report. Mr. Rossi asked for a general assessment of CP1, where we are and what the potential downsides are so we are aware of what's going on in a more detailed way. Mr. Griggs responded that he will start with a general assessment. We are having significant activity in CP1. We have the seven critical locations that we are concentrating on and seeing a lot of construction in those as we move forward. We are pushing to make sure we clear all the additional areas of CP1 so we can get that moving as quickly as possible. The first two years have really been concentrated on contractor mobilization and getting the final design done. Being a design build it's common to get that done on the front end to complete the final design. As indicated in these reports we are encountering some challenges as we have started up CP1. In particular the ROW area, third party agreements, and the environmental reexaminations done if they are required changes to the environmental footprint as we go forward then getting the permits in place. On the ROW side we have some litigation early in the process that held us up but we have that taken care of and are moving forward and organized in a way that we are processing ROW on the program. We have over 1,000 parcels that we are looking at in terms of CP1 and CP2-3. It took us a while to get up to speed and organized and keep pace with the requirements in delivering those parcels. We have now addressed that and have a team in place and are doing a lot better in terms of delivering those parcels. On CP2-3 we are ahead of the plan and getting started on CP4 as well. Third parties are always a challenge. We have agreements that we need with the utilities, railroads and others. That has taken longer than we have hoped for. We seem to be in good position now as far as having agreements in place for the construction that is currently under way. There are some additional third party agreements that are going to be required that depend upon the contractor advancing their design. We have also seen a significant increase in the cost associated with third party utility relocation as compared to the budget that we originally had. Design mobilization of the contractor has been slower than anticipated. Now that we have the construction areas freed up for active construction they are proceeding much more quickly. One thing with the environmental reexaminations is the contractors when they bid the work they came in with alternative technical concepts, design ideas that they thought could help reduce the cost of construction and that was very successful. We saw significant reductions in the contractor bids coming in because of their innovations in technical concepts. The other side of that related to the environmental work is that did open up additional requirements for reevaluations and in some instances more ROW requirements. There is a tradeoff there and that affected the schedule going forward. In general we feel we are up to speed now. We are getting those issues addressed and construction is stepping up significantly. Mr. Rossi asked what the potential impact will be on CP1 and how risks are being mitigated to some lesser number. Mr. Tapping responded that there could be potential schedule and cost impacts as a result of the slow pace of obtaining right-of-way, obtaining third party agreements and the slow start of construction. We earlier established an approved contingency on CP1 using a risk-informed contingency analysis to address these and other risks. We update the risk-informed contingency analysis on a continuing basis to reassess the adequacy of remaining contingency. Such a reassessment was recently completed on CP1. We will update these assessments as the program advances. Under the Finance & Audit Committee's oversight, we have implemented a risk management program that uses state-of-the-practice risk management tools and analyses (such as Monte Carlo simulations) in order to flag early warning signs associated with potential cost and schedule risk. These analyses are used to facilitate and drive prudent and timely risk response actions before program cost and schedule has the potential to be impacted. The updated CP1 cost risk analyses performed by our risk management team indicates a negative trend with respect to three of the costs risks originally identified in the CP1 contract contingency analysis. These particular cost risks relate to right-of-way, utility relocations, requirements requested by the adjacent railroads (UP and BNSF) such as intrusion protection. While the cost risk analysis indicates that there is the potential of exceeding the current contingency envelope for the CP1 contract if risk mitigation actions are not undertaken, we are working to identify and implement risk mitigation strategies and potential savings. Mitigation involves such strategies as considering alternative design and construction approaches not only on CP1, but program-wide as well. At this time, based on the assessment of our risk management group, we are forecasting a need to increase contingencies on CP1 by approximately $150 million which is about 10 percent of the original CP1 budget and the first construction segment by approximately $260 million which is about 5 percent of the original FCS budget. Please note that increasing the contingencies does not mean the existing budgets will actually be exceeded. It is a management response to early detection of potential impacts based on our risk assessments that we continually undertake over the course of the project. Mr. Rossi asked for more detail on what the mitigation strategies are and what is being worked on to minimize the probability of it occurring. Mr. Griggs responded that we have taken very strong action in terms of strengthening the delivery teams for ROW, for handling third party utilities, and environmental support required with evaluations and permitting. For ROW Mr. Glen has about 35 people on his staff, four supporting contracts for ROW engineering, and 12 supporting appraisal and acquisition contracts. Mr. Glen has taken leadership of this group and restructured it in a way that is showing great success. As of February 10th in terms of delivery on CP1, we are 60% or 470 parcels out of a total of 730. We are seeing good progress with stepping up the delivery pace on ROW. We need to recognize that we have additional requirements coming forward on CP2-3 and CP4. We will continue to build up that staff so we are in a place to address the additional requirements. In terms of the environmental team, Mr. McLoughlin has about 40 people on his team. We are increasing that staff as well. A lot of that is getting the environmental clearances for the other sections but also building up the permitting group and the group that is supporting the reevaluations. The reevaluations are being done by the contractor but we have to agree with them and work with FRA for approval. Similarly on the third party staff we have strengthened that team. We will be adding some resources, especially in the estimating area. Something we have been challenged with regarding third parties is the difficulty of estimating the cost of utility relocation when most of the utilities are buried. It is very difficult to make an assessment of that, so we are going to bring on additional professionals to do some advanced surveys in addition to what are regional consultants are doing to get a better understanding of what those utility requirements are. A lot of it has been to strengthen our teams, make sure we have clear leadership and to track very closely. We have been reporting to Finance and Audit every month and for ROW we report weekly on how we are progressing the work so we can make sure and detect early any problems and take action on them. A lot has gone into the way we are organized, the way we are managing our group and the way we are reporting and tracking our performance. Mr. Rossi asked what is the current status of change orders for CP1. Mr. Griggs replied for CP1 we currently have approved approximately $14 million of the change orders that have been submitted by the contractor that is reflected by the contingency burn down. Mr. Rossi asked for details on the non-processed change orders with TPZP. Mr. Griggs responded that we are using a fairly standard approach of handling the change orders. We have received approximately 70 potential change orders that have been submitted by TPZP for review. The process we have is the contractor can make a change order request. We will then undertake a review of that request to see if it has merit. If we do not believe there is merit, then we will reject it. They can then take it forward as a claim and try to go through a dispute resolution of it. If we do agree with it, then we will negotiate what that value is to be and then move forward to execute the change order. Sometimes the change orders are not initiated by the contractor. Often we will initiate the change orders ourselves if we see the need to change something from what the contract currently requires. We try to assess what we perceive as potential change orders. Mr. Rossi stated that isn't it true that not all change orders have a cost or schedule. Mr. Griggs replied that is correct. Sometimes there are changes that we may get a credit for. They are not always going to increase the cost or schedule. In order to keep the scope of the contract up to date we have to have a record of any changes whether they have impact or not. Mr. Rossi asked if we will stay on schedule in the Central Valley. Mr. Griggs responded that we are anticipating an extension of the CP1 contract schedule. We do not anticipate that will affect the overall delivery date of the first construction segment. We have float on the CP1 schedule so if we incur a delay in the CP1 contract in terms of completion we do not anticipate it to affect the date of completion on the FCS. In terms of cost impact, as discussed above and based on early warnings, we may need to increase the contingency of CP1 and overall for the FCS. We are still managing and mitigating those projections in a way that we will continue to strive to stay within the overall budget for the FCS. Mr. Rossi summarized what Mr. Tapping and Mr. Griggs reported by saying when we constructed the original budget, we did not have the amount of information and private sector input we now have. Getting the additional information and actual experience, we now have a better basis to move forward with more control and focus on the problem areas just enumerated. We have responded by putting mitigations in place. All of these experiences will be reflected to a degree in the 2016 Business Plan. It is important to reflect on what was said in prior F&A meetings. Because of our early warning system and risk analysis we have been able to address these specific problems and be prepared for new problems. Projections will go up and down. That is the standard risk profile you have with any large complex project. The efforts that you are undertaking reflects that you are analyzing early, addressing early, detecting early, reacting early to issues and trying to contain them as quickly as you can find them. We are looking forward to seeing the confirmation of these efforts as we move forward. Mr. Richards added that the policies and the reporting implemented over the last three years appear to be working. With the risk assessment and the information that has been inputted into it we are identifying the potential of risks early on and doing the kind of oversight expected from any management of a large infrastructure project. It is the challenge now to ensure the appropriate management of the mitigation measures that have been and are being put into place. Mr. Rossi added that the advantage of doing this type of risk analysis and risk mitigation is you do it at points in time and you talk about potential probabilities. Nothing that is said here indicates that we are over budget. It does indicate that we could be and we are getting prepared for that and doing everything we can to ensure that doesn’t happen.

Agenda Item – Audits – Paula Rivera

- None.

Agenda Item – CP 1 & 2-3 and SR-99 Project Update

- None.

Current Issues

- No current issues.

Meeting adjourned at 9:29 am.