



# LG Risk Assessment and Participation/Responsibilities in AFAs

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## **Local Government Participation and Responsibilities In Advance Funding Agreements**

The Negotiated Contracts Policy Manual, developed by the Contract Services Office, presents statutory authority and policies for negotiated contract management. Negotiated contracts involve services whose authorizing statute requires TxDOT to select a performing entity using a process other than competitive bids. An Advance Funding Agreement (AFA) between TxDOT and a local government, another state agency, or another state where both parties agree to a funding arrangement to contribute funds, labor, raw materials, or land in order to develop or maintain a highway project is a negotiated contract. In an AFA, TxDOT and a local government will conduct separate “typical” procurements for each of the tasks assigned to them (if any) by the AFA. It is each party’s responsibility to fulfill all of its respective obligations under the AFA and applicable laws, rules and regulations.

Texas Administrative Code, Title 43, Part 1, Chapter 15, Subchapter E defines available methods for federal, state, and local cost participation in highway improvement projects. In addition to identifying the scope of the transportation project and the amount of funding provided by each party, two major decisions must be made by TxDOT and the local government prior to execution of an AFA:

1. Which party is responsible for performing the various phases of the project development process?
2. Which method of funding participation is appropriate: fixed price, specified percentage, or periodic payments?

This document includes guidance on how to address these topics consistently throughout the state. It is based upon a review of applicable laws and regulations and discussion with many districts, divisions, and the Administration.

### **Responsibility for Performing Project Development Phases:**

#### **Title 23 United States Code (USC) 106(g)(4) states:**

Responsibility of the States -

(A) In general - The States shall be responsible for determining that subrecipients of Federal funds under this title have:

- (i) adequate project delivery systems for projects approved under this section; and
- (ii) sufficient accounting controls to properly manage such Federal funds.

(B) Periodic review - The Secretary shall periodically review the monitoring of subrecipients by the States.

#### **Title 23 Code of Federal Regulations (CFR), Chapter I, Subchapter A, Part 1 §1.11 (b) states:**

Governmental engineering organizations - The State highway department may utilize, under its supervision, the services of well-qualified and suitably equipped engineering organizations of other governmental instrumentalities for making surveys, preparing plans, specifications and estimates, and for supervising the construction of any project.

#### **23 CFR, Subpart A §635.105 states:**

Supervising agency -

(a) The State Transportation Department (STD) has responsibility for the construction of all Federal-aid projects, and is not relieved of such responsibility by authorizing performance of the work by a local public agency or other Federal agency. The STD shall be responsible for insuring that such projects receive adequate supervision and inspection to ensure that projects are completed in conformance with approved plans and specifications.

(b) Although the STD may employ a consultant to provide construction engineering services, such as inspection or survey work on a project, the STD shall provide a full-time employed State engineer to be in responsible charge of the project.

(c) When a project is located on a street or highway over which the STD does not have legal jurisdiction, or when special conditions warrant, the STD, while not relieved of overall project responsibility, may arrange for the local public agency having jurisdiction over such street or highway to perform the work with its own forces or by contract; provided the following conditions are met and the Division Administrator approves the arrangements in advance.

(1) In the case of force account work, there is full compliance with subpart B of this part.

(2) When the work is to be performed under a contract awarded by a local public agency, all Federal requirements including those prescribed in this subpart shall be met.

(3) The local public agency is adequately staffed and suitably equipped to undertake and satisfactorily complete the work; and

(4) In those instances where a local public agency elects to use consultants for construction engineering services, the local public agency shall provide a full-time employee of the agency to be in responsible charge of the project.

**Paragraph 15.52 (8)(D) of Texas Administrative Code (TAC), Title 43, Part 1, Chapter 15, Subchapter E states:**

Approval: ...In determining its approval or disapproval of local government's request to manage one or more elements of performance and management of a project, the Department will evaluate the following criteria:

- (i) previous experience of the local government in performing the type of work proposed;
- (ii) the capability of the local government to perform the type of work proposed or to award and manage a contract for that work in a timely manner, consistent with federal, state, and department regulations, standards, and specifications;
- (iii) the need for accelerated project delivery;
- (iv) Department resources available to perform or manage the highway improvement project in an efficient and timely manner;
- (v) cost effectiveness of local performance of the work as compared to awarding the highway improvement project through the competitive bidding process; and
- (vi) any other considerations relating to the benefit of the state, the traveling public, and the operations of the Department.

As clearly stated in federal law, federal regulations, and state regulations, TxDOT has a responsibility to determine each local government is qualified and has adequate resources and controls to perform the project work, prior to authorizing it to perform any element of the project development process.

**LG Risk Assessment and Qualifications Review Process**

In order to fulfil this requirement, and as good business practice, TxDOT has developed a standardized process and a series of forms to evaluate each local government's qualifications for performance of one or more elements of the project development process. The process includes the following forms:

1. LG Agency Risk Assessment,
2. Special Approval per TAC 15.52, Parts A & B, and
3. TxDOT Project Update Evaluation of LG Qualifications.

The LG Agency Risk Assessment is to be completed by the District in coordination with TxDOT's Local Government Projects Section (LGP). TxDOT's LGP Section will work with the Districts to develop a schedule to review the overall risk of each LG on a regular basis. This LG Agency Risk Assessment form uses multiple evaluation criteria to evaluate the overall risk to TxDOT if the LG is allowed to manage one or more elements of the project development process.

This form assigns one of the following risk levels to the LG:

- A – Low level of risk to TxDOT
- B – Moderate level of risk to TxDOT
- C – High level of risk to TxDOT
- D – Unacceptable level of risk to TxDOT

This overall agency level of risk is a component used in the other forms. If the LG agency is rated A or B, the agency will be re-evaluated every two years. If the LG agency is rated C or D, they will be re-evaluated annually. It is recommended that a group of individuals within the district familiar with the LG agency's capabilities work together to complete the form for acknowledgement by the District Engineer. District Engineers have the option of requesting that the evaluation for one or more LG agencies within their district be evaluated by a peer group of TxDOT individuals from other districts who manage LG projects. If this is requested, LGP will assemble a peer group and lead the LG agency evaluation process of completing the form for acknowledgement by the District Engineer.

For AFAs Executed on or after the effective date of this guidance:

“Special Approval per TAC 15.52, Parts A” is to be completed by the local government requesting approval to perform or manage one or more elements of the project development process. The district may assist the local government in preparation of this form. As indicated at the end of page four of the form, it must be signed and dated by a local government representative. It should then be submitted to the local district office to initiate the evaluation process. Upon receipt of the local government provided information form, the district will review the information furnished by the local government and complete its evaluation using “Part B - TxDOT Evaluation of LG Qualifications” of the Special Approval per TAC 15.52 form. The TxDOT risk rating (A, B, C, or D) from the LG Agency Risk Assessment Form is entered as one factor to be considered under evaluation criteria #1 on the “TxDOT Evaluation of LG Qualifications” form. Upon completion of its evaluation, the District Engineer is to recommend which elements, if any, be performed or managed by the local government. This recommendation will be signed and dated by the District Engineer and submitted to the Deputy Executive Director for review and concurrence. Upon receipt of concurrence from the Deputy Executive Director, the district and local government may complete negotiation of all Advance Funding Agreement terms and Contract Services is authorized to execute the AFA on behalf of the Department.

#### For Projects with Existing AFAs

As stated above, TxDOT's LGP Section will work with the Districts to develop a schedule to review the overall risk of each LG on a regular basis. The LGP Section and Districts will endeavour to complete the initial risk assessment of all local governments with active AFAs (approximately 200) prior to August 31, 2017. Within 90 calendar days after completion of the LG Agency Risk Assessment for a local agency, each district will complete a TxDOT Update Evaluation of LG Qualifications form for each active project which does not have a Special Approval per TAC 15.52, Parts A & B on file. For projects with AFAs executed on or after the effective date of this guidance, each District may

complete "TxDOT Project Update Evaluation of LG Qualification" forms at any time deemed appropriate by the District Engineer.

The Districts will coordinate these efforts with the LGP Section and will submit an electronic copy of all LG Agency Risk Assessment forms, Special Approval per TAC 15.52, Parts A & B forms, and TxDOT Project Update Evaluation of LG Qualification forms to the LGP Section within 30 days of execution.

Guidance on Method of Funding Participation:

Definitions:

**Fixed Price** - Costs will be allocated based on applicable Federal funding, State funding, and a fixed amount of Local Government funding until Local Government funding reaches the maximum obligated amount. The State (using State or Federal funds, as applicable) will then be responsible for 100% of the costs.

**Specified Percentage** - Costs will be allocated based on applicable percentages of Federal funding, State funding, and Local Government funding until Federal and State funding reach the maximum obligated amount. The Local Government will then be responsible for 100% of the costs. The following costs may be a fixed price with District Engineer approval:

- Environmental Direct State Costs
- Right of Way Direct State Costs
- Engineering Direct State Costs
- Utility Direct State Costs
- Construction Direct State Costs
- Non-Construction Direct State Costs
- Indirect State Costs

**Periodic** - The local government proposes a schedule to pay its allocated project costs that differs from the normal pre-payment schedule.

The standard funding arrangement on projects with a combination of local plus state and/or federal funds is Fixed Price according to T.A.C. §15.52 of Texas Administrative Code (TAC), Title 43, Part 1, Chapter 15, Subchapter E. This method of funding does not require final reconciliation of actual Department costs versus local government contributions on projects which include local funding participation. History has shown that on many Specified Percentage projects it has taken a considerable time to close out the project after construction completion due to the required process of:

- conducting a final project audit,
- preparation of a Statement of Cost,
- notifying the local government:
  - they have paid excess funds and reimbursing the local government the excess funds, or
  - additional local funds are required and collecting the additional funds from the local government, and
- closing out the project.

In many cases the funds owed/due were relatively minor yet required extensive analysis to quantify the exact amount.

Specified Percentage and Periodic Payments are alternate funding arrangements subject to special approval by the Executive Director (which has been delegated to the Deputy Executive Director).

The Commission's expectation is that the AFA for most projects which are managed from start to finish by TxDOT with partial funding from a local government will be Fixed Price. The districts should develop the initial cost estimates with proper care so that the projected costs for all elements of project development are reasonably accurate. This will minimize financial risk to TxDOT. The AFAs may be modified by written amendment when executed by both parties in the following instances:

- significantly differing site conditions,
- when work requested by the local government is determined to be ineligible for federal participation,
- when there is change in the scope of work,
- when the adjustment is mutually agreeable to the Department and the local government.

On substantial projects, it is likely that the Department and the local government should validate the local government Fixed Price upon receipt of construction bids to confirm the local government level of participation is at a similar percentage of total project costs as was anticipated upon execution of the AFA. If costs are considerably higher than originally estimated and the Department and the local government cannot agree upon a revised level for each party's financial participation through execution of an Amendment, the Agreement may be terminated in accordance with terms of the AFA.

For projects where the Department approves a local government to manage one or more elements of project development, using a Specified Percentage funding arrangement for the local government performed or managed elements of project development frequently is the appropriate choice. If the local government is managing all elements of the project development, Specified Percentage (in most cases) will be the preferred method of sharing costs. In Specified Percentage agreements, a maximum amount of federal and/or state participation is also appropriate. In these cases, the local government will be responsible for all project costs above the funding commitment of state and/or federal funds.

Examples of how this guidance may be implemented are as follows;

1. Off-system project with only federal and local funding, the local government is managing the entire process from start to finish.
  - a. Specified Percentage for all elements
2. Off-system project with only federal and local funding, the local government is managing design, utility relocation, and right-of-way acquisition, TxDOT is managing environmental and construction.
  - a. Specified Percentage for LG managed tasks
  - b. Fixed Price for TxDOT managed tasks
3. On-system project at request of the local government, TxDOT is managing the entire process from start to finish.
  - a. Fixed Price for LG contribution, TxDOT responsible for cost overruns.
  - b. Evaluate whether an Amendment is necessary upon receipt of construction bids to adjust LG financial participation to properly allocate actual construction bid amount to LG.
4. Major on-system project being managed by TxDOT with federal/state funding. Original project scope was all federal/state funding. Minor additions have been requested by LG and are incorporated into the project to accommodate local requests.
  - a. Fixed price for LG contribution, TxDOT responsible for cost overruns
  - b. Evaluate whether an Amendment is necessary upon receipt of construction bids to adjust LG financial participation to properly allocate actual construction bid amount for requested additions to LG.
5. Major on-system project with federal/state/local funding with all elements of work being managed by a Regional Mobility Authority.
  - a. Specified Percentage for all elements, LG responsible for cost overruns.

The attached FAQ responds to some recently asked questions.

**Frequently Asked Questions**  
**Fixed Price vs. Specified Percentage on AFAs**

**Estimates**

Question: In general, the project estimate for LG projects is based on an estimate the LG submits in their project nomination packet when responding to an MPO's Call for Projects for Cat 5, 7, and 9 funding. The project is selected by the MPO without review or input from the State on the accuracy of the estimate. Are we expected to update the estimate at the time of AFA development or are we supposed to use the project nomination estimate?

Answer: The AFA should only be executed using an estimate that is mutually agreed upon by the State and the Local Government. This may differ from the initial estimate submitted to the MPO by the LG. The agreed-upon estimate should be provided to the MPO to reflect the current estimated project cost.

**Overruns**

Question: If a fixed-price project overruns, is the State expected to amend the AFA to update the fixed price of the project? Or, is the intention to treat this like the Off-system Bridge Program and the LG costs are fixed regardless of work/cost overrun?

Answer: No, It is not anticipated that amendments to the AFA would be necessary or appropriate on a frequent basis to adjust for overruns due to changes in actual material and labor costs from those in the estimate used as the basis of the Agreement. Once the contract has been executed, the State has agreed to cover cost overruns, and should act accordingly. The State would be acting in bad faith if it requested an adjustment to the budget page due to cost overruns, when it agreed to cover them in the original contract. However, if anticipated costs of the project increase substantially due to major changes in scope or significant increases in material, right of way, or utility relocation costs, the State and LG should consider amending the AFA and adjusting participation by each party prior to awarding the construction contract. If a project's cost increases significantly and the parties cannot agree to an Amendment, the AFA can be terminated by either party in accordance with the terms of the AFA.

Question: If the project overruns its costs in a Fixed Price AFA, what funding source will be used to cover TxDOT's increased cost for the overrun? If the answer is, the overruns will come from the same funds for which it was funded, does this also apply to Category 5, 7, and 9 funds allocated by an MPO? Does this mean that future allocations of funding will be reduced to cover current overruns?

Answer: If a project overruns, the party responsible to cover the increased costs may use its available sources of funding to provide the required funds. If the available funds come from Category 5, 7, or 9 funds allocated by an MPO, and the MPO agrees to increase its contributions to this project, the MPO's available funds will be reduced for other projects from these sources.

### **ROW/Utilities**

Question: Do fixed price provisions apply to ROW and Utility agreements?

Answer: Fixed Price provisions should be implemented similarly on all agreement types.

### **Locally Funded Projects**

Question: Are Locally Funded Projects fixed price regardless of whether they are on or off system? If so, what source of funds will cover the overruns?

Answer: No. The funding structure for an agreement depends on the terms to which the parties agreed. However, Fixed Price provisions should be implemented for all TxDOT-managed elements of an AFA. If a project overruns, the party responsible to cover the increased costs may use its available sources of funding to provide the required funds.

### **Local Lets**

Question: The Fixed Price AFA does not have a requirement that the State approve cost estimates before an LG lets a project or adds additional work after the project has let via change order. Is the State still responsible for overruns?

Answer: Yes, if you have a Fixed Price AFA. However, it is recommended that AFAs for Local Let project contain Specified Percentage funding structures for any LG-managed project activities. Local-let projects and specified percentage AFAs require the Deputy Executive Director's special approval. .

### **Use of Fixed Price Template**

Question: In general, all of the LG federally funded projects were selected during previous MPO Program Calls, i.e., prior to the implementation of the Fixed Price AFA becoming the standard method. We would prefer to use specified percentage AFA for these projects; however, Contract Services is mandating use of the Fixed Price template. Can we use Specified Percentage for these projects?

Answer: All new AFAs should conform to the current requirements of TAC §15.52. Specified Percentage can be used with approval of the Deputy Executive Director.

Question: Amendments: Whenever an amendment to an agreement is necessary, Contract Services typically requires an update to all articles that have changed since execution of the original AFA. If we did that, we would change entirely the terms of the AFA. Will Contract Services amend specified percentage AFAs without requiring that we update to the new template?

Answer: Whenever an amendment to an AFA is necessary, any applicable changes in Federal or State law since the execution of the AFA (and subsequent amendments thereto) must be incorporated into the new amendment. Existing Specified Percentage AFAs do not need to be changed to conform to new TAC requirements unless it is deemed beneficial to both the State and the LG. Other Amendments to the AFAs may be executed without altering funding participation when there is no other business purpose to change the funding participation.