

# **Capital Project Funding Guide**

DGS Capital Programs

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## 1. Introduction

Pennsylvania law charges the Department of General Services (“DGS”) with the responsibility to manage all aspects of construction projects (“capital projects”) for executive agencies under the Governor’s jurisdiction and some independent agencies.<sup>1</sup> The primary principle underlying every capital project is very simple: a capital project represents a significant investment of long-term debt paid for with taxpayer dollars, to be treated with respect and a deep appreciation for the fiscal debt incurred by the Commonwealth to fund the project. As project managers, DGS Capital Programs balances our role of stewards for the taxpayers and advocates for our client agencies, carefully supervising every element of each project, including budget.

One of the most critical elements of any successful project requires adequate funding managed in a standard and transparent manner. Funding issues are the primary source of delays during the planning, design, and procurement phase of capital projects and directly impact project success. Inadequate funding exposes an agency’s capital plan to unplanned changes and places operating funds at risk if additional funds become necessary for the project. The project funding practices established in this memo are designed to structure budgets effectively to deliver an awardable project during the bidding/award phase while maintaining adequate contingency funds to execute a project during the construction phase.

## 2. Background Information

Effective management of a “capital project” (a.k.a. Public Improvement Project (PIP)) starts with understanding certain terms:

- **“Construction”**: is the process of building, altering, repairing, improving or demolishing any public structure or building or other public improvements of any kind to any public real property.
- **“Project”**: includes all work necessary to complete the entire scope of work, including all general construction, hazardous material removal, fire suppression, elevator, HVAC, plumbing, and electrical work.
- **“Capital Project”**: include various types of renovation projects, new buildings, nonstructural improvements, and land acquisition that is authorized in a Capital Budget Project Itemization Act when:

1. State bond proceeds are used and the total project is valued at \$100,000 or more; or

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<sup>1</sup> Act 45 of 1975 - established the contract administration responsibilities for all projects authorized by Commonwealth capital authorization acts to the Department of General Services. In fact, DGS administers contracts for professional services and construction based upon Act 45, the Commonwealth Procurement Code (62 Pa.C.S.), and departmental instructions. "Capital Project" (a.k.a. Public Improvement Project) includes bond funded projects greater than \$100,000 funded by bonds and agency funded projects greater than \$600,000.

2. Current revenues are used and the total project is valued at more than \$600,000; and
  3. The project has and an estimated useful life of not less than 10 years.
- **“e-Builder”**: is a construction project management software solution utilized by Capital Programs that is used to manage capital projects from planning through closeout including processing of Project Charters and Charter Revisions, schedule, and cost.

Any construction project, regardless of scope, with a cost exceeding \$100,000 for bond proceeds or \$600,000 for current revenue funds is a capital project<sup>2</sup> to be managed by DGS Capital Programs and must have legislative authorization in a Capital Budget Project Itemization Act.<sup>3</sup>

As the agency designated to manage capital projects, DGS accepts responsibility for being familiar with the project-specific legislative authorization and to ensure the project scope falls within this authorization. In essence, DGS lacks authority to build a swimming pool if the legislative language authorizes us to build a science center. If there are questions about scope, do not hesitate to submit the question to the DGS Office of Chief Counsel who can assist with interpreting the statutory language.

### **3. Project Funding – Legislation**

Agencies must receive legislative authority before starting a capital project. Each fall the budget office sends out instructions and templates for agencies to make requests for capital itemizations in the Governor’s Executive Budget.

Capital Budget Project Itemization Act - The draft bill is developed based on agencies’ budget book submissions and is proposed with the Governor’s Executive Budget. The draft is subsequently introduced by a member of the General Assembly. During the legislative process, agencies are permitted to submit proposed changes to be introduced as amendments to the bill. Agencies should contact the Budget Office if they want to introduce an amendment. Legislators can also add projects that they deem appropriate through an amendment.

Capital projects that have been included in a Capital Budget Project Itemization Bill that was passed by the General Assembly and signed by the Governor are now authorized under a Capital Budget Project Itemization Act. Projects authorized under a Capital Budget Project Itemization Act may be released and funded through bond proceeds when scheduled on the DGS Capital Plan.

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<sup>2</sup> When GGO funds are used, artificially breaking a project into increments less than \$600,000 subjects an agency to review for violations of the Procurement Code.

<sup>3</sup> Emergency projects can exceed \$600,000 and be performed through the JOC program but any JOC emergency must be funded only with Agency GGO funds.

The language in a Capital Budget Project Itemization Act that provides funding to projects may vary from Act to Act. More recently, language in Capital Budget Project Itemization Act funding contains only a lump sum dollar values with no reference to Base Allocation, Land Acquisition or Design & Contingency. This “Lump Sum” language creates opportunities for the Client Agency to request only a portion of the funding for the project, leaving funding in the line item for future projects at the facility or specific building, depending upon the legislative language. DGS Capital Planning will collaborate with Client Agencies during the capital planning phase of each project to create an accurate estimate of the funds that should be requested for the project based upon scope and priority, which may impact escalation calculations.

For Capital Budget Project Itemization Acts that specify funds for “*Land Acquisition*,” “*Base Allocation*”, and “*Design & Contingency*”, DGS cannot ‘reallocate’ funds as we deem necessary. The Legislative branch allocates the amount and category of the funds, which establishes the project budget. “*Base Allocation*” establishes the funds available to award construction contracts. “*Design & Contingency*” has usually, although not always, been set up as 20% of Base Allocation. If the project needs Land Acquisition, there must be specific legislative authorization to acquire land. Without authorization, DGS may not acquire land.

The Legislature usually, although not always, enacts a Capital Budget Project Itemization Act every two to three years. Each Capital Budget Project Itemization Act contains several sections authorizing projects using different funding sources. Capital projects that DGS manages appear mostly in Section 3 of each Capital Budget Project Itemization Act.<sup>4</sup>

During any point in the project, Capital Programs personnel may have to address whether the agency has Legislative language in a Capital Budget Project Itemization Act that authorizes the scope of work requested during design or as a change order during construction. If the additional scope exceeds legislative funding authorization, the progress must stop until the issue is resolved by either adding GGO funds or by getting legislative authorization to use additional PIP funds and/or to expand permissible scope.

#### **4. Project Funding – Capital Planning**

Early discussion on budget scope and budget are essential to manage risk during the planning phase of the project. Agencies shall participate in annual Capital Planning workshops to review their capital plan and adjust project priorities, as needed. Capital Planning will work with the agencies to create Pre-Project Charters that identify scope and validate cost assumptions in advance of the start of the projects planned for the next two fiscal years beyond

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<sup>4</sup> Each Capital Budget Project Itemization Act also contains language establishing funds for “Fixtures, Furniture & Equipment” (“FFE”) to be purchased for capital projects. FFE language appears in Section 4 of the bill. FFE funds cannot be used for construction, nor should scope of work that is actually construction be deferred to FFE funds for purchase, such as bleachers or various A/V work. Capital Programs personnel, designers and agencies should refer to the “FFE List” in e-Builder for guidance on what items fall within PIP, GGO and FFE. In addition, moving expenses (moving furniture out, back in or into the building from another site) are not eligible to be paid from PIP or FFE; GGO must cover these costs.

the upcoming budget year. Once projects are added to the plan, Capital Planning will set up project costs on the capital plan based on the following default formula:

**a) Design, Contingency, and Construction Budget Formula**

1. 75% of total funds allocated to Construction.
2. 25% of total funds allocated to Design and Contingencies, including:
  - a. Construction Contingency
  - b. Design Basic Services
  - c. Budgeted Work Orders
  - d. Anticipated 3rd Party Costs
  - e. Professional Change Order fee
  - f. Design Contingency

The budgeted breakdown of 25% for Design and Contingencies will be managed by the Bureau of Design Management during the pre-design and design phases. The default value for construction contingency shall be 10%. Deviations below the 10% default value require a cost risk assessment approved by the Assistant Director of Design Management. Deviations below 8% Construction Contingency require a cost risk assessment approved by the Director of Design Management, the Director of Construction, and the Client Agency Sponsor and must highlight that the agency will be responsible for cost overruns. The Professional Change Order fee shall be recalculated based on the negotiated agreement Change Order (CO) fee percentage of the approved Construction Contingency amount.

Deviations above the 75% fund allocation to Construction and below the 25% funds allocation to Design and Contingencies can only be approved by the Deputy Secretary of Capital Programs.

**b) Project with Land Acquisition**

This memo will set forth permissible use of Land Acquisition funds. REMEMBER: If the project needs land acquisition, there must be specific legislative authorization to acquire land. Without authorization, DGS may not acquire land.

As a matter of policy, permissible land acquisition costs are limited to those costs needed to legally purchase the site, namely:

- Purchase Price
- Closing Costs
- Title Insurance
- Appraisal
- Site Survey
- Phase 1 Environmental Costs

All other costs incurred prior to purchasing the property to assist in determining the acceptability of the site are to be performed through a Budgeted Work Order to the design professional paid from Design Contingency line item funds. These costs include any type of:

- Site Analysis
- Soil Borings
- Structural Analysis

- Test Pits
- Hearings/meetings
- Wetland Analysis
- Feasibility Studies
- Zoning/Land use reviews
- Other Engineering costs

If land acquisition costs exceed the funds allocated for land acquisition, the project must be suspended until such time as additional funds can be added, either from Agency funding source or from additional funding in an existing Capital Budget Project Itemization Act. (If PIP is added, the project must be reviewed by the Capital Planning Coordinator.) In Acts with specific Base Allocation line-item itemization, the Base Allocation funds may not be used at any time for any reason for land acquisition. Nor may the funds be taken from Design, Construction Contingency or Professional CO Fee line-item funds. The Commonwealth should not be considering or purchasing land that requires additional costs so as to prevent construction of the building the Client Agency needs or expects.

**5. Prioritization Memorandum**

Each year DGS Capital Programs provides the Budget Office a Capital Plan with priority projects for the following fiscal year, essentially a release strategy that identifies the Capital Projects that will be released (funded/allowed to begin the professional selection process) during each quarter of the following fiscal year.

Client Agencies establish the priority in which projects proceed within their planned allocation. Agencies are expected to commit to project priorities through a mutually agreed Prioritization Memo no later than the end of October each year to align with the submission of the Capital Plan to the Budget Office. Capital Planning will assist with early project validation and ensure projects included on the Prioritization memo have a pre-project charter completed. **Failure to approve the annual Prioritization Memo by the October deadline may result in the start of projects being delayed.**

**6. Project Charters**

The Project Charter is a high-level document that describes the purpose of the project, the general scope of work, the project budget and its funding sources. The Project Charter is approved by DGS and the Client Agency Project Sponsor. Any changes to the Project Charter require approval by the Agency Project Sponsor.

Following the endorsement of the agency Prioritization Memo, the Bureau of Design Management will work with the Client Agency to finalize all project charters for projects schedule to go to professional selections the following fiscal year by January. Approving the Project Charter provides the Bureau of Design Management the authorization to start working on the project and start the Pre-Design Phase.

**7. Pre-Design Phase**

During the Pre-Design Phase, DGS will elaborate and validate the project scope of work and budget described in the Project Charter by conducting a Project Development Study (PDS)

with the Client Agency to prepare the project for Professional Selections. Following Professional Selections, DGS will negotiate the agreement for professional services with the appointed Professional.

**a) Project Development Studies (PDS) and Budget Validation**

The goal of the PDS workshop is to establish a level of confidence the project can be delivered that satisfies the Client Agency's project values and desired scope of work within the constraints of the budget and schedule.

If during the PDS, the Department determines the budget is insufficient to accommodate the project, the Client Agency must reduce the scope of work or add funds to the project. The Project Charter Revision Process (PCR) will be used to add funding or make significant changes to the project scope. If a Client Agency does not approve a PCR, the project will not be advertised for a Professional until the Client Agency provides appropriate funding or scope modifications. Once project funding or scope is adjusted to match anticipated project costs, the project can proceed through the Professional Selections process.

**b) Design Fee Negotiations**

Following Professional Selections, DGS will negotiate design fees with the appointed Professional. There is no formula or percentage for determining design fees, rather fees are determined based upon each project's level of effort and Base Construction Amount (BCA).

During negotiations, the DGS Portfolio Manager and the Professional will negotiate the project's basic services fee and budgetary estimates for all anticipated additional services work orders and 3<sup>rd</sup> party costs. Additionally, the Portfolio Manager will establish a design contingency budget to account for unplanned design fees. The default design contingency budget shall be 8% of the Basic Services Fee. Deviation from the default 8% design contingency requires a risk assessment approved by the Director of Design Management.

The estimated costs for design fees, construction and contingencies must remain within the project budget documented in the Project Charter. **The Client Agency may not direct DGS Capital Programs to negotiate to an amount that exceeds the approved project budget.** In cases where the negotiated fees and forecasted costs exceed the allocation assigned to the project, the PCR process will be used to add funding or make significant changes to project scope. If a Client Agency does not approve a PCR, negotiations shall be paused until the Client Agency provides appropriate funding or scope modifications. Once project funding or scope is adjusted to match anticipated project costs, the project can proceed through negotiations.



## 8. Design Phase Cost Management

During the design phase, the Design Project Manager (“DPM”) is expected to manage the project in accordance with the budget, legislation and scope of work described in the Project Charter. The Design Project Manager is responsible for maintaining a cost forecast using the e-Builder cost forecasting tool. The cost forecast accounts for all current, projected and forecasted costs for the project. When the cost forecast indicates that a project is expected to be overbudget, the DPM must address the cost overrun by:

1. Reviewing cost estimates with the Professional, Cost Estimator and Client Agency to improve the accuracy of the estimate by clarifying scope and reducing assumptions.
2. Requiring the Professional to present options for the Client Agency to consider that would reduce the estimated project costs within budget.
3. Working with the Professional, Cost Estimator and Client Agency to change the scope of work to bring the estimated costs within the project budget.

In addition, the Department may reallocate some of the construction contingency budget to accommodate the cost overrun. Reallocation of the construction contingency below the 10% default value requires a cost risk assessment approved by the Assistant Director of Design Management. Deviations below 8% Construction Contingency require a cost risk assessment approved by the Director of Design Management, the Director of Construction, and the Client Agency Sponsor and must highlight that the agency will be responsible for cost overruns.

If the options above are not sufficient to reduce the project costs or not desirable by the Client Agency, the PCR process will be used to add funding (either Letter of Commitment(LOC) or additional PIP funding) or make significant changes to project scope. Releasing additional PIP funding is subject to revising the Agency’s Capital Plan.

**If a Client Agency does not approve a PCR, design work on the project shall not proceed beyond the current design stage until the Client Agency provides appropriate funding. Note: Any changes to scope must remain within the legislative language authorizing the project.**

DGS may suspend the project if the Client Agency does not provide direction on how to address the budget overrun or if the Client Agency delays the bidding of the project on their capital plan. Project suspension would also be appropriate if the project requires additional funding, and the Client Agency must wait until the next Capital Budget Project Itemization Bill passes to add funding to the project.

At the direction of the Client Agency, DGS may cancel the project if the project is no longer feasible or desired.

### a) Client Agency Requested Scope Changes

DGS is responsible for delivering a project that meets the Client Agency's expectations as documented in the Project Charter and validated during the PDS. During the Programming, Schematic and Design Development design stages of a project, it is expected that components of the project work and design solutions may change based on the iterative design process. During this period of time, DGS and the Professional will collaborate with the Client Agency to make decisions. Following the approval of the Design Development submission, the Professional will document all design decisions sufficiently in the drawings and specifications to bid the project. There should be no Client Agency requested scope changes after the approval of the Design Development submission.

**b) Insufficient Design Contingency**

If the DPM determines the design contingency line-item budget is insufficient to complete the project, the DPM may request additional funding by PCR or request a construction contingency reallocation to replenish the design contingency. The additional funds should be sufficient to replenish the contingency to an amount deemed acceptable to the DPM based on the level of risk remaining in design.

**9. Project Funding - Pre-Bid Requirements**

Prior to bidding, the DPM must ensure the estimated project costs are within the project budget including all design fees, estimated construction costs, third party costs and contingencies. Additionally, the DPM should do the following prior to sending the project to the Procurement Chief for bidding:

**a) Liquidate Work Orders**

The DPM should review all Work Orders issued and performed during the design phase. Any work that is complete should have invoices submitted and designated as the 'final invoice' in e-Builder. Upon receipt of a final invoice, DGS Fiscal will liquidate and uncommit the remaining work order funds.

**b) Finalize Construction Phase Work Orders**

The DPM is responsible for negotiating the costs and scope of work of all Construction phase work orders prior to bidding.

**c) Update the Cost Forecast**

The DPM will update the cost forecast to include all anticipated costs based on the approved construction documents submission including all additional services, third party costs, estimated construction costs and contingencies to complete the construction phase.

**d) Cost Estimates and Delays following the Construction Documents Submission**

The DPM is responsible for ensuring the cost estimate is less than 6 months old prior to bidding. All cost estimates older than 6 months must be revised to properly escalate the costs to the midpoint of construction. If the new cost estimate is within 10% of the BCA, the project may be bid. Prior to bidding in this scenario, the DGS Portfolio Manager, Director of Design Management and the DPM will meet with the Agency Project Sponsor to discuss the risks associated with bidding the project.

If the new cost estimate is not within 10% of the BCA, a PCR must be initiated and approved to add funds to the project prior to bidding. If a Client Agency does not approve a PCR, the project will not be bid until the Client Agency provides appropriate funding or scope modifications. Once project funding or scope is adjusted to match anticipated project costs, the project will proceed to bid.

If delays following the approval of Construction Documents are caused by scope changes (in extraordinary circumstances), the DPM must initiate a PCR and gain approval for the scope change and additional budget prior to implementing the change. Following the approval of the PCR, the DPM will direct the Professional to incorporate the change into the bidding documents and provide a new cost estimate in the e-Builder Construction Documents Review Process. The project may proceed to bidding only if the new estimated costs are within the BCA.

## **10. Project Funding – Post Bid/Award**

After the bids are opened, DGS posts the bid tabulation and waits three calendar days to see if any bidders request to withdraw their bids. When the three days have transpired, the Procurement Chief reviews bids. If bids are above the BCA, the Capital Programs DPM will provide the client agency with a preliminary Fiscal Analysis to determine if the project is affordable. The preliminary fiscal analysis is not binding. Any bids for contracts with Small Diverse Business or Veteran Business Enterprise goals will undergo a responsiveness review to determine if contract specific goals will be met or a good faith effort waiver is approved. Only Bidders determined to be responsive by the Issuing Office will be considered in the final fiscal analysis.

After a responsiveness review is complete, Capital Programs DPM will perform a final **Fiscal Analysis** of every base bid using the lowest responsive bidder total bid costs. The Funding Analysis Spreadsheet is presented to the Client Agency Project Coordinator by the DPM. The Client Agency Project Coordinator decides which base bid should proceed to award. If the desired base bid requires additional funds, the DGS Capital Planner will setup a teleconference with the DPM, DGS Portfolio Manager, Client Agency Project Coordinator and the Client Agency Project Sponsor to discuss the fiscal analysis, the budget change and any impacts the change may have on their capital plan. The Agency Project Sponsor will decide how to fund the desired base bid either through the release of additional PIP funding or by providing a LOC.

Once funding is adjusted, Capital Programs issues Notices of Award and obtains executed contracts based upon the values used for the awarded fiscal analysis.

## 11. Project Funding – During Construction

The project should proceed through construction with contractors paid from their distinct line items set up in the e-Builder cost module.<sup>5</sup> Change orders (CO) are paid from the collective Construction contingency line item. Bureau of Construction personnel will monitor the Construction contingency line item to ensure no CO are approved that would deplete or result in a negative construction contingency balance. If the Construction contingency line item drops below 50% of the original construction contingency amount, the Project Coordinator and Assistant Project Coordinator should discuss this fact in the Job Conference and notify the Client Agency that CO will be impacted if funds are depleted. If the CO are proposed that will deplete the contingency, they cannot be approved or otherwise processed until funds are added to the project through the PCR process. The Regional Director of Construction starts a PCR in e-Builder to gain approval for the budget change. The PCR must account for sufficient funds to replenish not only the Construction Contingency but also to replenish the Professional CO Fee Contingency line item. The Construction Contingency funding level should be replenished to an adequate amount to finish the project based on the percentage of unfinished construction (all Primes) remaining. The Professional CO Fee Contingency should be the appropriate percentage of the Construction Contingency. The Client Agency Project Sponsor approves the PCR and provides additional funding either by LOC or by adjusting the agency's capital plan. If a Client Agency does not approve a PCR, the project may have to be suspended until the Client Agency provides appropriate funding or scope modifications. Once project funding or scope is adjusted to match anticipated project costs, the CO can be processed.

**Funds must be provided (approved by the Client Agency Comptroller and allocated to Construction Contingency by the DGS Fiscal Unit) before work can happen on the CO. Bureau of Construction personnel may NOT direct a contractor to proceed with any CO work if there is no funding in place at the time of the directive.**

If the Construction Contingency is depleted, the Regional Director must start a PCR process in e-Builder and the Client Agency must approve the PCR and provide sufficient funds to replenish not only the Construction Contingency but also to replenish the Professional CO Fee Contingency line item. The Construction Contingency funding level should be replenished to an adequate amount to finish the project based on the percentage of unfinished construction (all Primes) remaining. The Professional CO Fee Contingency should be the appropriate percentage of the Construction Contingency.

Design professionals receive fees on CO pursuant to the particular language in their Professional Agreement. These fees are paid from the Professional CO Fee Contingency line item. Any work orders issued or performed during the construction phase are paid to the design professional from the Budgeted Work Order line item. Services such as Commissioning, Construction Management or Utility Agreement Costs identified in the Forecast Tool during project setup are paid from Anticipated 3<sup>rd</sup> Party Costs. Any unanticipated Work Orders or 3<sup>rd</sup> Party Costs can only be paid from Design Contingency.

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<sup>5</sup> There is no specific line item in e-Builder to retain or bookmark liquidated damages.

Funds for construction shall be maintained in the construction invoice process pursuant to the applicable version of the General Conditions to pay for punch-list items as they are completed by each prime contractor. Retainage and punch-list items are paid from the specific prime contractor's line item.

If the Design Contingency line item is depleted during construction, the Regional Director of Construction will start the PCR and the Client Agency will approve the PCR and add sufficient funds to the project to pay for services and to replenish the design contingency to an appropriate level based on risk and duration remaining on the project. Depending upon the nature of the service that cannot be performed due to lack of funding, the project may have to be suspended until such time as funds are in place in e-Builder to resume service.

## **12. Project Funding – Post-Final Inspection**

Payments to the prime contractors based upon satisfactory completion of punch-list work shall be paid from the prime contractor's specific e-Builder line item. If one prime requests that Capital Programs withhold funds from another prime in accordance with the language of the General Conditions, the funds remain in the prime contractor's line item and may not be used to pay any invoice until the dispute/claim is resolved or settled.

Funds for the professional's 5% final payment are paid from the e-Builder Basic Services line item. Depending upon the language of the applicable Professional Agreement, the professional may be entitled to request a reduction of the final payment from 5% to 2.5% after Final Inspection. Only the Deputy Secretary can approve any request for reduction in the professional's final payment.

Upon completion of the last punch-list item, the contractor may submit a final invoice and the project enters the final close-out phase. Based upon the language in both the General Conditions and the Commonwealth Procurement Code, a contractor has 6 months after a claim accrues to request a claim conference. Typically, this means the contractor would have 6 months from receipt of the Bureau of Construction's final decision on the 100% Field Dispute Resolution (FDR) meeting. The Close-Out Process in e-Builder accounts for the last day of final inspection and freezes any activity on the project for 6 months from that last date. If no activity occurs and no claims are filed, the project proceeds to close-out.

Any funds remaining in any line item on the e-Builder Cost Module after the Final Invoice is paid are 'frozen' and unavailable to spend on anything except to settle construction contractor claims. Once the 6 months have expired and no claims are filed, any funds remaining from an LOC will be returned to the Client Agency. After those funds are returned, Capital Planning checks if any additional phases of work are planned for the next five years. If so, the balance is transferred to the future project; if not, all remaining funds are returned to the Office of Budget.