



## M E M O R A N D U M

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**Date:** January 25, 2024

**To:** California State Lottery Commission

**From:** Harjinder K. Shergill Chima, Director *HKC*

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Operations Division

**Subject:** Item 8(c) – Amendment to Add Funds to Z Squared Construction Agreement for Completion of the Northern Distribution Center (NDC) Remodel

### **ISSUE**

The California State Lottery (Lottery) seeks California State Lottery Commission (Commission) approval to add additional funds to the existing Agreement with Z Squared Construction (Z Squared) to complete the Northern Distribution Center Remodel Project (Project). The approval to add funds will require an additional \$1,156,265.00 (inclusive of a 10% contingency of \$105,115) raising the maximum authorized expenditure amount from \$5,770,910 to \$6,927,175.

### **BACKGROUND**

In 2022, the Lottery solicited an Invitation for Bid to provide construction services for completion of the Project. The Lottery executed an Agreement with Z Squared in the amount of \$5,777,910 (including a \$670,910 contingency) for the term of November 15, 2022 to November 4, 2024 with options to extend the Agreement for two (2) one-year periods.

The Project includes expanding a portion of the supply warehouse to support additional Pick and Pack stations for sales growth. This includes installation of the following: a new roof, heating, ventilation, air conditioning (HVAC) equipment to address health and safety issues, pallet racking to support storage of Lottery products, and upgrading the physical security system for the protection of Lottery assets and staff. The additional purpose of the Project is to modernize operations, secure assets and support the health and safety building occupants. Due to the critical sales and supply chain activities performed at the NDC, the building is required to remain fully operational during construction. This requires careful planning and consideration of phasing the Project through completion.

Full mobilization of the construction team on site commenced in April 2023, with an initial projected completion date of November 30, 2023. In May 2023, the Project completion date was extended to January 31, 2024.

## **DISCUSSION**

Within the first few months of Agreement commencement, Z Squared submitted a Bid Analysis of the Security System Scope to point out design omissions and other deficiencies with the physical security specifications provided at bid time. The Lottery found merit in their position and agreed with the analysis. These issues have resulted in increased costs, which were not originally anticipated, for the acquisition and installation of the security equipment.

Additional challenges arose causing cost increases and delays of the Project due to the Lottery's building security requirements and the necessity to remain fully operational during construction. These efforts required project phasing, which limited the contractor's ability to work in multiple areas simultaneously. This also required repeated mobilization/demobilization for the contractor and subcontracted trades, breaking their work into smaller portions and reducing their ability to scale up operations. Ultimately this led to an increase in costs as the contractors were not able to reduce overhead through economies of scale. The Lottery's Contractor also experienced supply chain issues with critical infrastructure to support the added electrical load, which resulted in higher than anticipated costs to obtain the necessary equipment.

The Project was also impacted by requirements for temporary heating and cooling necessary for continuous proper working climates for Lottery staff working at the NDC during the remodel. Other unforeseen expenses included requirements for equipment manufacturer changes (as earlier equipment was no longer available) and water damage on the roof deck which required replacement prior to the installation of the new roof and HVAC. To date, the Lottery has approved \$621,103 in change orders, leaving approximately \$49,807 of the original \$670,910 contingency.

At the request of the Lottery, Z Squared has provided a Rough Order of Magnitude (ROM), which is an estimate of the efforts and costs involved in completing the Project with inclusion of the physical security requirements. This ROM estimate came in at \$1,051,150. This amount includes approximately \$696,100 for the physical security scope of work (procurement and installation), temporary heating, and an extension of General Conditions, which are daily operational costs of \$1,902 to keep the contractor mobilized on site through Project completion. In accordance with the Agreement and Lottery Regulations, the contractor has competitively bid the physical security scope of work which is the bulk of the ROM estimate. Removing this would only require the Lottery to resolicit that scope of work and run that project separately later, and likely for increased costs.

The Lottery has reviewed the ROM and agrees with the estimates set forth. If the additional funding is not approved, it would significantly impact the Lottery's ability to complete the Project. This would negatively impact NDC operations and the ability to secure and distribute Lottery products to support the Lottery's mission to education.

### **RECOMMENDATION**

The Lottery recommends the Commission approve the amendment to the Lottery's Agreement with Z Squared to add additional funds in the amount of \$1,156,265 raising the total Agreement value of \$6,927,175 to complete the Project.