



Number: IL 4071.00

/s/ John F. Conrad
Assistant Secretary
Engineering and Regional Operations

Date: ~~July 13, 2007~~
Extended to: July 14, 2009

Inflation and Market Conditions Applied to Base Estimates

I. Introduction

A. Purpose:

This Instructional Letter provides guidance to region management, project managers, and project teams in applying inflation rates and determining market condition risks on all Washington State Department of Transportation construction projects. Guidelines for the use and reporting of Cost Estimated Validation Process (CEVP[®]) and Cost Risk Assessment (CRA) are included. In addition, data requirements for the Capital Program Management System (CPMS) are identified.

This Instructional Letter supports the principles and practices outlined in [Project Management Executive Order E 1032.00](#), dated July 1, 2005. Good cost estimating practices consider all factors such as keeping estimates current and up to date, as well as considering specialty services and/or proprietary items.

B. Background

In 2006, the Director of Environmental and Engineering Programs and the State Construction Engineer formed a team to address concerns about statewide treatment of inflation and market conditions. The team was tasked with developing recommendations for consistent treatment of inflation and market condition risks in CEVP[®] and CRA efforts in state construction projects. A secondary task was to develop recommendations for the use and reporting of CEVP[®] and CRA results. The team's recommendations take effect with the approval of this Instructional Letter.

C. Term

This Instructional Letter remains in effect for one year, or until rescinded in writing.

II. Rules

This Instructional Letter implements the following rules as recommended by the team:

A. Inflation and Market Conditions

1. Inflation Rates

Inflation rates for construction, right of way, and preliminary engineering to inflate Current Year (CY) Dollars to Year of Expenditure (YOE) Dollars must be estimated using CPMS inflation rate tables.

2. Market Conditions

Market conditions for a project may be influenced by several factors. The following factors must be documented and mitigation strategies proposed when preparing cost estimates if the project team determines the market condition is applicable to their project.

a. Bidding Environment and other Construction Market Conditions

- 1) Bidding environment refers to how the number of potential bidders for a project will impact the estimate for construction. The project team must document whether the project will be subject to a “non-competitive” bidding environment and develop mitigation strategies for this risk.

Current, up to date information regarding bidding environment and market conditions is located at: <http://www.wsdot.wa.gov/Projects/ProjectMgmt/RiskAssessment/workshop.htm>. The document, [*Common Assumptions*](#), contains this information.

- 2) Other market condition risks for construction are to be captured through the risk elicitation process. A well documented explanation must be provided that describes why the project is subject to additional market condition risks. Potential response strategies to mitigate these risks must be provided.

b. Right of Way Market Condition Risks

Right of way market condition risks must be obtained from subject matter experts in real estate services. The project team must document information that affects the project including

right of way, zoning, speculation, and other market condition risks that may be obtained from a variety of sources such as real estate services or planning. Comparable recent real estate transactions must be a primary source of right-of-way cost data.

c. Preliminary Engineering (PE) Market Condition risks

Preliminary engineering (PE) market condition risks must be identified and documented. Sources for characterization of the risk must be clearly stated in the documentation describing why this project is at risk (i.e., availability of skilled labor or specialty professional services).

B. Use and Reporting of CEVP®/CRA Results

Project teams must use 90 percent as the default percentile for reporting CEVP® and CRA results. Exceptions to this requirement must use the following approval process (see Attachment A):

1. Projects with an Executive Oversight Committee (EOC)
 - a. The Project Manager presents the results of the CEVP to the EOC along with a recommendation including supporting information on the confidence level to be included in management plans and budget.
 - b. The Secretary's Office makes final decisions.
2. Projects without an EOC:
 - a. Project managers will report the results of the CEVP® or CRA to region executive management and provide supporting information on the confidence level to be included in management plans and budgets.
 - b. Region executive management will decide what dollar amount to use for final decision making.

C. Documentation Requirements

Documentation needed to support the proposed budget level shall include:

1. A summary of the current base estimate.
2. A description of each significant risk or opportunity that has been identified, including potential impacts to the project cost and schedules.

3. A developed plan for managing each identified significant risk or opportunity.

D. Exceptions

Any exceptions to the above rules must undergo a Change Management Review process for approval by the Assistant Secretary for Engineering and Regional Operations.

E. CPMS Data Requirements

Project teams must provide specific data to the region program management office for inclusion into CPMS and the Transportation Executive Information System (TEIS). The required data is:

1. Project scheduling data for the following milestone dates:
 - Project definition completion date
 - Date for the beginning of preliminary engineering
 - Completion date for the environmental document
 - Start date for the acquisition of right of way
 - Date of right of way certification
 - Project advertisement date
 - Date project is operationally complete (substantially complete)
2. Estimated Project Cost Data (in Current Year Dollars, CY\$)
 - Date of estimate basis (i.e., “2007 \$”)
 - Design cost estimate
 - Right of way cost estimate
 - Construction cost estimate
3. CPMS will be modified to calculate the midpoint for construction phases using the project award date and the operationally complete date.

III. Contact Information

For information regarding this Instruction Letter, contact the Cost Risk Estimating Management Office at (360) 705-7452 or visit their Web site at: www.wsdot.wa.gov/Projects/ProjectMgmt/RiskAssessment/

IV. Definitions and References

A. Definitions

Inflation: *A Dictionary of Economics* defines inflation as a persistent tendency for prices and money wages to increase. Inflation is measured by the proportional changes over time in some appropriate price index. *Merriam-Webster* defines inflation as an increase in the volume of money and credit relative to available goods and services resulting in a continuing rise in the general price level.

Market Conditions: For the purposes of this Instructional Letter, market conditions are defined as the consequence of supply and demand factors which determine prices and quantities in a market economy and are separate from inflation. Market conditions may include competitive environments during bidding and contracting; the labor market; resource availability, etc.

CEVP[®]: Cost Estimated Validation Process. The process used to review cost estimates and assess risks for projects estimated to be over \$100 million.

CRA: Cost Risk Assessment. A Workshop Process used to review cost estimates and assess risks for projects estimated to cost \$25 million to \$100 million.

B. References

Project Management Online Guide

<http://www.wsdot.wa.gov/Projects/ProjectMgmt/>

WSDOT Guidelines for CRA CEVP Workshops

<http://www.wsdot.wa.gov/Projects/ProjectMgmt/RiskAssessment/workshop.htm>

Project Estimate Basis Form

<http://www.wsdot.wa.gov/Projects/ProjectMgmt/RiskAssessment/workshop.htm>

CPMS Construction Inflation Table

<http://wwi.wsdot.wa.gov/ppsc/pgmmgt/cpms/fields/cci.txt>

CPMS Right of Way Inflation Table

<http://wwi.wsdot.wa.gov/ppsc/pgmmgt/cpms/fields/RW.infl.txt>

CPMS Preliminary Engineering Inflation Table

<http://wwi.wsdot.wa.gov/ppsc/pgmmgt/cpms/fields/pe.infl.txt>

Common Assumptions

<http://www.wsdot.wa.gov/Projects/ProjectMgmt/RiskAssessment/workshop.htm>

Proposed Statement on Inflation Rates

See [Attachment B](#), Statement on Inflation Rates

[Attachment A](#), Flowchart of the Approval Process for Using a Percentile Less Than 90 Percent

Available Training

Introduction to Cost Estimating – Course Code CZV

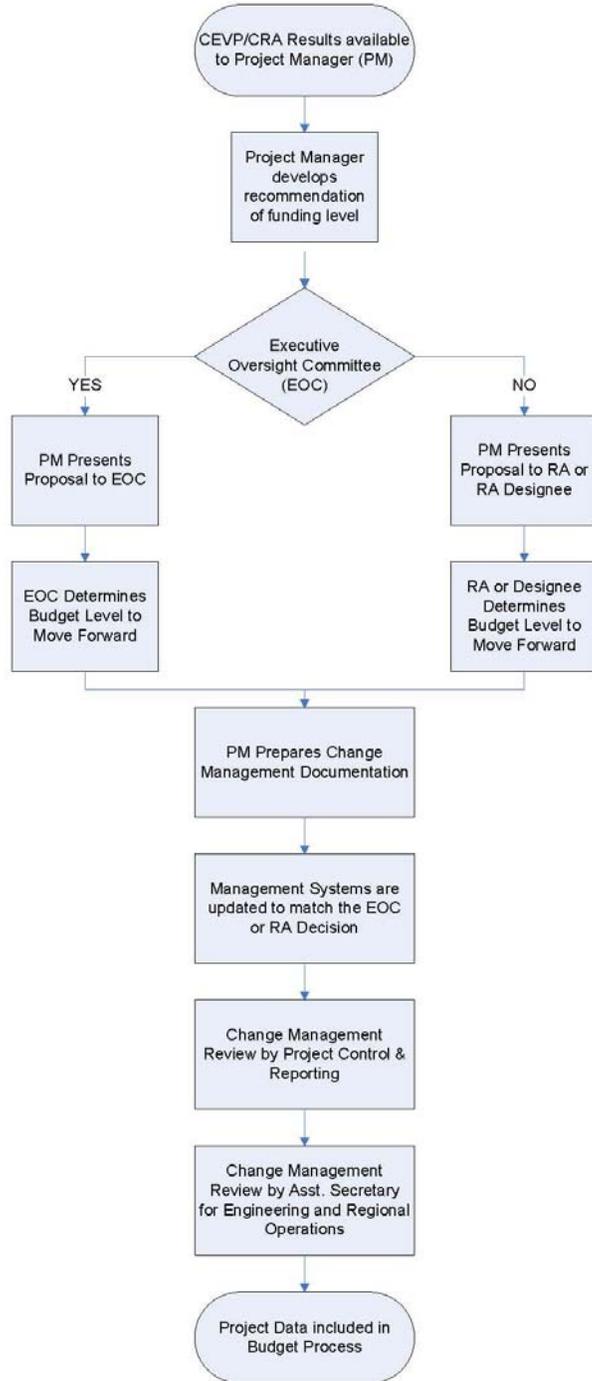


Americans with Disabilities Act (ADA) Information

Materials can be provided in alternative formats for people with disabilities by calling:

- Office of Equal Opportunity (OEO) at (360) 705-7097.
- Persons who are deaf, hard of hearing, or speech disabled may contact OEO through the Washington Relay Service at 7-1-1.

Approval Process for Using a Percentile Less Than 90 Percent



**Washington State Department of Transportation
Statement on Inflation Rates**

WSDOT requires the use of CPMS inflation tables posted at the time of the estimate. The projections in the inflation tables are provided by Global Insights and are to be used to forecast Year of Expenditure (YOE) costs. Global Insights is recognized as a leader in economic financial analysis and forecasting. Their forecasts are employed by governmental agencies and private companies around the world.

The Statewide Programming Office receives project estimates in Current Year (CY) Dollars and inflates project estimates to YOE using the inflation tables posted in CPMS. Model forecasts prepared following CRA and CEVP workshops will also use the CPMS inflation tables. It is important that the most current CPMS tables are used and the date of these tables well documented.

It is not within the scope of activity for project estimators or the participants at CRA and CEVP workshops to unilaterally establish inflation forecasts. Therefore, the discussion of inflation and uncertainty is not an effective use of time at CRA and CEVP workshops. The responsibility of inflation rates rests with the Statewide Programming Office and the rates to be used are those posted in CPMS at the time of the estimate.

Liberal use of market condition risks creating a "range" of inflation rates is not to be used. Workshops need not discuss inflation rates and should focus on areas of respective expertise for the project.