



Memorandum

19 West Flagler Street ♦ Suite 220 ♦ Miami, Florida 33130
Phone: (305) 375-1946 ♦ Fax: (305) 579-2656
visit our website at www.miamidadeig.org

To: The Honorable Carlos Alvarez, Mayor, Miami-Dade County
The Honorable Chairman Bruno A. Barreiro
and Members, Board of County Commissioners, Miami-Dade County

From: Christopher R. Mazzella, Inspector General

Date: May 12, 2008

Subject: Memorandum of OIG Observations, Review and Comments on the *Proposed Amended and Restated Terminal Agreement between Miami-Dade County and Seaboard Marine Ltd.* Ref. IG07-74

As part of the Miami-Dade Office of the Inspector General's (OIG) continuing oversight of Seaport Department (Seaport) operations, the OIG has been monitoring the contract negotiations process and reviewing the current and proposed agreements with the current terminal operators (Operators) serving the Port of Miami (POM). The three Operators serving the POM are Maersk, Inc. (Maersk), Port of Miami Terminal Operating Company, L.C. (POMTOC) and Seaboard Marine, Ltd. (Seaboard).

This memorandum sets forth the OIG's observations and comments with respect to the proposed Seaboard agreement only (see May 14, 2008, Transit Committee Agenda Item No. 3P). These concerns are not new, as the OIG has been providing comments on the proposed agreements throughout the period of negotiations. The OIG, however, wanted to wait on the finalized proposed amended agreement prior to publicly issuing its comments.

Further, the OIG would like to express gratitude to the Seaport and the Operators for their cooperation and assistance during this process. In particular, the Seaport ensured that the OIG was kept informed of all meetings, provided copies of correspondence and documentation, and in general provided orientation and information on cargo terminal operations.

BACKGROUND

In July 2007, the Seaport Director advised the OIG that the Seaport was about to begin terminal operating negotiations with the Operators at the POM. Due to complexity of simultaneous negotiations with the Operators and the future implications of any or all of those agreements, the Seaport Director requested that the OIG observe and comment on the negotiation processes.

Since that time, OIG activities have included attendance at all scheduled negotiation meetings with the Operators; review of all existing terminal operating contracts and their amendments, if any, Port tariff, historical statistical and financial data, current financial data, and two independent studies of POM operations.¹ OIG staff also made numerous site visits to observe cargo operations and facility conditions. Meetings and interviews were held with various Seaport staff members representing the Administration, Finance, Maritime, and Marketing divisions.

On November 13, 2007, the OIG issued a memorandum to the Seaport Director on the *Oversight of Seaport Terminal Operator Lease Agreement Negotiations* that provided our initial comments on the negotiations process with emphasis on areas of concern that were either the subject of negotiations or areas that, we believed, should be included in the negotiations. That memorandum discussed the subject areas of: the Seaport's Strategic Plan, Synchronizing Future Contract Renewal/Expiration Dates, Cargo Contract Revenue Projections, Subletting, and Accounts Receivables – Arrearages.

On December 14, 2007, the Seaport Director provided responses to issues raised in the aforementioned OIG memorandum, and shortly thereafter, OIG staff met with the Seaport Director and his staff to go over the comments more thoroughly. As negotiations continued, the OIG issued additional comments to the Seaport Director. Among the other issues surfaced were the contract renewal options and electrical surcharges.

On April 11, 2008, the OIG issued essentially this memorandum in draft format to the Seaport Director for review and comment. On April 22, 2008, an addendum to the original OIG draft memorandum was issued due to the discovery of an outstanding item that is directly related to Seaboard (included in this memorandum under the subject heading CRIMINAL VIOLATION, page 11).

On April 25, 2008, the Seaport Director responded to the original draft memorandum. On May 6, 2008, the Seaport Director responded to the addendum. (Responses attached as A and B, respectively.) We have carefully taken the Seaport's responses into consideration. Revisions to our initial memorandum were made, where appropriate. The following "final" memorandum discussed the amended agreement, as it is proposed for the upcoming May 14th TC Agenda, Item 3P.

SUMMARY OPINION

The OIG believes that certain major provisions contained in Amended and Restated Agreement (Agreement) are not in the best interest for the future growth and development of all the stakeholders in the Port of Miami. The opinion of the OIG is based on three major areas of concern, summarized as follows:

¹ *Port of Miami Tariff Analysis*, Planning and Economics Group, May 24, 2006, and *Port of Miami Cargo Terminal Capacity Analysis*, TranSystems, October 26, 2007.

1. **CONTRACT TERM** – The OIG could not find any sound economic or financial reasons for proposing an initial term of 20 years with two unilateral 5-year renewal options, making this a potentially 30-year unilateral agreement.
2. **CAPITAL IMPROVEMENTS** – Both the Seaport and Seaboard agree on the less-than-acceptable condition of the Seaboard terminal yard and the failure of the Seaport to complete certain improvements required under the present agreement, however, the OIG is concerned that the Seaport may be committing to fund improvement projects that it may not be able to afford and may not be able to adequately manage and complete within the required time frames.
3. **FINANCIAL TERMS** – While the financial terms of proposed Agreement significantly increases the near-term revenues, the OIG is concerned that such increases might not be sufficient to offset current operating expenditures and debt requirements and still provide funding to support additional debt, as required by this Agreement.

1998 AGREEMENT WITH SEABOARD MARINE LTD.

On November 18, 1998, Miami-Dade County entered into the current agreement with Seaboard for terminal operations at the POM. This agreement provided an initial term of 10-years with two 5-year options with mutual consent and subject to renegotiations as part of any renewal. The initial term will be completed on November 17, 2008. It is under the requirements of this first renewal option that this Agreement is being presented to the Miami-Dade County Board of County Commissioners (BCC) for consideration and approval.

At present, Seaboard operates from a terminal yard consisting of approximately 75 acres; the yard includes 14.16 acres that are sub-leased from POMTOC.² Seaboard does not pay rent to the County for use of approximately 61 acres of land. Instead, Seaboard pays a negotiated TEU³ rate that is intended to cover the costs for dockage, wharfage with no separate charge for land; other items, such as vehicles and break bulk cargo are paid at negotiated or Tariff rates.

² Exception: At present, Seaboard pays POMTOC the rate of \$0.28 per square foot for the 14.16 acres. This amount is to be included in the monthly rent payments made by POMTOC to the Seaport according to the terms of POMTOC lease agreement.

³ TEU means Twenty Foot Equivalent Unit and is the standard measure for cargo shipping containers, e.g., a 40-foot container counts as 2 TEUs.

AREAS OF MAJOR CONCERN

1. CONTRACT TERM – 20 YEARS PLUS TWO 5-YEAR OPTIONS

The Agreement provides for an initial term expiring on September 30, 2028 (20 years) with two renewals of 5-years each at the option of the Seaboard. This provision gives Seaboard the right to continue terminal operations for an uninterrupted period of 30 years, notwithstanding the reappraised rental value of the land, the achievement of certain pre-defined performance thresholds, and compliance with other contractual requirements. During this 30-year period, the Seaport cannot require Seaboard to negotiate any changes to the Agreement that maybe necessary and in the best interest of the Seaport or Miami-Dade County. The OIG believes that the structure of this 30-year agreement (initial 20-year term and the two 5-year options) are not in the best interest of the Seaport.

Our position is substantiated by the repeated comments of the Director with respect to the POMTOC agreement that because of POMTOC's unilateral renew options, ("POMTOC shall have the right to renew this Agreement for each of the 3 additional five-year renewal periods ...") he will have to wait 7 years until after the expiration of the current and final renewals before the Seaport may require POMTOC enter into any negotiations. The proposed language of this amendment, which significantly changes the current agreement's requirement of mutual consent, would place the Seaport in a similar position that it finds itself with POMTOC. If the Agreement is approved with this provision, the Seaport would not be able to require renegotiation of any contract provision until the termination of the entire Agreement in the year 2038. The Agreement will tie the hands of all future directors for the next 30 years (or in the best case scenario for only 20 years) regardless of international, national, or local economic conditions.

Additionally, there are two major projects⁴ that are designed to provide significantly increased benefits to the POM and are expected to be completed within the next ten years, by the year 2018. The viability and competitiveness of the POM is expected to significantly improve following the completion of these projects and it would then appear to be an appropriate time to review all terminal operating contracts.

Finally, the duration for the Agreement should consider the value of any infrastructure investments to be made by Seaboard with a reasonable amount of time for them to depreciate or recapture the cost of those investments. Seaboard's initial capital contribution of \$1.150 million does not, in our opinion, justify a 30-year agreement, or even a 20-year agreement for that matter. Even taking into accounts the five phased capital payments of \$1 million each, discussed in the next section below, we still do not believe that these contributions in conjunction with the proposed land and TEU rates warrant an initial 20-year uninterrupted term, with the unilateral option on another 10 year.

⁴ The two projects are identified as the "Port of Miami Tunnel" and "Dredging to 50 foot depth."

In his April 25, 2008 response (Attachment A), the Seaport Director states that:

POM was amenable to a contract of 30 years length (inclusive of options) for two principal reasons: 1) Seaboard has offered long-term financial and cargo throughput guarantees that greatly exceed any found within the South Florida market; and 2) Seaboard has consented to being on Tariff excepting certain specific charges. These two conditions – along with contractual protections against inflation, a run-up in port land values and poor financial performance on Seaboard’s part – leave future port directors in a much stronger (an more flexible) position to absorb financial challenges than we find ourselves today.

It is true that the proposed throughput guarantee of 4,000 TEUs per acre may exceed any other guarantee found in the South Florida market, however 4,000 TEUs per acre is only approximately 80% of its historic averages. Second, the majority of Seaboard’s cargo operation will be subject to the land and TEU agreed rates, subject only to formula increases. In fact, only limited categories, such as break bulk (i.e. palletized cargo) and automobiles are subject to Seaport tariff. The OIG believes that these two reasons do not warrant 30 years.

The OIG is pleased that the Seaport is proposing a long-term business partnership with a company that has maintained its headquarters in Miami-Dade County (Medley) for the past 25-years. Seaboard is the largest user of the POM with more than 70 sailings per month, moving more cargo to and from the POM than any other carrier. It is estimated that Seaboard’s operations has an estimated annual economic impact of \$16 billion.

The OIG is not against a long-term agreement. The OIG, however, believes that for any long-term agreement to be successful, certain ingredients are necessary, such as the ability of each of the partners to be able to adjust business plans or renegotiate contract terms as may be required by international or global conditions. Partners in long-term agreements with the mutual options to extend the relationship provide the opportunity for continuation. In the case of Seaboard, it has assurances that the Seaport would not arbitrarily seek bids from other potential operators at the end of the initial period. On the other hand, while the Agreement provides for formula increases to be paid to the Seaport in each year of the Agreement through the entire 30-year period, there isn’t any assurance that such formula would be still relevant 10, 20, or 30 years in the future. A mutual agreeable renewal option provides protection to both partners.

We believe that for all terminal operating agreements, the Seaport must retain the mutually agreeable renewal option that would place the POM in a more favorable position to plan for growth and development.

2. CAPITAL IMPROVEMENTS –PAVING AND DRAINAGE

The OIG is concerned about both the Seaport's ability to fund all the proposed capital commitments and their ability to adequately manage the implementation and completion of those projects.

In the proposed Agreement, the Seaport is committing up to \$21 million to complete approximately 62 acres of paving maintenance and upgrades and RTG runways within five phased areas by September 2013, as outlined in Exhibit E of the Agreement. In return, Seaboard is committing to make a \$1 million contribution after the timely completion of each of the five scheduled phases. Seaboard's total contribution would be up to \$5,000,000 with penalty reductions of \$100,000 for each month any of the phases are delayed. Should the Seaport still not complete the improvements, as was the case in the current agreement, Seaboard would not be required to make any contributions; additional penalties in the form of rent reductions, would also be imposed.

While the penalties for delays in completing these improvements may appear harsh, the OIG notes that during negotiations, both parties readily agreed, without hesitation, on the sub-standard condition of the Seaboard terminal area and the failure of the Seaport to have completed many of the proposed improvements that were required under the current contract. Thus, Seaboard's contribution of up to \$5 million may be viewed as a generous contribution to reward the Seaport for completing improvement projects, which it failed to complete the first time around.

Although the OIG concurs with both the Seaport and Seaboard that the identified improvement projects are a high priority to bring the terminal yard up to minimum standards, the OIG has severe reservations about the Seaport's ability to manage and fund these projects due to the following considerations:

- In the 10 years since the signing of the current agreement, the Seaport has completed only one of nine projects identified in the contract; none of the remaining eight projects were even started. All these projects were to have been completed by March 2000. Seven of the remaining projects were for re-grading, paving, and drainage of the terminal yard that are now being carried forward to the new agreement.
- Negotiations with other Operators may include similar type terminal improvements with Seaport funding contributions and project management requirements, which may impact the Seaport's ability to complete these projects timely.
- Two proposed mega-projects (the dredging of the POM South Channel to depth of 50 feet and the Port tunnel) will be competing for funds, which may impact the Seaport's ability to borrow additional Sunshine State Loans, and/or impact current abilities to satisfy debt obligations.

The Seaport has stated that funding for these projects are expected to come from future Sunshine State Loans and available State of Florida grants. However, the OIG is reminded of its earlier audit of the Miami Seaport Redevelopment Program (MSRP) and the various construction manager at-risk agreements encompassing a variety of cargo terminal yard improvement projects.⁵ In summary, we found an alarming number of improvement projects being cancelled in an effort to keep the overall CM contract within budget. These cancelled projects, however, were budgeted in many of the associated “borrowings” and, thus, we questioned the department’s ability to budget and “pay” for them again. Should the BCC approve this Agreement as proposed, it should be with the mandate that the Seaport devote such resources to ensure that the experiences of the MSRP do not recur.

In his response of April 25, 2008, the Seaport Director states that:

Our five-year financial and capital funding plan is readily available; it shows our strategy for financing approximately \$200 million in capital improvements, including those associated with three contracts that are bound for the Board of County Commissioners in the coming months. Each of these agreements guarantees revenues beyond those required to finance any contractually obligated commitment.

While the OIG sincerely hopes that that is the case, we have not been provided with any assurances that the Seaport’s current and projected operating deficits, debt service, and any other financial obligations would not significantly erode the increased revenues from the land rent. This is particularly significant since the Seaport has been losing other revenues (wharfage, dockage, and crane) due to the overall cargo volume decrease in each of the past 2 years (-8.7% and -9.4%, respectively) and the concerns about rising security costs.

3. FINANCIAL TERMS - REVENUE ANALYSIS⁶

An OIG analysis of the major fiscal terms (Land Rent⁷ and TEU Rate⁸) of the proposed Agreement projects an annual revenue increase of \$3.613 million due almost entirely to the first time imposition of a \$1.00 per square foot charge for 81.91 acres. The revenues from cargo volume would increase marginally based on a projected volume of 360,000 TEUs. The summary result for the first year is shown on the next page:

⁵ “Final Audit Report of the Cargo and Cruise Project of the Miami Seaport Redevelopment Project (MSRP) at the Miami-Dade County Seaport”, issued by the OIG on August 11, 2004.

⁶ The analysis considers only land rent and TEU rate because all other revenue sources will for the most part remain the same and is not expected to have any significant impact on projections.

⁷ Currently, Seaboard does not pay land rent. Consideration for land rent is included in a TEU charge.

⁸ TEU Rate is the negotiated amount that includes consideration for land rent, dockage, and wharfage that is charged for each container loaded or unloaded from a vessel.

	\$x000,000			
	Current	Proposed	Inc/(Dec)	%chg
TEU	\$7.590	\$7.635	\$0.045	0.6%
Land	0.000	3.568	3.568	n/a
	<u>\$7.590</u>	<u>\$11.203</u>	<u>\$3.613</u>	<u>47.6%</u>

While we acknowledge that the agreement positively affects Seaport revenues, we are reminded of its consultant's financial report, which recommends, in part, that: *"If the lease is awarded through negotiation, presumably with an existing tenant, it is recommended that the Port agree to the lease only if it funds the Port's expenses shown above."*⁹ (Table from report not included.)

This 2006 report indicated that in Fiscal Year 2004, total expenses to support the cargo operations averaged \$180,542 per acre; revenue from Seaboard was \$80,852 per acre less (not including gantry cranes). While these cost figures have not been updated, the OIG is concerned that the Seaport's own projected revenues of \$158,710 per acre will not be sufficient to offset current expenses, much less fund the improvements mentioned earlier.

At this point, the OIG would also like to point out that on page 3 of the County Manager's memorandum regarding this Agreement, in reference to the land rental rate, states that "This rate shall escalate up to 3% compounded yearly..." However, in the actual Agreement on page 14, Section 5A Land Rent it states that "subject to an annual increase of not more than three percent (3%) ..." Even the language in the Agreement is ambiguous in that there is no determinant as to what will cause an increase or determine the amount of the increase.

OTHER AREAS OF CONCERN

EFFICIENT USE OF LIMITED TERMINAL AREAS – MINIMUM ANNUAL GUARANTEE TEU (MAGT) – AN OIG CONCERN IMPACTING THE SEAPORT'S OTHER TERMINAL AGREEMENTS

The OIG makes the following comment relative to the two other terminal operating agreements that are in contemplation of being amended, renegotiated, etc.

Due to the limited land space available for cargo operations at the Port of Miami, the Seaport is strongly encouraged to negotiate meaningful productivity measures to ensure that all cargo terminal operators increase the productivity in their allocated terminal area. Simply stated, this means that all cargo operators must be required to achieve higher minimum guarantees for their through-put per acre. Consequently, if operators are not able to achieve the required productivity measures for allocated land, then land would be reduced until the minimum throughput measure is achieved.

⁹ *Port of Miami Tariff Analysis – Final Report*, Planning and Economics Group, Inc., May 24, 2006

Both Seaboard and the Seaport are to be commended for attempting to set higher standards for the utilization of limited acreage. The proposed Agreement with Seaboard sets the MAGT at 4,000 TEUs per acre with a projected annual volume of 5,538 TEUs per acre (based on total volume of 360,000 TEUs). In comparison, under the current agreement, the MAGT for FY 2007-08 is 2,000 TEUs per acre and would have been 3,300 TEUs per acre had the Seaport completed the required improvements. The MAGT of 4,000 TEUs per acre was offered by Seaboard despite the sub-standard land and without the benefit of RTGs.

This MAGT of 4,000 TEUs per acre, without the benefit of RTGs, should now be considered the minimum standard when negotiating with other terminal operators. The 4,000 TEU minimum should be further increased if the Seaport is to be required to invest in infrastructure enhancements to accommodate RTGs.

The OIG has difficulty understanding the Seaport's strategy or the economic reality of having one terminal operator guarantee 4,000 TEUs per acre on substandard land while others are permitted to provide anywhere from 2,000 to 3,000 TEUs per acres.¹⁰ Using the Seaport's own model, a cargo terminal operator with a proposed minimum throughput guarantee of 2,750 TEUs per acre would have until the year 2026 (18 years) before they would be required to have the same throughput rate guaranteed by another provider, today.

ARREARAGES

On November 13, 2007, the OIG advised the Seaport that its own financial report, as of 10/24/07, entitled *Analysis of Outstanding Customer Balances*, reported that Seaboard had an outstanding balance of \$807,005.33 (including late payment charges) that was in excess of 90-days, with many charges going as far back as 1997. At that time, the OIG reminded the Seaport of Miami-Dade County Administrative Order (A.O.) 3-29 *Prohibiting County Contracting with Individuals and Entities Who are in Arrears to the County*. A.O. 3-29 states in part:

This Administrative Order prohibits contractors that are in arrears to the County in excess of the enforcement threshold^[11] from obtaining new County contracts, extensions of contracts, or new purchase orders, until such time as the arrearage has been paid in full or the County has agreed in writing to an approved payment plan.

¹⁰ The Seaport Director's response of April 25, 2008 states "POM is confident that it understands the natural growth trajectories of cargo, the underlying economic realities of terminal land utilization rates, and the important peculiarity of being located at the tip of a peninsula. In constructing our contract models, we took into consideration these factors, having been supported in our efforts by a leading cargo consulting firm."

¹¹ "Enforcement Threshold" shall mean any arrearage under any individual contract, final non-appealable judgment or lien with Miami-Dade County that exceeds \$25,000 and has been delinquent for greater than 180 days.

Even absent the requirements of A.O. 3-29, the OIG strongly believes that as a prerequisite to good faith contract negotiations, all debts to the County should be paid. Our concerns were shared with the Seaport.

Most recent data indicates that \$200,132 of the outstanding receivables occurred between 1997 and 1999, of which \$96,451 pre-dates the current agreement. The annual receivables recorded from 1997 to 2007 are shown below.

Seaboard Outstanding Receivables 1997 to 2007 (Not including Interest Calculations)									
<i>Total</i>	<i>2007</i>	<i>2006</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>	<i>2001</i>	<i>2000</i>	<i>1997-99</i>
\$973,224	\$409,658	\$113,289	\$132,186	\$62,453	\$6,701	\$14,471	\$29,153	\$5,181	\$200,132

A review of the information relating to these receivables indicate that a large portion of the more recent receivables relate to the disputed methodology of counting “flat racks” for billing purposes, which we are glad to see has been clarified in the proposed agreement. However, the Seaport’s documentation for the remaining receivables were either scant or non-existent. Over the past 10 years, efforts by the Seaport’s Finance Department to collect or resolve outstanding receivables have either been non-existent or ineffective as evidenced by the increasing age and magnitude of the receivables.

In an effort to conclude negotiations, Seaboard offered a one-time payment of \$500,000 to settle all outstanding receivables up to December 31, 2007. This settlement represents \$0.51 per \$1.00 for the outstanding amount between 1997 and 2007.

The OIG is concerned that had it not been for our intervention, these outstanding receivables might have remained unresolved. The OIG recommended to the Seaport that it review their collection processes and make changes as necessary to ensure that all invoices and outstanding balances be resolved on a timely basis. Further, with the understanding that there may be other accounts in a similar situation, the OIG is strongly recommending that Seaport consider implementing a system so that the supporting documentation for all open, disputed, or unpaid invoices remain in a current filing system rather than being sent to storage at the end of the fiscal year. In doing so, the Seaport would have all necessary documentation readily available to ensure effective collection or resolution of all receivables.

Moreover, given the initial 20-year uninterrupted contract term, as discussed above, the OIG feels strongly that there must be a mechanism or protocol in place to ensure that arrearages are dealt with timely. The Seaport and Seaboard have agreed to create a joint accounts receivable committee to review this account on a bi-monthly basis. We surely hope that this actually occurs, and we do not find ourselves with a substantial delinquency at the end of 20 years.

CRIMINAL VIOLATION

Subsequent to our draft memorandum of April 11, 2007, the OIG discovered that in 2005, Seaboard was sentenced for criminal violations relating to the transportation of hazardous materials over public highways.¹² As part of the sentence, Seaboard was placed on criminal probation for a period of three (3) years and required to pay significant amounts in large monetary payments in fines, restitution, and clean-up costs. This information is contained in a press release from the United States Department of Transportation – Office of the Inspector General, dated May 05, 2005, titled *Seaboard Marine Sentenced for Criminal Violations*. According to the information contained in the press release, Seaboard was convicted for improperly transporting hazardous materials over public highways, which included two (2) stops, traveling back and forth between its terminal yard at the Port of Miami and other locations. From the sentencing information, it appeared that Seaboard was still on criminal probation during the negotiation process.

On Monday, April 14, 2008, the OIG presented copies of this press release to the Seaport negotiating team to determine what impact it may have on Seaboard operations or on the negotiation process. The Seaport negotiating team stated that they were not aware of this issue, nor were they aware that Seaboard was convicted and sentenced for acts that were, in part, committed on Port of Miami property. Neither were they aware of the Seaboard probationary requirements or compliance status.

On Friday, April 18, 2008, during negotiations, the OIG raised this issue with the Seaboard representative and requested further information. Among the information requested was proof that the fines were paid (\$305,000 in aggregate) and that Seaboard is in compliance with the terms and conditions of the criminal probation. We subsequently received documentation from Seaboard demonstrating its compliance and showing that it was granted early termination of its probation, one month earlier, effective March 24, 2008.

As the OIG was very concerned that that this matter was previously unknown, we posed several questions to the Seaport in an addendum to our April 11th memorandum. In his response of May 6, 2008, (Attachment B) the Seaport Director stated that "...under the terms of the existing agreement between Seaboard and the County, and to the best of our knowledge, Seaboard is not obligated to notify the County of such a conviction..." He further points out that "... the agreement provides for the operator to indemnify the County for any actions caused by them." However, it is the opinion of the OIG that the Seaport strongly consider the inclusion of such a requirement whereby all tenants and operators on POM property be obligated to advise the Seaport whenever there are potential dangers due to environmental issues or wherever not prohibited by law, the initiation of any investigation pursuant to applicable environmental laws and of the findings of any such investigations. For that matter, we believe such a requirement should be in all County contracts. Under separate cover to the County Attorney, the OIG is recommending that such language, as may be necessary, be developed and included in

¹² Case No. 04-20455-CR-GOLD/SIMONTON

all future renewals, agreements, etc. requiring the vendors to notify the County when they have been charged or convicted with any crime.

The OIG is concerned that had the OIG not made this discovery and that if this Agreement been brought forward for approval, as originally scheduled, the Board of County Commissioners would unwittingly have been considering an agreement with an entity that was convicted of criminal charges and would have been on criminal probation while the renewal was being considered.

Cc: George M. Burgess, County Manager
Robert A. Cuevas, Jr., County Attorney
Ysela Llort, Assistant County Manager
Bill Johnson, Director, Miami-Dade Seaport Department
Denis Morales, Mayor's Chief of Staff
Charles Anderson, Commission Auditor
Clerk of the Board (copy filed)

Attachments

Memorandum



DATE: April 25, 2008

TO: Christopher R. Mazzella
Inspector General

FROM: Bill Johnson
Port Director

SUBJECT: Response to OIG Draft Memorandum IG07-74 of Observations, Review and Comments on the Proposed Amended and Restated Terminal Agreement between Miami-Dade County and Seaboard Marine, Ltd.

On April 11, 2008, the Office of the Inspector General (OIG) issued Draft Memorandum IG07-74 concerning a proposed amended and restated cargo terminal operating agreement between Miami-Dade County, specifically the Port of Miami (POM) and Seaboard Marine Ltd. The OIG's memorandum presented three principal concerns and several minor ones. This memorandum serves to address the OIG's concerns and is intended to be included within the OIG's final report.

ISSUES/RESPONSES

Issue 1: Contract Term - The OIG could not find any sound economic or financial reason for proposing an initial term of 20 years nor a 30-year non-negotiable agreement with Seaboard.

Response: POM has conducted significant research into the customary lengths of cargo terminal operating agreements, finding that long-term contracts like the one proposed for Seaboard fall well within the industry norm. (Upon request, POM will provide its research to the OIG.)

POM was amenable to a contract of 30 years length (inclusive of options) for two principal reasons: 1) Seaboard has offered long-term financial and cargo throughput guarantees that greatly exceed any found within the South Florida market; and 2) Seaboard has consented to being on Tariff excepting certain specific charges. These two conditions - along with contractual protections against inflation, a run-up in port land values and poor financial performance on Seaboard's part - leave future port directors in a much stronger (and more flexible) position to absorb financial challenges than we find ourselves today.

APPENDIX A

Mr. Christopher Mazzella, Inspector General
Response to OIG Draft Memorandum IG07-74
April 25, 2008
Page 2 of 4

In terms of revenues, POM expects actual revenues from Seaboard to increase 40+% in the first year of this agreement, and guaranteed revenues to triple. A shorter term agreement may have been possible, but not at these revenue levels. Seaboard is a very valuable and not readily replaceable community asset; we are happy to have their long-term commitment to POM and our local economy.

Issue 2: Capital Improvements - Both the POM and Seaboard agree on the less-than-acceptable condition of the Seaboard terminal yard and the failure of the POM to complete certain improvements required under the present agreement. However, the OIG is concerned that the POM may be committing to fund improvement projects that it may not be able to afford and also the ability of the POM to adequately manage such projects.

Response: The OIG's concern that POM may not be able to fund all its future capital commitments is an important one, but this concern needs to be taken somewhat apart from the proposed Seaboard agreement. The Seaboard agreement (re-)commits POM to making improvements to its infrastructure, but under the protection of a \$26 million cap. The Seaboard agreement was designed to financially accommodate this commitment and to produce substantial new net revenues to POM.

The broader capital funding concern is fundamental to POM's future and, for that matter, to the future of most landlord ports and other governmental operations that are infrastructure-intensive. Long-term capital needs, as a matter of course, outstrip resources. However, there is an important distinction to be made between "needs" and "commitments." While POM has tremendous capital needs, POM has committed only to those projects for which it has a funding strategy. Our five-year financial and capital funding plan is readily available; it shows our strategy for financing approximately \$200 million in needed capital improvements, including those associated with three contracts that are bound for the Board of County Commissioners in the coming months. Each of these agreements guarantees revenues beyond those required to finance any contractually obligated capital commitment.

Sitting just outside of our five-year financial plan are two important projects: one involves POM's commitment to funding a portion of a tunnel, while the other involves a potential deep-dredge project. The Draft Memorandum inadvertently overstated POM's financial commitment to the tunnel as being \$257.7 million; POM's actual commitment ranges from a low of \$43.5 million to a maximum of \$143.5 million. At the low end of the commitment, POM intends to fund its obligation within its normal growth, as we quite typically take on \$50 to \$60 million annually in capital improvements. On the high end of our funding commitment, we may require a toll or other similar access charge to support our

Mr. Christopher Mazzella, Inspector General
Response to OIG Draft Memorandum IG07-74
April 25, 2008
Page 3 of 4

obligation. Various financing schemes have been worked out and presented to the Board concerning the tunnel. The Finance Department or my staff can walk your staff through them at your convenience.

With regards to future dredging, the OIG report inadvertently noted that the Water Resources Development Act (WRDA) approved funding of \$64 million for dredging POM's South Channel to 50-foot depth. No such funding was committed, as WRDA is an authorizing bill and not an appropriations bill. Neither the federal government nor POM is presently committed to fund, in whole or in part, this project.

Providing funding for dredging projects has long been a challenge for port directors. Typically, these projects are of such a financial scope that they require federal and state grants, in addition to a large local funding commitment. POM does not intend to commit to future dredging projects (or other capital projects, for that matter) in advance of developing adequate funding plans.

Managing capital planning over a long-term horizon is a dynamic process, whereby unending needs are only slowly accepted as funding commitments. Although we cannot definitively answer today how we will piece together future funding for projects like the deep-dredge, we can tell you that we are purposefully advancing contracts to the Board that are stripped of many of the financially limiting provisions of our existing contracts, and that are positioned to help absorb extraordinary cost increases.

Issue 3: Financial Terms – While the financial terms of the proposed agreement significantly increases the near-term revenues, the OIG is concerned that it is almost entirely due to the new land rent component with no requirement for capacity growth.

Response: The substantial revenue increase to POM linked to a new and significant Seaboard land rent obligation was by design, not accident. Adding a substantial land rent component to terminal operating agreements not only provides much needed guaranteed revenues to POM, it puts in place the proper economic incentive for private operators to maximize land productivity. We consider traditional terminal operating agreements with low land rents to be antiquated and counter-productive, as the intentional undervaluing of land assets encourages "land banking."

Though it is not readily apparent to someone outside the port industry, the \$10 per TEU increase to Seaboard is of little or no consequence to the competitive position of either POM or Seaboard. While the \$10 represents a 40% increase in revenues paid by Seaboard to POM, it represents in the range of 1% of the

Mr. Christopher Mazzella, Inspector General
Response to OIG Draft Memorandum IG07-74
April 25, 2008
Page 4 of 4

charge incurred by a Seaboard customer in getting goods to their new market. A \$10 increase to a discretionary customer or shipping line (e.g., POMTOC customers that pay Tariff rates) would, however, have a detrimental effect on our competitiveness with other South Florida ports.

Other Issues: The OIG raised other concerns about increasing land utilization rates and about settling Seaboard arrearages prior to taking the proposed contract to the Board.

Response: POM is confident that it understands the natural growth trajectories of cargo, the underlying economic realities of terminal land utilization rates, and the important peculiarity (from a competitive perspective) of being located at the tip of a peninsula. In constructing our contract models, we took into consideration these factors, having been supported in our efforts by a leading cargo consulting firm.

Regarding outstanding balances, POM advised Seaboard that it would not take any amendment to the Board unless all receivables past 90 days were resolved. Nonetheless, the OIG's presence at our meetings played a significant role in ensuring a fair resolution to this matter.

PORT OF MIAMI 002
Memorandum



Date: May 6, 2008
To: Christopher R. Mazzella
Inspector General
From: Bill Johnson *Bill Johnson*
Port Director
Seaport Department
Subject: Addendum to OIG Draft Memorandum IG07-04

In response to your memorandum of April 22, 2008, regarding recent findings by the Office of Inspector General related to a past conviction of Seaboard Marine for the transportation of hazardous materials over public highways, please be advised of the following. We have addressed this issue with top management from Seaboard Marine who has provided us the attached letter regarding the incident, as well as their compliance with and early release from the terms of their court-ordered probationary period. It is our understanding that the Inspector General's office has already received copies of the attached letter, as well as proof of payment of Seaboard fines.

More directly, in response to the issues you raised in your memorandum, under the terms of the existing agreement between Seaboard and the County, and to the best of our knowledge, Seaboard is not obligated to notify the County of such a conviction although it was public and reported in the media. With regard to the level of proof and documentation of Seaboard's compliance, we are satisfied with the information they have provided. This conviction does not have any effect on our negotiations, on the agreement going forward, nor on their standing with the Port of Miami. With regards to your last issue regarding what provisions exist in the current and proposed amendments to protect the interests of Miami-Dade County and to protect the County from liability resulting from spillages and environmental hazards on County property, the agreement provides for the operator to indemnify the County for any actions caused by them.

I trust the above will address your concerns. Should you wish to discuss further, please do not hesitate to contact me.

Attachments

APPENDIX B