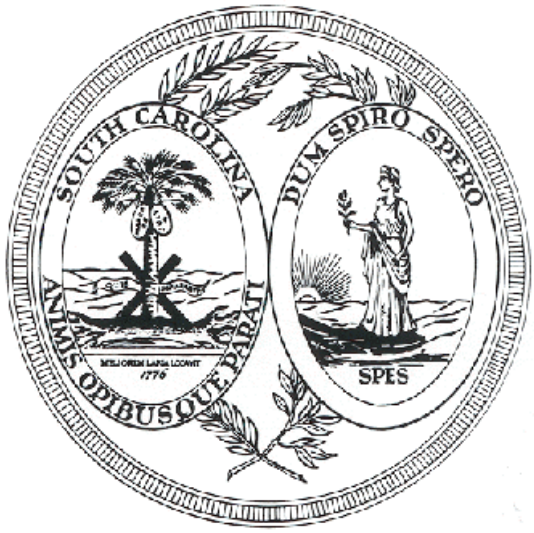
LAC

Report to the General Assembly

September 2000

A Management Review of the Charleston Naval Complex Redevelopment Authority



Legislative Audit Council

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A Management Review of the Charleston Naval Complex Redevelopment Authority
was conducted by the following audit team.

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Report to the General Assembly

A Management Review of the Charleston Naval Complex Redevelopment Authority

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Synopsis

As requested by members of the General Assembly, we conducted a management review of the Charleston Naval Complex Redevelopment Authority (RDA). Since 1994, the RDA has been responsible for the redevelopment and reuse of federal property at the former naval base in North Charleston, which was closed in 1996. Because the U.S. Navy still owns the naval complex, the RDA has entered into master leases with the Navy and has subleased the properties to businesses, governments, and other organizations.

The audit requesters were primarily concerned about the methods by which the RDA leases out land, buildings, and equipment at the naval complex. We were also asked to review the RDA's relationship with another state agency, the S.C. State Ports Authority (SPA), as well as the RDA's compliance with the S.C. Freedom of Information Act.

One of the primary goals of the RDA has been to replace jobs lost by the closing of the Charleston naval base. When the base closed, 6,272 civilian and 8,722 military jobs were lost. As of May 2000, a total of 4,089 workers were employed at the complex. The RDA has also made progress toward renovating the infrastructure at the complex.

According to RDA officials, maximizing rent from subleases has not been a goal. The agency, however, has not adequately marketed available properties at the naval complex. Therefore, the RDA may have limited the pool of qualified businesses seeking to bring new jobs and economic development to the area.

Our findings include the following:

- ❑ The S.C. State Budget and Control Board, which is responsible for overseeing state government leasing, reports that the RDA has complied with state laws and policies concerning the leasing out of real property.

- ❑ In February 1995, the RDA issued a request for proposals to companies interested in subleasing all or part of the naval complex. Companies were permitted to submit proposals for different combinations of property and with different methods for determining rent. It is therefore not clear how the RDA was able to rank the companies.

- ❑ Since 1995, the RDA has leased out piers, buildings, and other properties without adequate marketing. As a result, properties have been leased out without fully determining the level of interest from other potential tenants.

- ❑ The RDA has not established written asking prices when renting its available buildings and piers.

- ❑ The RDA has not adequately controlled the process by which its tenants sublease properties to other organizations. Tenants have sometimes not obtained the required prior approval. In addition, the RDA has not sufficiently controlled the rental rates charged by its tenants to other organizations.

- ❑ When the RDA took over the management of Navy-owned equipment, the Navy's inventories were inaccurate and incomplete. The RDA, however, did not immediately conduct a more complete inventory of its own. While theft may have occurred during the early years of the RDA's management of the naval complex, poor record-keeping has made it impossible to determine what was stolen.

- ❑ We found no material problems with the RDA's current inventory tracking system, taking into consideration the inaccuracy of the Navy's initial inventory and the difficulty of monitoring equipment that is constantly being relocated over a widespread area. However, the RDA does not hold tenants accountable for Navy-owned equipment that is damaged or missing, and does not charge for the use of extra equipment relocated from other facilities.

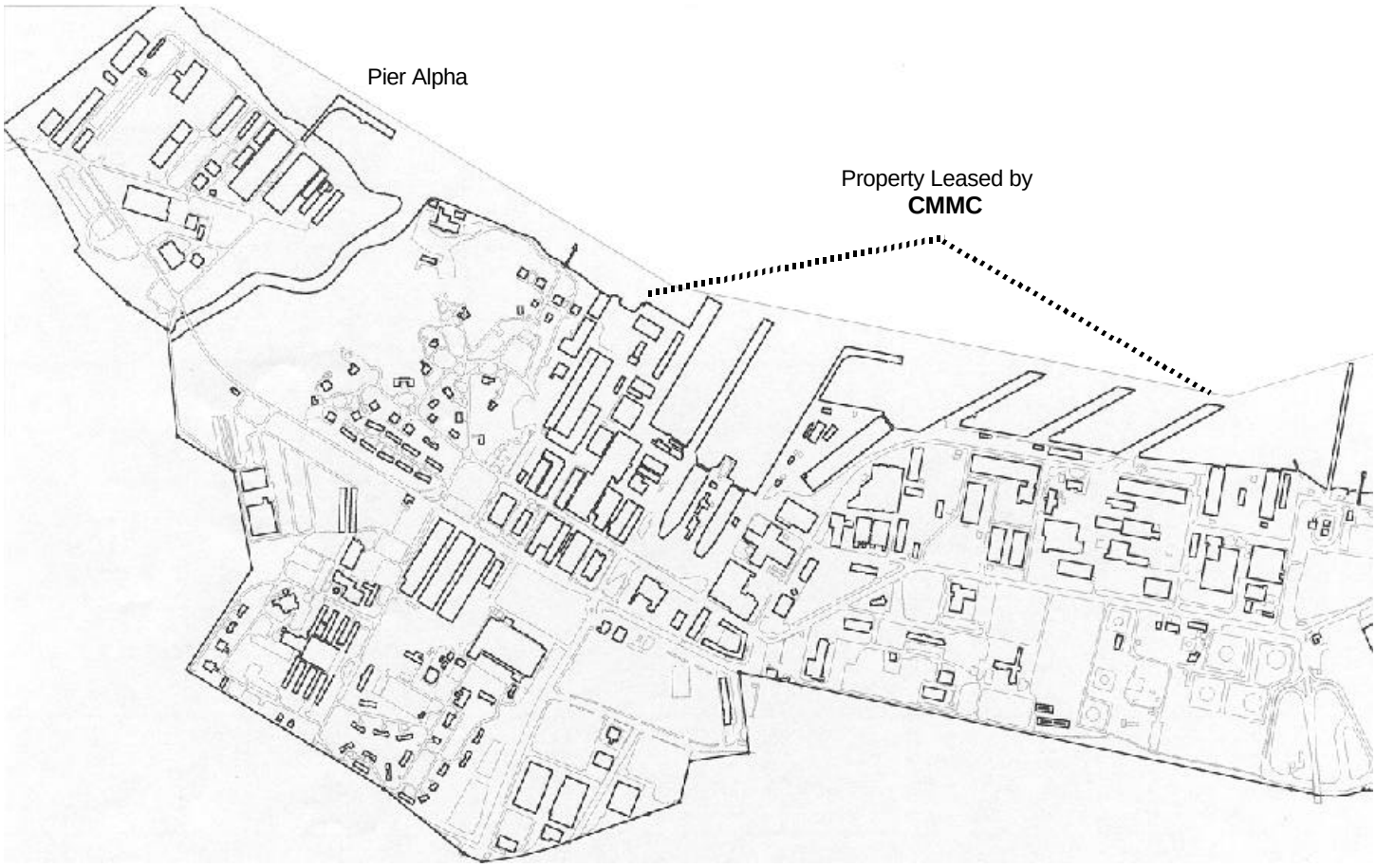
- ❑ The RDA's system for signing out building keys is ineffective as a means of controlling access to nonleased or unoccupied buildings. There also is little monitoring of vehicles exiting the complex. We observed no effort being made by gate guards to restrict access to the naval complex.

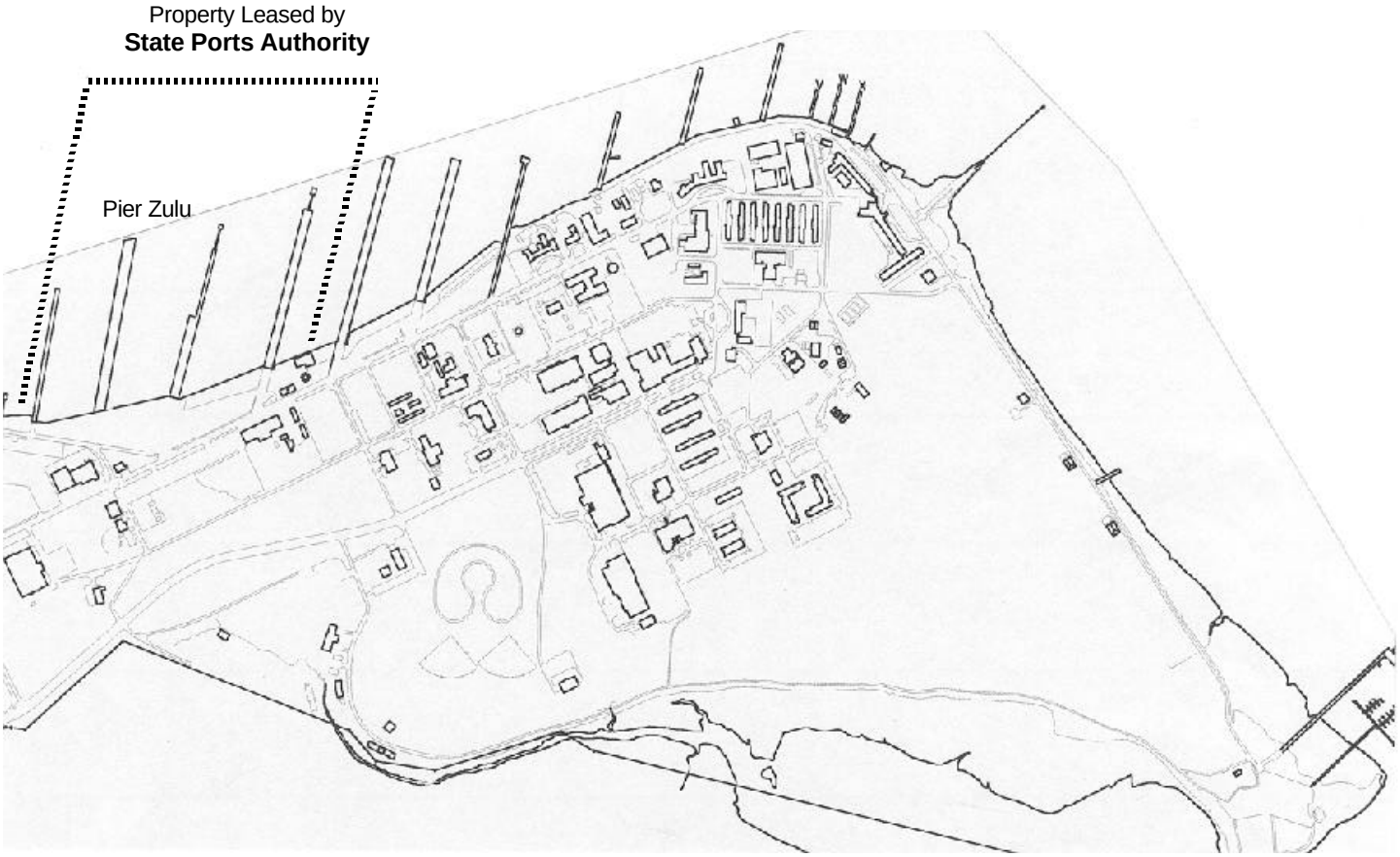
- ❑ The RDA awarded a sublease with an option to purchase to the State Ports Authority for a large portion of the base, including four piers and 38 buildings. As with other tenants, the RDA did not adequately market these properties. To make properties available to the SPA, six small businesses will not be permitted to renew their subleases.

- The State Ports Authority, in August 1999, awarded a license to a private company called Charleston International Ports (CIP) to operate a cargo terminal on properties subleased from the RDA. The SPA official who negotiated the sublease with the RDA and the license with CIP resigned in January 2000 and accepted a job from the owner of CIP. While not employed directly by CIP, he is involved in matters concerning the CIP license. The State Ethics Commission, in a confidential opinion, found no prohibition to this employment. However, we have concluded that the current ethics law may need to be strengthened.

- The RDA is generally in compliance with the state Freedom of Information Act (FOIA) regarding public access to RDA meetings and records. The RDA and the State Ports Authority held confidential lease negotiations during 1998 and 1999. Keeping the negotiations private was technically in compliance with FOIA, but the purpose of the FOIA is to ensure that government activities are conducted in public.

Charleston Naval Complex




Property Leased by
State Ports Authority
Pier Zulu

Synopsis

Background

Audit Objectives

As requested by members of the General Assembly, we conducted a management audit of the Charleston Naval Complex Redevelopment Authority (RDA). The RDA is responsible for the redevelopment and reuse of federal property at the former U.S. Naval Base in North Charleston. The requesters were primarily concerned about the way in which the RDA has been leasing out land, buildings, and equipment at the naval complex. Based on this request, we sought to determine whether the Redevelopment Authority has:

- ❑ Complied with state rules and regulations regarding subleases of properties.
- ❑ Adhered to sound business practices regarding subleases of properties.
- ❑ Implemented an adequate system for safeguarding equipment, furniture, and other property owned by the U.S. Navy.
- ❑ Maintained a proper relationship with the South Carolina State Ports Authority (SPA), consistent with the statutory mission of the RDA.
- ❑ Complied with the S.C. Freedom of Information Act.

Scope and Methodology

The period covered during this audit was primarily 1995 through 1999. Our sources of evidence included:

- Relevant South Carolina laws, including the RDA's governing statutes, the Procurement Code, the Freedom of Information Act, and the Ethics Act.
- Leases, subleases, and related documents of the RDA.
- Minutes and agenda for meetings of the RDA board.
- Inventories of land, buildings, and equipment maintained by the RDA.
- RDA correspondence and financial reports.

In addition, we interviewed officials with the RDA, the U.S. Navy, and the South Carolina State Budget and Control Board (B&CB). We also interviewed officials with industrial parks and closed miliary installations in other states. We reviewed RDA subleases for major pieces of property, and conducted an on-site inventory of a sample of equipment and other items located in subleased facilities. Any computer-generated data supplied by the RDA was used for background information and was not verified by us. This audit was conducted in accordance with generally accepted government auditing standards.

In December 1999, the RDA agreed to pay $4 million in damages to settle a lawsuit filed by Braswell Services Group, Inc., a ship repair company. Braswell had sued the RDA in 1997 for violating the terms of a prior agreement. In January 2000, members of the Charleston legislative delegation held a public hearing to air concerns about the Braswell lawsuit settlement and to receive testimony from the Redevelopment Authority. During the hearing, an audit requester expressed the need for immediate information on the lawsuit settlement. In response, we released a limited-scope report reviewing the lawsuit and the RDA's settlement in March 2000. (See *A Review of the Charleston Naval Complex Redevelopment Authority's 1999 Lawsuit Settlement with Braswell Services Group.)*

Scope Impairment

Generally accepted government auditing standards require us to report significant constraints imposed upon the audit by "scope impairments." A scope impairment hampers our ability to fully accomplish our audit objectives. In this audit, a scope impairment has occurred.

On page 27 we describe a possible conflict of interest involving a former state employee and a sublease between the RDA and the State Ports Authority. The State Ethics Commission had issued an advisory opinion on the matter in January 2000 and voted to keep it confidential. We requested that we be allowed to review the text of their opinion and the documentation of the material facts supporting the opinion. Section 2-15-61 of the S.C. Code of Laws states:

> [f]or the purposes of carrying out its audit duties, the Legislative Audit Council shall have access to the records and facilities of every state agency during that agency's operating hours with the exception of reports and returns of the South Carolina Department of Revenue . . . .

In addition, §2-15-62 requires LAC staff, in the performance of audit duties, to be ". . . subject to the statutory provisions and penalties regarding confidentiality of the records of the agency under review." Therefore, state law allows us access to the records of other state agencies while still protecting the confidentiality of these records.

Even though the General Assembly has authorized our access to state agency records, the State Ethics Commission has refused to allow us to review the text of this opinion and the supporting documentation unless we obtain a court order. To seek a court order at this time would delay the timely release of this report. The former state employee who sought the opinion and requested that the commission keep the opinion confidential also refused to waive confidentiality of the opinion. This has impaired our ability to determine compliance with state ethics laws as they related to the scope of this audit.

Background of the RDA

The Charleston Naval Base dates back to 1901 and comprises 1,574 acres located in the city of North Charleston, with almost 4.5 miles of shoreline on the Cooper River. During World War II, it grew to become a major Navy port. But in 1988, under the federal Defense Base Closure and Realignment Act, the U.S. Department of Defense started closing selected military installations around the country. The Charleston Naval Base was targeted for closure in 1993, and full closure occurred in 1996. According to the Department of Defense, this resulted in the loss of 6,272 civilian and 8,722 military jobs at the base.

Reuse planning for the naval complex began in 1993 with the BEST (Building Economic Solutions Together) Committee, which was formed by executive order of the Governor and included representatives from Charleston, Dorchester, and Berkeley Counties (known as the Trident Region). In 1994, the S.C. General Assembly passed the Military Facilities Redevelopment Law, finding that:

> . . . federal property located in the State has and will become available for the state's use. It is in the best interests of the citizens of this State for the State, municipalities, and counties to work in concert and oversee and dispose of federal military facilities and other excess federal property, in an orderly and cooperative manner. [S.C. Code §31-12-20(1)]

The act authorized the Governor to create separate and distinct redevelopment authorities. In 1994, the Charleston Naval Complex Redevelopment Authority (RDA) was created by executive order, and the BEST Committee was phased out.

The U.S. Navy currently holds title to the land at the naval complex. Conveyance of part of the complex to the state is expected to occur in 2000.

The RDA's purpose is to oversee the redevelopment and reuse of the real and personal federal property at the Charleston naval complex. (Real property consists of land, buildings and other structures; personal property consists primarily of equipment, furniture, and vehicles.) The Redevelopment Authority board is comprised of seven members:

- One at-large member appointed by the Governor.
- Three members from the City of North Charleston appointed by the Governor from a slate of candidates submitted by the North Charleston City Council.
- One member each from Berkeley, Dorchester, and Charleston counties, also appointed by the Governor.

State law authorizes the RDA to:

- Make and amend by-laws, rules, and regulations.
- Sue and be sued.
- Make and execute contracts.
- Carry out redevelopment projects.
- Purchase, acquire, improve, sell, exchange, transfer, mortgage, retain for its own use or otherwise encumber or dispose of any real or personal property within its area of operation.

The RDA is also authorized to issue bonds and borrow money, provided it does not pledge the full faith and credit of the state or any political subdivision for repayment. The RDA is required to comply with the provisions of the S.C. Procurement Code. The RDA may dissolve itself when all properties have been sold to the private sector or if it decides to transfer any remaining redevelopment property to another public body or successor entity.

The Authority has a staff of 16, and is funded by the Navy, federal grants, rural development funds, revenue from subleases, and miscellaneous revenues. Appendix A shows a schedule of the RDA's revenues and expenditures for FY 94-95 through FY 98-99. As of April 2000, the RDA had approximately 80 tenants and subtenants. The RDA has also made progress toward renovating the infrastructure of the complex, including its water and sewer systems.

History of Major Leasing Efforts

Since 1995, the RDA has been subleasing land and buildings to private businesses, government agencies, and nonprofit groups. When the RDA finds a suitable tenant for property, it first obtains a master lease with the Navy and then subleases the property to the tenant. Both the B&CB and the Navy must approve all leases for property. One of the primary goals of the RDA has been to replace jobs lost by the closing of the base. Below is a summary of the major leasing efforts by the RDA.

1995 Request for Proposals

In February 1995, the RDA and the B&CB formally issued a request for proposals (RFP) to more than 90 private companies to lease all or part of the naval complex (see p. 12). After receiving various proposals from 13 companies, the RDA ranked them and reported that it would negotiate subleases with the top four companies:

- Babcock & Wilcox was awarded a sublease for two buildings in November 1995. Babcock & Wilcox terminated its sublease in 1998 due to lack of business.

- Charleston Marine Manufacturing Corporation (CMMC) was awarded a sublease for one dry dock and three buildings, and by 2000 its sublease included more than 100 buildings and three dry docks. CMMC is currently the RDA's largest tenant and occupies almost 1.9 million square feet, most of which is under a 30-year sublease awarded in 1999. CMMC is a conglomerate of smaller companies plus two large companies, Detyens Shipyard, Inc. and Metal Trades, Inc.

- Charleston Shipbuilders Incorporated (CSI) was awarded a sublease for one building, and by 1997 its sublease included a pier and almost 40 buildings. In 1999, because of an unsuccessful business venture, CSI terminated its original sublease but continues to lease a pier and one building under a short-term license that will expire November 30, 2000.

- The RDA attempted to negotiate a sublease with Braswell Services Group, Inc., for Pier Alpha and related buildings at the north end of the complex. Braswell proposed to conduct ship repairs at the site, but in 1996, the negotiations stalled.

1996 Competition for Pier Alpha

After negotiations with Braswell stalled, the RDA placed Braswell in competition with three other companies and the State Ports Authority for a sublease of Pier Alpha and related properties (see Figure 1.1 on p. viii). The RDA declared Braswell the winner of the 1996 competition; however, negotiations stalled again. The RDA was reluctant to sign the sublease until Braswell terminated lawsuits and procurement protests it had previously filed against the RDA regarding the 1995 RFP.

In March 1997, Braswell agreed to terminate its legal actions in exchange for a sublease. The RDA awarded Braswell a six-month license to prepare the Pier Alpha area for ship repairs. Then, for a third time, neither party agreed to the terms of a sublease. The RDA stated that Braswell had not obtained necessary environmental permits. Braswell contended such permits were not a prerequisite to a sublease. In October 1997, its temporary license to occupy the Pier Alpha area having expired, Braswell filed a lawsuit against the RDA for not agreeing to sign a sublease. This lawsuit was settled out-of-court in 1999, and Braswell was awarded $4 million in damages. (See our March 2000 audit, *A Review of the Charleston Naval Complex Redevelopment Authority's 1999 Lawsuit Settlement With Braswell Services Group*.)

1998 Efforts to Sublease Pier Alpha

In 1997, the SPA and a newly formed private company, now called Charleston International Ports (CIP), entered into negotiations to jointly seek a sublease for Pier Alpha and related buildings. Under this arrangement, the Ports Authority would obtain a sublease from the RDA and lease out the properties to CIP under a license. CIP would operate a public shipping terminal at the site, specializing in noncontainerized cargo.

In August 1998, the RDA announced its decision to award the sublease for Pier Alpha and related buildings to the SPA, with the understanding that the SPA would, in turn, lease the properties to CIP. Immediately, officials from the city of North Charleston, in which the naval complex is located, protested the use of the north end of the complex for cargo shipping. City officials wanted to develop the site into a recreation area for the public. In December 1998, after the protest by the city of North Charleston, the RDA rescinded its approval of the SPA's sublease of Pier Alpha. Currently, Pier Alpha is not under a sublease to any tenant.

1999 State Ports Authority Sublease

In April 1999, the RDA and the SPA signed a 30-year sublease for an alternative site near the center of the naval complex. This site became available after two other companies terminated their subleases. In August 1999, the SPA signed a license agreement with CIP for these properties. The SPA will receive rent from CIP equal to the amount the SPA pays to the RDA, plus half the annual net income of CIP. By 2007, the SPA's sublease will include 4 piers and 38 buildings. In addition, the sublease gives the SPA the right of first refusal of subleases for a fifth pier and 33 additional buildings.

Current Status

Table 1.1 shows the status for all the types of facilities at the complex as of May 2000. ("Other" includes nonbuilding structures such as quay walls, bus shelters, etc.)

Table 1:1: Percent of Naval Complex Occupied

	Buildings	Piers	Dry Docks	Utility Infrastructure	Other	TOTAL
Total	566	27	5	73	198	869
Leased, Licensed, or Owned	394	22	3	36	75	530
Percent Occupied	69.6%	81.5%	60.0%	49.3%	37.9%	61.0%

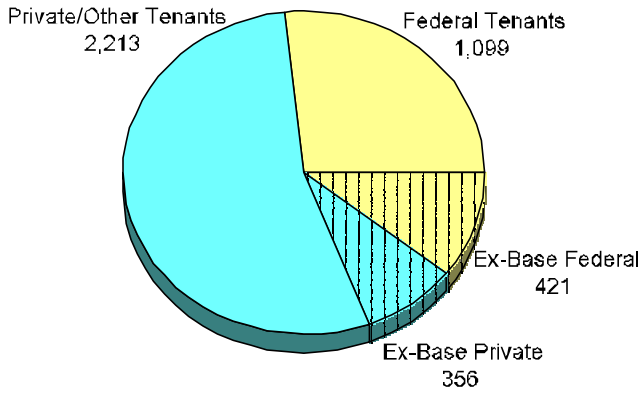
Source: RDA Master Inventory.

Approximately 34% (by square feet) of the occupied buildings at the complex are used by federal agencies. The remainder are subleased or licensed to private businesses and local and state agencies.

About 65% of the 6,272 civilian jobs lost when the base closed have been replaced.

When the naval base closed, a major concern of the community was the loss of jobs. According to RDA data as of May 2000, a total of 4,089 workers are employed at the complex (see Chart 1.1). Therefore, about 65% of the 6,272 civilian jobs lost when the base closed have been replaced. Federal agencies employ 37% of the total workers currently at the complex, and CMMC alone accounts for another 29% employed. The RDA collects employment information from the tenants but does not verify or monitor this information. As far as we could determine, no agency has tracked the other former Naval base workers to see whether they found employment and where. Former base workers currently comprise almost 20% of the workforce at the complex.

Chart 1:1: Workers Employed at the Naval Complex



Source: RDA.

Pending Lawsuits

As of July 2000, three lawsuits filed against the RDA were pending. These lawsuits concerned the process by which the RDA awards subleases. A fourth lawsuit had been filed against the Navy concerning its oversight of the subleasing process used by the RDA. This lawsuit was withdrawn in July 2000, but, according to the plaintiffs, it will be refiled.

Chapter 1
Background

Subleasing of Properties

In this chapter, we address the following issues regarding how the RDA manages subleases for naval complex properties:

- The requirements of state law.
- The RDA's 1995 request for proposals.
- The marketing of naval complex properties to the public.
- How the rents charged to tenants are established.
- The leasing-out of properties by RDA tenants to other organizations.

Requirements of State Law

The State Budget and Control Board . . . reports that the RDA has complied with state laws and policies pertaining to leasing out real property.

The State Budget and Control Board, which is responsible for overseeing state government leasing, reports that the RDA has complied with state laws and policies pertaining to leasing out real property.

Beginning with the RDA's first sublease of naval complex property, the Budget and Control Board has interpreted state law as requiring its approval of all subleases. Until 1997, S.C. Code §11-35-1590 (1) designated the B&CB as the:

> . . . single central broker for the leasing of real property for governmental bodies. No governmental body shall enter into any lease agreement or renew any existing lease except in accordance with the provisions of this Section.

In 1997, the General Assembly amended state law, creating S.C. Code §1-11-55 in which subsection (4) states that the B&CB:

> . . . shall adopt procedures to be used for governmental bodies to apply for rental space, for acquiring leased space, and for leasing state-owned space to nonstate lessees.

According to an attorney with the Budget and Control Board, the RDA has flexibility in the way it selects tenants as long as potential tenants are made aware of the availability of properties, are given the opportunity to submit proposals, and the results are "fair."

Leasing Methods

There are different methods potentially available to state agencies for leasing out real property:

- Competitive Bids — A written "invitation for bids" is issued in which qualified parties are asked to submit to a governmental body the amount of rent they propose to pay. Bids must be submitted by a certain date. The lease is awarded to the entity with the highest bid. The RDA has not used this method.

- Competitive Proposals — A written "request for proposals" (RFP) is issued in which qualified parties are asked to submit lease proposals that will be evaluated based on a number of factors, only one of which is the proposed rent. Proposals must be submitted by a certain date. The RDA has used a formal version of this method only once, in 1995.

- Leasing Without Formal Competition — Potential tenants submit lease proposals that are evaluated based on standards established by the governmental body. There is generally no date by which proposals are required to be submitted. In some instances, a property may be leased after only one proposal. In other instances, multiple proposals may be received. This is the primary leasing method used by the RDA.

Commercial and industrial real estate leasing in the private sector is not usually conducted through competitive bid or competitive proposal. These methods have specific time limits that can reduce the number of offers from prospective tenants and the amount of rent. For properties that are known to be in high demand, however, a competitive proposal process may be an effective way to select tenants.

1995 Request for Proposals

In February 1995, the RDA and the State Budget and Control Board issued an RFP to obtain offers from companies interested in competing for subleases for naval complex property. These companies were permitted to submit proposals to sublease different properties which were not comparable. In addition, most of the proposals did not offer a specific amount for rent.

According to the RFP, the RDA was seeking proposals from companies "interested in leasing all or major portions of the naval complex." These proposals were to be evaluated and ranked based on financial factors, employment, lease length, property requirements, environmental factors, and economic impact. Rental payments were a component of the financial factors.

The naval complex encompasses approximately 1,500 acres and includes 566 buildings, 27 piers, and five dry docks. Each of the four highest ranked proposals was for a different combination of facilities, and each proposed a different way to establish rents.

- Babcock & Wilcox requested three buildings and a portion of another and proposed rental payments based on overhead costs.

- Braswell Services Group, Inc., submitted a proposal consisting of three business options, each with a different combination of properties. The proposed rental payments included a base rate plus a percentage of gross revenues for each option.

- Charleston Marine Manufacturing Corporation (CMMC) requested 28 buildings, six piers, and three dry docks. CMMC proposed escalating rental payments, ranging from no cost during the first year up to $2,829,500 during the fifth year.

- Charleston Shipbuilders Incorporated (CSI) requested more than 30 buildings, 13 piers, and dry docks. The rental payments were to be based on the number of production workers employed.

The RDA ranked Babcock & Wilcox first, followed by CMMC, CSI, and Braswell Services Group. Subleases were later negotiated with three of the four companies, only one of which is still operating at the naval complex.

It is not clear how the RDA was able to rank the companies, considering that no two proposals contained exactly the same properties and that most of the proposals did not offer specific amounts for the rental payment. Thus far, this has been the only instance in which the RDA used the RFP process for subleasing.

Marketing of Properties

. . . the RDA has leased out piers, buildings, and other properties without formal marketing.

The RDA has not adequately marketed the properties at the naval complex, and in general does not use advertising. As a result, properties have been subleased without determining the level of interest from other potential tenants, which may have reduced the pool of qualified businesses able to bring new jobs and economic development to the area.

In connection with its 1995 RFP, the RDA and the State Budget and Control Board, with the assistance of the South Carolina Department of Commerce, mailed announcements to private companies in the United States and other countries. Advertisements were placed in newspapers and trade journals. Through these actions, the public and businesses were informed that the naval complex had properties available for sublease. Since 1995, however, the RDA has leased out piers, buildings, and other properties without formal marketing. For example:

- In 1998, Babcock and Wilcox terminated its sublease. The RDA then subleased the machine shop to an existing tenant, Charleston Marine Manufacturing Corporation, without notifying the public and the business community that the property had become available. The machine shop was highlighted by the RDA as one of the important properties at the naval complex. In 1999, the RDA awarded CMMC a 30-year lease for the machine shop as well as for dry docks, buildings, and other facilities.

- In 1996, the RDA and Braswell Services Group reached an impasse in negotiating a sublease for Pier Alpha and related properties. The RDA decided to consider other proposals in August 1996 but did not publicly announce this decision. Instead, the RDA decided to review proposals from Braswell and four other entities: Carolina Marine Handling, Maybank Shipping, Charleston Shipbuilders Incorporated, and the State Ports Authority. In October 1996, the RDA announced that it would award a sublease to Braswell. In October 1997, the RDA and Braswell reached another impasse and negotiations for Pier Alpha were terminated.

- Following the termination of Pier Alpha negotiations with Braswell, the RDA did not publicly announce that this area of the naval complex was still available. The Ports Authority, however, in conjunction with Charleston International Ports (CIP), approached the RDA about subleasing the properties for a cargo shipping terminal. In August 1998, the RDA announced that it would award a sublease to the Ports Authority for Pier Alpha and related properties. This sublease was never executed because of opposition from the city of North Charleston.

- In 1999, Charleston Shipbuilders Incorporated terminated its sublease for Pier Zulu and other properties near the center of the complex. In addition, Carolina Marine Handling terminated its sublease for Pier Mike and other properties near Pier Zulu. The RDA did not publicly communicate the availability of these properties. Instead, the RDA awarded the Ports Authority a 30-year lease for Piers Zulu and Mike, as well as other piers and a number of buildings. The Ports Authority in August 1999 entered into a license agreement for these properties with CIP. The RDA also gave the SPA "right of first refusal" for an additional pier and buildings.

The Department of Commerce has conducted limited marketing of naval complex properties. Companies interested in maritime sites or the Charleston area may be directed to the RDA. The website of the Department of Commerce lists the south end of the naval complex as available; however, individual buildings and piers are not listed.

According to an RDA official, it would be ". . . ineffective to begin an 'organized marketing plan' prior to the establishment of zoning or the ownership of the property." However, neither the zoning nor ownership status of the naval complex prevented the RDA from awarding long-term, 30-year leases to two of its largest tenants, CMMC and the Ports Authority. In addition, the SPA has an option to purchase the property it subleases.

Potential Effects of Increased Marketing

Increased marketing could have resulted in greater access by companies that did not know which parts of the naval complex were available, particularly properties made available through sublease terminations. With greater interest from more companies, the RDA might have more opportunities to sign short-term and long-term subleases with established businesses that provide more jobs and pay higher rents.

We found that industrial parks in South Carolina and closed military bases in Pennsylvania and California have used a variety of methods to market their properties. Examples of these methods include websites, brochures, ongoing advertising in print media, and the use of real estate brokers. None of these marketing methods have been used by the RDA except for advertising in the print media, which the RDA did only in 1995.

How Rent is Determined

One of the RDA's primary goals has been to replace jobs lost by the closing of the base. Therefore, according to RDA officials, maximizing rent from subleases has not been a goal. Tenants may pay reduced or below market rents based on factors such as the number of jobs they provide or renovations they agree to make to the properties.

We found areas in which improvements could be made:

- The RDA has not established written asking prices when renting its available properties. There are two potential negative effects of not having written "asking rents." First, the number of prospective tenants interested in the naval complex may be reduced because the degree to which the RDA's rents are lower than those at alternative locations may not be widely known. Second, public confidence in the leasing process may be reduced because the process of determining rents is less open and less understandable to the public.

  It is important to note that written asking rents would not preclude negotiated discounts based on factors such as jobs or commitments to renovate the properties, as discussed above. Written asking rents would also not preclude negotiated discounts for tenants who lease multiple properties.

- The rents paid by two large tenants, CMMC and CSI, have been based primarily on the companies' gross revenues. Other tenants are charged fixed amounts per month. Revenue-based rent is more subject to misinterpretation and fraud than fixed rent. It also makes auditing necessary. As of April 2000, the RDA had not yet completed its first audit of CMMC and CSI, which covers 1997 – 1998.

Controls Over Secondary Subleases

Several tenants have sublet some of their property to other entities under agreements referred to as secondary subleases. As of April 2000, there were 28 secondary subtenants operating at the naval complex. We found that tenants did not receive prior approval from the RDA board for some secondary subleases, and that rental rates paid to tenants have not been sufficiently controlled.

Subleases prohibit tenants from assigning or subleasing their interest in the premises or any portion thereof without the prior written consent of the RDA. According to an RDA official, once the board consents to a secondary sublease, tenants are sent a letter or a copy of the board minutes which reflects this decision.

Between 1996 and 2000, tenants subleased property to more than 40 companies and other organizations. Agency records show that tenants did not obtain prior written consent for some of these secondary subleases as required. For example, on July 13, 1999, the board consented to the following secondary subleases after the fact:

- An agreement made on July 1, 1997, for three piers and a portion of one building.
- An agreement made on August 1, 1998, for portions of two buildings.
- An agreement made on April 1, 1999, for a portion of one building.

The RDA, through its subleases, has not controlled or limited the rental rates charged by its tenants to secondary subtenants. We found that, over a two-year period, one tenant leased out a building for approximately $122,000 more than the rent it was required to pay the RDA. In some cases, it was difficult to determine the degree to which tenants profited from secondary subleases. When subleasing more than one piece of property, the RDA does not always identify the amount individual pieces of property contribute toward the total rent payment.

. . . over a two-year period, one tenant leased out a building for approximately $122,000 more than the rent it was required to pay the RDA.

The Mare Island Conversion Division, which is redeveloping a former naval shipyard in California, also requires its tenants to obtain written consent prior to leasing out property. Other requirements help Mare Island control secondary subleasing practices of its tenants. For example, tenants must give Mare Island 30 days notice of their intent to sublease. At this time, tenants must provide information about the prospective company and pay a nonrefundable administration fee. In addition, tenants are not permitted to profit from secondary subleases. Any excess rent tenants receive from secondary subtenants is required to be paid to Mare Island.

Without prior approval of secondary subleases, the RDA cannot ensure proper use of facilities by its occupants. Also, when rental rates paid by secondary subtenants are not controlled, tenants are allowed to profit by leasing out naval complex property. Tenants' ability to profit from secondary subleases are an indication that the RDA's rents are below market rates (see p. 16).

Recommendations

1. If the Redevelopment Authority decides to issue a request for proposals to lease out property in the future, it should require that each company submit a proposal for the same property and offer a specific amount for rental payments.

2. The Redevelopment Authority should conduct ongoing marketing of naval complex properties available for lease or sale. When establishing a marketing plan, the Redevelopment Authority should consider the merits of a website, print advertisement, brochures, and real estate brokers.

3. When marketing naval complex properties available for lease or sale, the Redevelopment Authority should include written asking rents or asking prices, subject to negotiation.

4. The Redevelopment Authority should not base rental payments on revenues generated by tenants.

5. The Redevelopment Authority should ensure that its tenants obtain written consent before subleasing out property. Also, the Redevelopment Authority should explore methods for monitoring and controlling rental rates charged by tenants to secondary subtenants.

Controls Over Equipment

According to its Cooperative Agreement with the U. S. Navy, the RDA is responsible for Navy-owned equipment and other movable property at the naval complex. This includes vehicles, small water craft, movable cranes, material handling equipment (e.g., forklifts), and office equipment (including computers and furniture). The complicated process of transferring management of a huge volume of property from the Navy to the Redevelopment Authority has been further hindered by loosely enforced policies, lack of standardized procedures, and ineffective security. In this chapter, we discuss issues related to:

- The RDA's method of establishing its own equipment inventory system.
- The general lack of accountability for Navy-owned equipment.
- The incidence of break-ins and missing equipment.

Problems With Inventory

Federal procedures require the Navy to provide an inventory record to a redevelopment authority in order to facilitate the transfer of personal property. According to both Navy and RDA officials, the inventory lists compiled by the Navy at the time of base closure were not always accurate or complete. The RDA did not immediately conduct a more complete inventory of its own, thereby depriving itself of a major tool for controlling the location and movement of equipment and other types of property. Thus, while some instances of theft may have occurred during the early years of base conversion, it is impossible to determine what was missing.

Equipment associated with facilities is generally included in each sublease. The RDA inspects and records a facility's contents at the time it is subleased, then keeps this record on file to serve as the basis for subsequent inspections. Its policy calls for an annual wall-to-wall inspection of equipment used by smaller tenants and a quarterly inspection of 50 randomly selected items used by larger tenants. Since some tenants sublease multiple buildings, the agency gives tenants two weeks to locate the items chosen to be inventoried.

Tenants may obtain additional items of equipment and furniture from nonleased facilities by submitting a written request, which must be approved by the Navy. Consequently, equipment and furniture are no longer associated with specific buildings as they were when the base closed. Because tenants use this relocation system repeatedly and sometimes exchange equipment without first obtaining approval, the Redevelopment Authority's ability to

keep track of equipment may be hindered. The RDA keeps a copy of the equipment transfer request on file and attaches a list of relocated items to the tenant's inventory record; however, it does not keep a computerized log of requests so that a specific one can be located on short notice.

Sample Inventory

To test the RDA's process for tracking equipment, we conducted our own inventory inspection of a sample of 52 items selected from lists of equipment for buildings currently subleased to tenants. The lists contained only items that were marked with serial or Navy numbers; nonnumbered items such as furniture were not included. Criteria for item selection were: (1) size of tenant, in terms of area occupied and volume of equipment leased, (2) variety of types of equipment, e.g., vehicles, boats, cranes, and (3) items and facilities believed to be particularly vulnerable to security problems based on documentation obtained from the RDA. Although agency staff accompanied us during the inventory, they had no prior notification of the items we intended to verify.

We found no material problems with the RDA's inventory tracking system, given the inaccuracy of the Navy's initial inventory and the difficulty of tracking equipment that is constantly being relocated over a widespread area. Forty-eight of the fifty-two items were successfully located; two (a forklift and a crane) were away for repairs; one (a Hydra Sport boat) matched the inventory description but had no identification number; and one (a small trailer) could not be located.

Accountability for Equipment

We could find no evidence that the RDA, in either its leasing or inventory process, holds tenants accountable for Navy-owned equipment.

- The Redevelopment Authority does not specifically show how the value of equipment is factored into determining rent (see p. 16). A sound business practice would be to determine the rental value of equipment that accompanies buildings being leased.

- The RDA does not charge tenants for the use of extra equipment relocated from other facilities or for leased items that are damaged or missing. A staff person at a former naval shipyard in California stated that equipment there is leased to tenants at a separate rate based on its original cost, and lease rates are adjusted to reflect any additional equipment the tenant obtains from other facilities. The RDA does not

charge tenants for equipment, according to a staff member, because its mission is not "profit-oriented."

- During one inventory inspection in the fall of 1998, the RDA could not locate 4 of the 50 selected items of equipment leased by one of the tenants. A mower and tiller were discovered missing, and a test pump and forklift were in use away from the complex; as of June 2000, however, the tenant has produced only one of the missing items. And although the tenant is preparing to vacate the complex as of November 30, 2000, there are no plans to charge a fee or otherwise hold the tenant accountable for the equipment, which is still owned by the Navy.

Equipment Taken From the Complex

From March through June 1999, the State Law Enforcement Division (SLED) investigated specific allegations involving improper removal of Navy property from the complex. Following are details concerning three of the allegations:

- In May 1996, a former employee of one of the RDA's largest tenants arranged to have Navy-owned office furniture moved to his home in Florida, later claiming that Navy personnel had given him permission to do so. However, Navy procedure at the time of base closure required having the furniture screened by the RDA and then disposed of through the Defense Reutilization and Marketing Office (DRMO). The Navy required the former employee to return the furniture. Once it was finally returned, in April 1999, there was no fee charged for the three years the furniture was used outside the complex.

RDA staff acknowledge that tenants sometimes "relocate" equipment from unoccupied facilities without first obtaining approval.

- In April 1997, this same tenant company had 2 Navy boats, 19-foot Boston Whalers, re-registered in its name and taken to Florida. The RDA traced the location of the boats and requested that they be returned. According to documentation, the boats were returned in May 1999; we verified this through observation during our sample inventory. We found no evidence that the Navy pressed charges or otherwise held the tenant accountable for stealing property owned by the Navy.

- On at least five occasions, beginning in January 1996, the RDA loaned Navy-owned office furniture and computer equipment to the city of North Charleston with the understanding that it would be used in support of redevelopment of the naval complex. In all instances, an itemized listing of the equipment or furniture loaned was signed by a North Charleston official; however, a more specific use for the furniture and a

time for its return were given in only two cases. Although the Navy is aware of this arrangement, RDA staff could not provide written documentation of its approval. Loans of personal property outside the complex do not comply with official Navy policy; however, the Navy's caretaker officer stated that he does not enforce this policy with the RDA.

After reviewing SLED's investigative report, the S.C. Attorney General's office could not find sufficient evidence to warrant criminal prosecution. In response to RDA requests, the Navy has declined to investigate such incidents and has declared itself satisfied with the level of accountability maintained by the agency.

RDA staff acknowledge that tenants sometimes "relocate" equipment from unoccupied facilities without first obtaining approval. Equipment relocation causes the most recent inventory for that facility to be inaccurate and deprives a new tenant of the use of equipment that otherwise would have been included in the lease.

Security Issues

According to its Cooperative Agreement with the Navy, the RDA is responsible for security at the complex. Reports of theft and break-ins indicate that the RDA may need to improve its efforts to safeguard equipment and other personal property. We reviewed the two main systems in place for deterring theft — a key sign-out procedure to limit access to buildings, and placement of guards at designated entrance gates to monitor access from outside.

Key Sign-Out System

The key sign-out system is ineffective as a means of controlling access to nonleased or unoccupied buildings. According to RDA staff, the Navy initiated the system in August 1995 as part of the transfer process; at the time, base personnel were signing out keys with little or no oversight. In April 1996, an RDA staff person was given control of the keys. However,

the sign-out system provides only superficial control over building access because the RDA has no power to enforce:

- When keys are returned. There is a list of keys that are long overdue.
- What is done with the keys while they are signed out. They could be copied, lost, or stolen.
- Who actually uses the keys. Only Navy and RDA staff are officially authorized to sign out keys; according to the custodian, however, keys are sometimes loaned to prospective tenants so they may inspect a building or to contractors who are supervising a renovation project. In one particular case, the log book shows an individual signing out keys initially as a naval officer working in the base closure office and later, after his retirement from the Navy, as an employee of one of the largest tenants. The RDA did not withdraw this person's authorization to access unoccupied buildings once he became employed with the tenant.

Security Guards

The security system has not been effective in keeping unauthorized people out of the complex. According to staff, the RDA contracts for these services because hiring its own security personnel would be too expensive. From April 1, 1996, through March 31, 1998, the city of North Charleston provided security for the complex. Beginning July 1, 1998, the RDA contracted with a private company for security services for $234,000 annually. Security consists of one patrol that tours the complex at designated times during the day and night, and guards stationed at all gates where external access is maintained.

In July 1998, as a result of unauthorized individuals at the complex, the RDA requested gate guards to restrict access to only those vehicles displaying the proper identification. We observed no effort being made by gate guards to restrict access. Furthermore, there have been reports of unauthorized entry. For example, in March 2000, the North Charleston police charged two men with stealing $88,000 worth of pure aluminum from a tenant at the complex. According to news reports, it took the men seven trips in a pick-up truck to remove the four tons of aluminum ingots. This incident clearly indicates that there is little monitoring of vehicles exiting the complex.

The RDA has no plans to increase security at the complex; in fact, officials stated they would like to place even less restriction on outside access in the future. Tenants who wish additional security must provide their own.

Conclusion

Incomplete and inaccurate inventories passed on by the Navy at the time of base closure obviously hindered the RDA in its efforts to establish and maintain an inventory system for personal property. Moreover, the RDA has not included accountability measures in its management of Navy-owned equipment. Tenants are not charged for the use of additional items of equipment obtained from nonleased facilities or for equipment discovered missing from their inventory. The RDA has also not complied with base redevelopment policy by loaning Navy-owned equipment and furniture to groups outside the complex. The Navy may bear some responsibility for this lack of accountability; for example, it has refused requests by the RDA to investigate cases of missing equipment.

Finally, reports of break-ins and missing equipment are evidence that the overall security system is ineffective. Tenants are expected to provide their own security for their facilities, but that does not affect the high incidence of equipment "relocation" by the tenants themselves. The RDA has not been aggressive in preventing abuse of its equipment transfer system.

Recommendations

6. The Redevelopment Authority should ensure proper identification of the Hydra Sport boat listed on its inventory by attaching a numbered identification tag to the boat.

7. To hold tenants accountable for Navy-owned equipment and other personal property, the Redevelopment Authority should:
   - Include the rental value of equipment associated with a sublease in determining the rent amount to be paid.
   - Charge tenants a fee for the use of additional equipment items.
   - Charge tenants for missing equipment.

8. The Redevelopment Authority should comply with Navy policy concerning loans of equipment and furniture to groups outside the complex.

9. The Redevelopment Authority should explore alternatives for strengthening both internal and external overall security.

Other Issues

In this chapter we examine several issues relating to other audit objectives; specifically, whether the RDA has maintained a proper relationship with the S.C. State Ports Authority (SPA), and whether the RDA has complied with the Freedom of Information Act. Also, in the course of audit work, we noted two possible conflicts of interest.

Relationship Between the RDA and the State Ports Authority

We confined our review of the relationship between the RDA and the State Ports Authority to:

- The history of the current sublease between the RDA and Ports Authority for piers and buildings at the central part of the naval complex; and
- The license between the Ports Authority and Charleston International Ports (CIP), the private company which will operate a cargo terminal on these properties.

We noted some areas in which the Ports Authority received preferential treatment from the RDA. In other aspects, however, the RDA has treated the Ports Authority the same as most other tenants at the complex. For example:

Under the terms of its 30-year sublease, the SPA has the option to buy the naval complex property [that it leases] . . . .

- ❑ Twice the RDA offered subleases to the SPA for valuable properties and piers without any marketing or advertising that these properties were available. We have noted that other businesses have been offered subleases without prior marketing (see p. 14).

- ❑ Negotiations between the RDA and the Ports Authority were kept confidential until the subleases were drafted. Again, negotiations for other subleases have not always been disclosed, and this is allowed by the Freedom of Information Act (see p. 30).

In some aspects the relationship between the RDA and the Ports Authority is unique, as follows:

- ❑ In 1997, the RDA board voted to award subleases to three small businesses in the Pier Alpha area at the north end of the naval complex. In March 1998, the RDA board voted to rescind its approval of the subleases before they were finalized so that the same properties could be awarded to the Ports Authority. As it turned out, the SPA's sublease for Pier Alpha was never executed (see p. 7). The three businesses agreed to sublease other properties at the naval complex.

- ❑ The current sublease between RDA and Ports Authority is for an area

near the center of the naval complex and includes 4 piers, 38 buildings, part of a rail system, and equipment. Much of this property was formerly subleased by Charleston Shipbuilders Incorporated (CSI). When the Ports Authority sublease was executed, six small companies were occupying some of the property under secondary subleases with CSI. The Ports Authority is required to continue these secondary subleases until they expire; however, the six companies will not be permitted to renew their secondary subleases and will have to leave the property.

- The RDA has relied on the Ports Authority to ensure that a cargo terminal is successfully operated on the property. Under the sublease with the RDA, the Ports Authority agrees to be "personally obligated" to "conduct operations" on the premises. However, day-to-day operations of the cargo terminal facility will be handled by CIP, which is a start-up company.

  Under the license agreement, CIP will operate the cargo terminal and pay the rent plus half of its annual net income to the Ports Authority, which in turn will provide marketing and other support services. CIP has agreed to charge the same terminal tariffs as the Ports Authority and to deviate from these tariffs only upon agreement of a "joint cooperation committee" comprised of representatives from both parties. In its sublease with the RDA, the Ports Authority has agreed, through CIP, to create at least 40 jobs and spend $7 million in capital improvements within six years of the commencement of the sublease.

- Under the terms of its 30-year sublease, the SPA has an option to buy the naval complex property, with the purchase price to be the present value of any unpaid lease payments. This option can be exercised anytime during the sublease.

Conclusion

The RDA has stated that it desired to have the Ports Authority as a tenant at the naval complex because of SPA's long and successful history in operating ports and cargo terminals. There also is nothing inherently improper about one state agency relying on another. However, since none of this property was advertised when it became available, and no other proposals from the business community were solicited, there is reduced assurance that the RDA is getting the best developer for a unique and valuable piece of property. The preference shown to the Ports Authority also may have been unfair to the smaller businesses.

Possible Conflicts of Interest

During the course of this audit, we noted two possible conflicts of interest — one involving a former employee of the State Ports Authority and one involving an RDA board member.

Former State Ports Authority Official

While reviewing the RDA's sublease with the State Ports Authority, we found a possible conflict of interest involving the employment of a former SPA official by a private company.

According to Ports Authority officials, Charleston International Ports approached them in November 1997 with a proposal for a joint venture to operate a heavy lift cargo terminal at Pier Alpha at the naval complex. Subsequent negotiations between the Ports Authority and the RDA, and between the Ports Authority and CIP, were conducted primarily by the Ports Authority's chief operating officer and executive vice president at that time.

Under current state law, if a public employee or official accepts a job with a private employer contracting with the government, the official cannot work on matters related to a government contract in which he had responsibility . . .

As previously described, the Ports Authority's sublease of Pier Alpha was never executed, and other properties at the center of the complex were substituted. The sublease between the RDA and the Ports Authority was signed April 9, 1999, and the operating license between the Ports Authority and CIP was signed August 31, 1999. This sublease was signed by the SPA's chief operating officer as a witness, who also signed the CIP license as a party to the agreement.

In January 2000, the chief operating officer resigned from the Ports Authority after receiving a job offer from a businessman who is president and owner of CIP. The former SPA chief operating officer did not go to work directly for CIP but rather is employed by another company, headed by the same president and with the same corporate address as CIP. We obtained information that the former SPA chief operating officer is also directly involved in matters concerning the CIP license that he helped negotiate as a state employee.

Under current state law, if a public employee or official accepts a job with a private employer contracting with the government, the official cannot work on matters related to the government contract which he helped procure when he worked for the government. S.C. Code §8-13-760 states that:

> . . . it is a breach of ethical standards for a public official, public member, or public employee who is participating directly in a procurement . . . to resign and accept employment with a person contracting with the governmental body if the contract falls or would fall under the public official's, public member's, or public employee's official responsibilities.

It is the responsibility of the State Ethics Commission to determine if a breach of ethical standards has occurred. Prior to accepting employment, the former SPA chief operating officer obtained a formal advisory opinion from the full Ethics Commission. The commission issued a binding opinion finding no prohibition to his accepting this employment. The opinion remains confidential, and we were not allowed to review the opinion nor the information provided to the State Ethics Commission (see p. 2).

Since the situation described above could be allowable under current state ethics law, we have concluded that the current law may need to be strengthened. When it is legal for a public official to accept a job from an individual who recently benefitted from a contract negotiated by that public official, there is increased potential for conflict of interest.

Also, enforcing S.C. Code §8-13-760 can be difficult because it requires ongoing knowledge of the former public employee's responsibilities in his new job. The ethics statute could be strengthened by prohibiting public employees or officials who directly participate in a procurement from accepting *any* job involving the same contractor and/or contract, for a specified period of time after the contract is executed.

Recommendation

10. The General Assembly should consider amending S.C. Code §8-13-760 to prohibit employment of a public official by an organization or a person who has benefitted from a recent procurement in which the public official directly participated. The General Assembly should consider prohibiting such employment for a specified period of time after the procurement.

RDA Board Member

In the course of reviewing minutes for board meetings, we noted that one RDA board member is a partner in an accounting firm which has provided financial services to several tenants, including CMMC, the RDA's largest tenant, and to the owner of CIP. This member abstains from voting when the board votes on subleases and other matters having to do with these tenants. Votes directly involving subleases to this member's clients have occurred in 26 out of the 49 board meetings that were held from 1997 – 1999, and accounted for a total of 42 (16%) of 263 votes taken by the board.

RDA board members are appointed by the Governor and confirmed by the Senate, based on nominations by local governments in the Charleston area. The Governor's Office has a procedure for screening nominees to state boards. Part of this procedure consists of a two-page application form, which contains the following question: "Do you have any interest in any business that has, is, or will do business with the State of South Carolina or the entity for which you are applying?" This board member answered "no" to that question when he applied for re-nomination to the board in 1999.

Under state ethics law [S.C. Code §8-13-700(B)(4)], public officials must be excused from voting on matters in which the potential conflict of interest exists. This board member may be less than effective since he cannot participate in board decisions involving major subleases.

Because RDA board members are appointed based on nominations from Charleston, Dorchester, and Berkeley counties and the city of North Charleston, these local governments may need to be more involved in the screening process.

Compliance With the Freedom of Information Act

One of our audit objectives was to determine whether the RDA has complied with the South Carolina Freedom of Information Act (FOIA). We reviewed RDA records pertaining to board meetings and requests for information from 1996 through January 2000, and found that the RDA is generally in compliance with the FOIA. However, we have some concerns which are discussed below.

Negotiations With the State Ports Authority

The FOIA allows certain matters to be exempt from public disclosure, including, "Documents of and documents incidental to proposed contractual arrangements . . ." [S.C. Code §30-4-40 (a)(5)]. A meeting may be closed to the public for several reasons, including, "Discussion of negotiations incident to proposed contractual arrangements . . ." [§30-4-70 (a)(2)]. Therefore, the RDA and the State Ports Authority were in compliance with the FOIA when they held confidential negotiations during 1998 and 1999. These negotiations concerned a potential sublease for Pier Alpha and the properties at the north end of the complex, and then later concerned the substitution of Pier Zulu and other property formerly subleased to Charleston Shipbuilders Incorporated (CSI) (see p. 15). SPA officials requested that these latter negotiations remain confidential, in part, because of the potential for embarrassment to the two agencies should they not be able to reach an agreement on the substitution of the properties.

The purpose of the FOIA is to ensure that government activities are open to the public; however, exemptions in the law allowed the RDA-SPA negotiations to be kept confidential.

- In February 1998, SPA officials attended a closed door meeting of the RDA board where they formally presented their proposal to sublease Pier Alpha and other properties.
- Details of this proposal were not made public until the RDA board voted in August 1998 to approve the sublease of Pier Alpha to the SPA.
- In December 1998, the RDA board publically withdrew this approval and instead approved subleasing Pier Zulu and the surrounding area to the SPA.
- Details of the final agreement were not publically released until May 1999, after the RDA and the SPA had signed the sublease.

The RDA allowed inadequate time for public review or comment before it announced it would sublease the central area of the complex to the SPA. The RDA had received at least 12 FOIA requests between June 1998 and April 1999 asking for information on the former CSI properties and any SPA subleases; none of these were granted until May 1999. There may have been interest by other businesses in obtaining subleases of the former CSI properties, and also possible community opposition to any lease between the RDA and the SPA.

On August 2, 1999, the Office of General Services of the B&CB held a public hearing on the sublease between the RDA and the Ports Authority. The B&CB gave final approval to the sublease on August 12, 1999.

The purpose of the FOIA is to ensure that government activities are open to the public; however, exemptions in the law allowed the RDA-SPA negotiations to be kept confidential. While the FOIA does not require disclosure of lease negotiations until after the contract has been signed, it does not prohibit any disclosure of lease negotiations if the agency wants them to be public. Since these negotiations were between two public agencies, a more open process may have been appropriate, and may have allayed the concerns of the community about a sublease with the SPA.

Executive Sessions

The FOIA requires the board to announce the specific purpose of the executive sessions, and in June 1998 the S.C. General Assembly passed amendments which required public bodies to identify the specific exemptions to the FOIA that applied before going into executive session. We found that prior to August 1998, the board did not announce the specific purpose for the executive session but said only it was for "contractual matters." In its meeting on August 4, 1998, however, the board began to announce the specific items that would be discussed in executive session and what exemptions of the FOIA applied. Also, since 1998, the RDA board has become more willing to discuss some lease arrangements in public session.

Public Access to Records

From 1996 through January 2000, the RDA received more than 80 written requests for information. For the most part, the RDA provided the information requested. Three requests were denied outright on the grounds that the information requested was exempted from public disclosure by the FOIA; specifically, §30-4-40(a)(5) (see p. 30). We noted eight requests that were denied on the grounds that the RDA had no documents "responsive" to the request.

Fees Charged for Records

The FOIA allows the RDA to charge fees not to exceed the actual cost of searching and copying records, and the records must be furnished at the lowest possible cost. The agency may charge a reasonable hourly rate for making records available to the public.

According to staff, the RDA usually charges fees of about 20¢ to 25¢ a page for the costs of copying and searching records. In FY 98-99, the agency had revenues of $1,316 from FOIA requests. On two occasions, the requesters may have been discouraged from pursuing an FOIA request because of the excessive cost involved. For example, one requester was told that the material she wanted would cost $5,750 to research and copy.

Fifteen-Day Response Period

The FOIA also requires that, upon receiving a written request for records, the public body shall have 15 business days to notify the person making the request of its determination as to the public availability of the documents. We found several occasions where the RDA took more than 15 work days to notify the requester if the documents sought were available.

Recommendations

11. Whenever possible, the Redevelopment Authority should discuss leases in public session, especially leases with other public agencies such as the South Carolina State Ports Authority.

12. In compliance with the FOIA, the Redevelopment Authority should ensure that it responds to written requests within 15 work days as to the public availability of the documents requested.

Appendices

Appendices

Schedule of RDA Revenues and Expenditures

While the Redevelopment Authority does not receive an appropriation from the state general fund, the "rural development" funds it receives are state income tax money paid by federal employees who work at the complex. Since federal tenants pay no rent for the property they lease at the complex, this offsets the lost revenues to the RDA. The federal grants are earmarked for specific purposes, and the Navy also requires the RDA to spend lease income on improvements to the complex. The rural redevelopment funds carry no such restrictions as to their use.

RDA Revenues and Expenditures, FY 94-95 Through FY 98-99

	FY 94-95	FY 95-96	FY 96-97	FY 97-98	FY 98-99
Revenues					
Federal and Special Revenue	$312,823	$759,591	$2,318,703	$3,334,715	$2,514,698
State Funds*	$150,990	$1,071,971	$2,175,514	$3,171,044	$2,443,217
Rents	$0	$102,304	$583,899	$1,441,170	$2,210,190
Other Revenue	$114,538	$105,788	$199,695	$131,306	$257,809
TOTAL	**$578,351**	**$2,039,654**	**$5,277,811**	**$8,078,235**	**$7,425,914**
Expenditures					
Payroll	$240,400	$465,882	$443,802	$511,006	$652,411
Benefits	$49,206	$88,257	$96,467	$104,182	$124,574
Travel	$6,421	$25,473	$28,848	$25,761	$14,717
Equipment and Supplies	$12,237	$39,116	$64,358	$112,697	$154,984
Contractual	$180,340	$961,211	$2,597,101	$3,723,591	$3,156,664
Renovations, Capital Outlay	$0	$248,732	$214,538	$7,638	$17,381
Debt Service	$0	$8,677	$34,706	$45,282	$39,351
Other	$35,339	$85,222	$134,695	$93,581	$410,528
TOTAL	**$523,943**	**$1,922,570**	**$3,614,515**	**$4,623,738**	**$4,570,610**
Other Financial					
Proceeds from Long-Term Borrowing**	$0	$275,000	$0	$0	$0
Excess of Revenues Over Expenditures	$54,408	$392,084	$1,663,296	$3,454,497	$2,855,304
Fund Balances at End of Year	$54,408	$446,492	$2,109,788	$5,564,285	$8,419,589

* Rural Redevelopment Income.

** A bank loan that the RDA used to renovate a building that currently is subleased to the SC Department of Health and Environmental Control.

Source: RDA Annual Financial Reports, FY 94-95 through FY 98-99.

Appendix A
Schedule of RDA Revenues and Expenditures

Agency Comments

Appendix B
Agency Comments

September 11, 2000

Mr. George L. Schroeder
Legislative Audit Council
1331 Elmwood Ave., Suite 315
Columbia, SC 29201

Re: Final Comments on a Report to the General Assembly entitled *A Management Review of the Charleston Naval Complex Redevelopment Authority.*

Dear Mr. Schroeder:

The Charleston Naval Complex Redevelopment Authority (the "RDA") appreciates the opportunity to comment on this report. My staff and I have invested a great deal of time in trying to assist your auditors by providing information as well as explanations. However, no amount of effort on our part can substitute for a basic knowledge of real estate development. This shortcoming is evident in the "findings" contained in your report.

I understand that my entire comments will be inserted as a part of the overall report to the General Assembly. My Staff and I have spent hundreds of man-hours defending the RDA against uniformed, pre-conceived and false "findings" made by your audit staff. It is my hope that members of the General Assembly will question the way that these audits are prepared and save other state agencies from having to go through this ordeal. An "audit" begins with many accusations against the subject agency and as these accusations, one by one, are proven to be false, the audit team feels more pressure to uncover new "findings" and is reluctant, even defensive, about deleting further "findings" from their report. A practical way to correct this flaw would be to mandate that the agency be allowed to hire an "advocate" to work daily with the audit team or even to hire an outside expert on the nature of their business, rather than have to submit to an audit performed by people who are uneducated and unqualified in the business of the agency.

Page v Synopsis

In February 1995, the RDA issued a request for proposals to companies interested in subleasing all or a part of the naval complex. Companies were permitted to submit proposals for different combinations of property

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and with different methods for determining rent. It is therefore not clear how the RDA was able to objectively rank the companies.

RDA Comment:

One of the first facts learned in the study of real estate is that real property is unique. Values (and therefore rental rates) vary with each individual and unique parcel of real estate. It is inaccurate to state that companies were permitted to submit proposals . . . . with different methods for determining rent. These proposals were offers to rent, not final determinations of rent. It was fairly simple to negotiate a fair rental rate using established appraisal methods. In regard to "objectively" ranking the companies, the LAC auditors were given a copy of the RFP. On page eleven (11) of that document, seven (7) criteria are listed for the evaluation of all proposals. These criteria are largely subjective, not objective. The final evaluations were made, in writing, using the criteria listed in the RFP. This bullet is not a "finding", it is a comment intended to imply that the ranking of the proposals was inequitable. The comment is unsupported and offensive and should be deleted from this report.

Page vi - Synopsis

Since 1995, the RDA has leased out piers, buildings and other properties without adequate marketing. As a result, properties have been subleased without fully determining the level of interest from other potential tenants. (Page v) Therefore the RDA may have limited the pool of qualified businesses seeking to bring new jobs and economic development to the area.

RDA Comment:

This is absolute nonsense. This "finding" seems to be based on a self-imposed requirement by the auditors to address the complaints raised by those companies who claim that they have been excluded from the process. By stating that the RDA "may have limited the pool of qualified businesses" the auditors are admitting that they have made no attempt to base this conjecture on actual economic or market studies. Furthermore, this report contains absolutely no evidence of any limitation in the "pool of qualified businesses" and, insofar as we are aware, no such evidence exists. The RDA has taken a marketing approach, as recommended by its consultant, which has made Charleston the number one job-producing base redevelopment project in the history of base closure. Since 1997, over 700 information packets have been distributed, by request, to companies all over the country seeking property at the Naval Complex. North American Realty Services (NARAS), the New York based consulting firm that prepared our reuse strategy, is eminently more qualified to recommend a marketing plan than your LAC auditors. NARAS understood that it was best to use "state or local sources" and it was ineffective to begin an "organized marketing plan" prior to the

establishment of zoning or the ownership of the property. Mr. Theodore Pugh, our NARAS consultant calls your statement "inaccurate". As you are aware, Mr. Pugh's credentials are impressive. Inasmuch as you have chosen to ignore his opinion, I requested that you produce the qualifications and educational background of the auditors who contributed to and/or reviewed this report. Your September 6, 2000 "snowplow defense" letter did not provide this information to me and I do not share your confidence that this report is balanced, accurate, and unbiased. I will comment further on this later in this document. This "finding" is only an opinion and has no basis in fact.

Page vi - Synopsis

The RDA has not established written asking prices ~~for rent nor has it used appraisals as a factor in determining the rent it negotiates for~~ when renting its available buildings and piers. (See page 11).

RDA Comment:

This is an example of the difficulty experienced by your auditors in trying to understand the nature of our business. To begin with, rental rates are not "asking prices". The auditors seem to believe that it is appropriate to rent out the entire naval base as if it were waterfront condominiums or motel rooms. I suppose they think that the RDA should just establish a rate of say $15.00 per square foot for all offices; $10.00 psf. for industrial property; $2.50 psf. for warehousing; $10.00 psf. for educational space; $12.00 psf. for housing, etc. and disregard all other factors like location (which is fairly important) and combinations of properties. Later I assume they would suggest posting these rates on a website to insure that we have no room for negotiation with potential tenants. The first part of this very naïve "finding" is completely unrealistic and impractical. Your auditors may believe that they have addressed my earlier comments by inserting the word "available" in the statement, but they have not. The first step in estimating a rental rate, as published by the Appraisal Institute, is to identify the property to be rented. I am reasonably sure that your auditors envision simply determining what properties go together in advance and advertise them under a single rate in a brochure or in the housing section of the newspaper. Any real estate professional would recognize the absurdity of this notion after a tour of the base and only a few of its 614 structures. How would your auditors identify the parcels to be rated? Does each building represent a parcel? Since all of the land is under the single ownership of the Navy, how much land would your auditors assign to each parcel? What is their suggested rate for the Admiral's home? How about the combination of the Admiral's home and H &I? How about the combination of the Admirals House, H&I, Pier Bravo and six acres? I hope you are beginning to understand the absurdity of this "finding". Our procedures, which you confirm that we are following, call for us to respond to the specific needs of prospective tenants by identifying properties or

groups of properties. Only after a specific property has been identified may a supportable rental rate be estimated. In every instance, the RDA has established an asking "price" (rental rate) from which to negotiate following the identification of a site. Your broad statement that we do not establish a rental rate is ***false****. In some cases, we have identified a single purpose building or groups of buildings and have established a working rental rate for these structures. In the near future, we plan to identify certain industrial properties and offer them to the public under an RFP, but we do not plan to establish an asking "price" (rental rate). We will put that burden on the prospective tenant.*

I am pleased that you deleted the second part of your "finding" which stated that the RDA had not used appraisals as a factor in determining the rent it negotiates for buildings and piers. This "finding" was completely ***false****. I am a State Certified General Real Estate Appraiser with 30 years experience and I hold several professional appraisal designations. The appraisal firm of Tercorp, Inc. prepared an "as-is" appraisal for the RDA to be used as a tool for estimating rental rates and to support future conveyance negotiations. I have referred to that appraisal for almost every leasing negotiation. Prior to that, I relied on available data from my past experience and other sources. Also, I have had prepared eight separate appraisals of property on the naval base for negotiation purposes and I have ordered eight additional appraisals for current projects. Your auditors were provided copies of all of these appraisals and were fully briefed on how they were being used. What did they think we were using the appraisals for? I cannot understand how the auditors could completely miss these facts when they asked for the information specifically. You were correct to delete this "finding".*

Page vi - Synopsis

The RDA has not adequately controlled the process by which its tenants sublease properties to other organizations. Tenants have sometimes not obtained the required prior approval. In addition, the RDA has not sufficiently controlled the rental rates charged by its tenants to other organizations.

RDA Comment:

To over-simplify, each total property has its own assets and liabilities. Our rates reflect both assets and liabilities. Our tenant may sublease to a secondary subtenant a portion of his property without obligating the secondary subtenant to his proportional share of liabilities. Therefore, the rental rates may be much higher for the secondary subtenant. These subleases are negotiated between competent adults. Why should we "control" these rates? Of course by using the term "sufficiently controlled" you recognize that indeed we do check each secondary sublease to determine if the rate is "reasonable" but we have no problem allowing market forces to determine market rents. Contrary to

what your auditors may believe, these rents cast no reflection on the value of the original sublease. As you know, the consent of the RDA is required prior to the subleasing of any property. Its true that tenants have sometimes not obtained the required prior approval. These tenants risk an Event of Default and eviction for these actions. What other "adequate" controls would your auditors have us impose? This is another attempt to imply that something is improper without any substantial factual basis for the implication. Nothing is improper, impractical, or unusual in the way we handle secondary subleases.

Page vi - Synopisis

When the RDA took over the management of Navy-owned equipment, the Navy's inventories were inaccurate and incomplete. The RDA, however, did not immediately conduct a more complete inventory of its own. While theft may have occurred during the early years of the RDA's management of the naval complex, poor record-keeping has made it impossible to determine what was stolen.

RDA Comment:

Your auditors are correct to say that Navy inventories of Navy-owned equipment were inaccurate. You state later in the report that you found no material problems with the RDA's current inventory tracking system. However, this paragraph suggests that the RDA is somehow at fault for not conducting an inventory of thousands and thousands of personal property items that are not owned by the RDA and not under the control of the RDA. The RDA did not have a master lease of the property. Our system, as explained to your auditors, established accountability of these Navy-owned articles only when a sublease was executed. For the first few years, most of the buildings and related personal property were under the jurisdiction of the Navy, not the RDA. Also, Navy-related operations such as the Environmental Detachment plundered and confiscated this property making no attempt to notify the RDA or even to provide an inventory list. To attempt to conduct an inventory of this property under these conditions would have been useless and a total waste of time and money. It is true that the RDA adopted the Navy's inventory list for our earlier subleases, but this was just prior to base closure and an independent inventory would have delayed leasing activity for months. Furthermore, it is patently unfair to speculate "theft may have occurred" and then attempt to justify the speculation by stating that it is impossible to determine that anything was stolen. The "finding" turns logic on its head and cannot possibly be a sound auditing practice.

Page vi - Synopsis

We found no material problems with the RDA's current inventory tracking system, taking into consideration the inaccuracy of the Navy's initial

inventory and the difficulty of monitoring equipment that is constantly being relocated over a widespread area. However, the RDA does not hold tenants accountable for Navy-owned equipment that is damaged or missing, and does not charge for the use of extra equipment relocated from other facilities.

RDA Comment:

Your report contains no supporting evidence for the claim that the RDA does not hold tenants accountable for equipment nor have you specified a situation or case where this has occurred. In fact, my staff does a final walk-through inspection, accompanied by the tenant, to determine what deficiencies need to be addressed prior to termination. The one example you give involving four (4) items out of fifty concerns a tenant who is still operating on the base and will be held accountable for facility deficiencies.

Page vi - Synopsis

The RDA's system for signing out building keys is ineffective as a means of controlling access to nonleased or unoccupied buildings. There also is little monitoring of vehicles exiting the complex. We observed no effort being made by gate guards to restrict access to the naval complex.

RDA Comment:

The key system being used is the most practical system since, as you state, the RDA has no power to enforce. In regard to the gate guards, your auditors need to understand that this is no longer a military facility. It is an area occupied by private businesses. Which customers would our tenants identify as being authorized or unauthorized? This "authorization" concept has been invented by your auditors, not by my staff or staff contractors. I informed your auditors that during the evening hours, the gate guards may question a suspicious looking vehicle, but generally, I directed them to allow all vehicles during the day to pass to allow the free-flow of business. If they remember, my comment was that "the Navy kept the public out for a hundred years and now we are trying to invite the public inside". You don't accomplish that by treating this facility like an exclusive country club. Obviously, we are concerned whenever there are thefts and break-ins, but a traffic jam at the gate due to vehicle checks is not the answer.

Page vi - Synopsis

The RDA awarded a sublease with an option to purchase to the State Ports Authority for a large portion of the base, including 4 piers and 38 buildings. As with other tenants, the RDA did not adequately market these properties. ~~or include an appraisal of the properties as a factor in determining rent.~~ To make properties available to the SPA, ~~the RDA also rescinded previous lease~~

~~approvals and didn't renew leases held by~~ several small businesses ~~in order to sublease properties to the Ports Authority~~ were not permitted to renew their subleases. (See page 21)

RDA Comment:

My consultant and I strongly disagree with the auditor's opinion regarding marketing (see comments above). Following my past comments, the auditors deleted the false portion of their statement, but were somehow compelled to make some statement regarding the renewal of secondary subleases. I remind the auditors that these secondary subtenants entered into their secondary subleases with the full knowledge of the short-term nature of the arrangement. The RDA was not a party to these transactions. They should, at least, mention that the RDA allowed those secondary subtenants, upon request, to stay for the remainder of their secondary sublease term, although the RDA was not legally compelled to do so.

Page vii - Synopsis

The State Ports Authority, in August 1999, awarded a license to a private company called Charleston International Ports (CIP) to operate a cargo terminal on properties subleased from the RDA. The SPA official who negotiated the sublease with the RDA and the license with CIP resigned in January 2000 and accepted a job from the owner of CIP. While not employed directly by CIP, he is involved in matters concerning the CIP license. The State Ethics Commission, in a confidential opinion, found no prohibition to this employment. However, we have concluded that the current ethics law may need to be strengthened.

RDA Comment:

We are the RDA, **not the SPA**. Please explain how this "finding" relates to a Management Review of the Charleston Naval Complex Redevelopment Authority. The RDA was unaware of any of these actions that occurred following the execution of the contracts and certainly played no part in them. This irrelevant "finding" implies that the RDA officials were being "bought" or unduly influenced. I requested that your senior auditor insert, at a minimum, a statement that the LAC was not implying any participation or guilt by the RDA. Your failure to insert this statement leads me to assume that you are accusing the RDA of a wrongdoing.

Page vii - Synopsis

The RDA is generally in compliance with the state Freedom of Information Act (FOIA) regarding access to RDA meetings and records.

RDA Comment:

The RDA has made a conscientious effort to be even more open in its activities over the past two years or so.

Page 1 – Audit Objectives

The report makes it clear that the audit objectives are to determine whether the Redevelopment Authority has:

1. Complied with state rules and regulations regarding subleases of properties.

2. Adhered to sound business practices regarding subleases of properties.

3. Implemented an adequate system for safeguarding equipment, furniture, and similar property owned by the U. S. Navy.

4. Maintained a proper relationship with the South Carolina State Ports Authority, consistent with the statutory mission of the RDA.

5. Complied with the S. C. Freedom of Information Act.

RDA Comment:

*In the case of objectives 1, 3, and 5, the answer seems to be **yes** based upon the information reported on pages v, vi, and vii and related chapters in the report. However, the answers to objectives 2 and 4 are difficult to glean from the innuendos, irrelevant and inappropriate remarks and false statements contained in the body of the report. Where is your final statement regarding these objectives? After reading and verifying the information provided here, the reader should conclude that the answers to objectives 2 and 4 are also **yes**. This means that the RDA has conducted its business in a proper manner. The reckless accusations made during the past years against the RDA have been shown to be without foundation by the U. S. Navy, FBI, SLED, and now by the Legislative Audit Counsel.*

Page 2 – Scope Impairment

On page 27 we describe a possible conflict of interest involving a former state employee and a sublease between the RDA and the State Ports Authority.

RDA Comment:

How can your auditors say that the conflict of interest, if one existed, involved the sublease between the RDA and the State Ports Authority? The subject state employee was the chief operating officer for the SPA and was fully empowered to execute the sublease between the RDA and the State Ports Authority with no possible conflict of interest. The possible conflict of interest would only be associated with the secondary sublease between the State Ports Authority and CIP. The RDA was not a party to this secondary sublease. Your auditors continue to make reckless statements. This "finding" should be corrected immediately on this page and in Chapter 4 relating to this issue.

Page 11 – Requirements of State Law

According to an attorney with the Budget and Control Board, the RDA has flexibility in the way it selects tenants as long as potential tenants are made aware of the availability of properties, are given the opportunity to submit proposals, and the results are "fair."

RDA Comment:

I am unaware of any document from an attorney with the Budget and Control Board that outlines our overall procedure in this manner. The description in this paragraph applies only to the competitive proposal process, if chosen by the RDA. The term "potential tenants" could mean anyone in the world. Through general publicity and the efforts of our local development agencies, the availability of "properties" at the Naval Complex is well known locally and regionally. The availability of "specific" properties is determined only in response to inquiries from "specific" potential tenants and only if the RDA determines it is in its best interest. General publicity regarding sites will only be issued after being identified for competitive proposals by the RDA. The RDA may consider for negotiation any and all proposals if they are complete and responsive. The availability of properties; opportunity to submit (solicited) proposals; and the results being "fair" exist only in the "Competitive Proposal" method. The auditors should keep in mind that no person or business has the "right" to be selected or to lease property at the Naval Complex. Since as far back as the original CNCRA1 proposal, neither the State of South Carolina nor the RDA has had a mandate to lease facilities to a specific proposer or proposers. Rather we represent the best interests of the State in all of our transactions.

Page 12 – Leasing Methods

There are different methods potentially available to state agencies for leasing real property.

RDA Comment:

The same attorney to whom you refer will verify that competitive bidding" is **not feasible** for leasing Naval Complex property.

Page 14 – Marketing of Properties

The RDA has not adequately marketed the properties at the naval complex and in general does not use advertising. As a result, properties have been subleased without determining the level of interest from other potential tenants, which may have reduced the pool of qualified businesses able to bring new jobs and economic development to the area.

RDA Comment:

I have already addressed the absurdity of this statement, however, I thought that I would include some quotes from a letter addressed to me from Mr. Theodore Pugh representing Master Development Management Company so that the readers of this document may also review portions of that letter on-line.

My immediate response is that the statement is inaccurate. In order to shed light on why I believe the statement is a false allegation, I've gone back to 1998, when the report entitled "Reuse Strategy and Business Plan for the Charleston Naval Complex" was submitted to the RDA as a part of our engagement. I directed a team of real estate professionals to evaluate the CNC's land and buildings, create a strategic reuse and development plan, devise a marketing program, and provide a financial foundation to justify pricing for the Navy's multi-year process that required an understanding of the project's physical, financial, environmental and political elements. All to be addressed in a marketing program created to build on the RDA's progress, and set the tone for future reuse and development by the private sector.

By 1997, when my engagement began, the RDA and its predecessors successfully marketed, by a Request for Proposal (RFP) process, a majority of the Base's usable space. Over 4.7 million square feet, or 60% of the CNC's 7.7 million square feet was occupied, keeping in mind that over 1 million square feet was either unmarketable, obsolete, unusable or unsafe, that we ultimately recommended for demolition.

In relation to the Charleston "Trident" area's small, physically isolated market of less than 500,000 people, the enormity of the CNC'c real estate assets and the "interim" 3,000 employees on-site was significant, and accomplished with a locally focused marketing effort and no local city/state outlays.

By contrast, former military bases in larger markets, like Boston (Fort Devens), San Francisco (Presidio), and Philadelphia (Naval Yard) struggled to successfully market, as caretakers prior to federal conveyance, old military buildings and underutilized land "as-is", with little or no infrastructure improvements, environmental contamination, and like impediments, all of which exist at the CNC.

Key to the RDA's successful marketing has been to represent a clear and credible message to the market. That is, knowing what you're selling, i.e. the "opportunity", which until the RDA owns the CNC, will be somewhat limited, until environmental issues are addressed, and the RDA can legally sell land and buildings and convey marketable title.

We understand that since 1998, the RDA , as master developer, is implementing our strategic recommendations, intended to move closer to, and bring some definition to the long-term future opportunity for private sector businesses to invest in the CNC. . . .

When the RDA can represent in its marketing program that it owns and controls the property, then private sector businesses, developers and investors will take interest in zoned, subdivided land and buildings made available for sale.

The allegation that advertising infers adequate marketing is incorrect, particularly in small markets where the RDA's marketing has included continuous outreach, to the community's businesses, political leaders and decision-makers, of the available opportunities at the CNC.

In my opinion, the RDA has admirably fulfilled its mission objectives to date as custodian of the Navy's property, and is well positioned, as future owner, toward achieving the ultimate goal to turn the CNC over to the private sector for long-term ownership and capital investment, all to the benefit of the residents of North Charleston, the Trident area, and the State of South Carolina.

Sincerely yours,

MASTER DEVELOPMENT MANAGEMENT COMPANY

Theodore D. Pugh
Managing Director

The full text of Mr. Pugh's letter, that your auditors have chosen to ignore, has been submitted to you for distribution. Readers of your report may also obtain a copy from my office.

Also your auditors list several instances where the RDA chose a successor tenant or conducted a limited competition rather than doing an open solicitation. Again, they are attempting to imply that our process is improper. ***There is no legal requirement that the RDA conduct open competition for properties at the Naval Complex****. The SC Budget and Control Board has stated that to do so would not be sound business practice. In each of the cases cited in this report, the RDA had sound business reasons for making its decisions and your auditors are ignoring the economic, physical, and political forces that affected these decisions.*

By either not understanding or ignoring the facts presented by Mr. Pugh, the auditors are giving an opinion that is both uniformed and inaccurate. In an attempt to bolster their position, they have listed the CMMC and the State Ports Authority long-term leases as justification. These subleases were just completed in the last few months and both tenants are well-established Charleston businesses. In addition, the CMMC selection was a direct result of our initial 1995 marketing effort through an RFP. CMMC was found to be the best selection for operation of the shipyard following inquiries made around the world. What possible advantage would there have been to repeat that process? Also, if your auditors have read Mr. Pugh's letter or even his Strategic Plan,

they have discovered that establishing the Port's cargo handling facility was one of his early recommendations.

Page 16 – Potential Effects of Increased Marketing

We found that industrial parks in South Carolina and closed military bases in Pennsylvania and California have used a variety of methods to market their properties. Examples of these methods include websites, brochures, ongoing advertising in print media, and the use of real estate brokers. None of these marketing methods have been used by the RDA except for advertising in the print media, which the RDA did only in 1995.

RDA Comment:

Our consultant said in his letter that the "allegation that advertising infers adequate marketing is incorrect, particularly in small markets where the RDA's marketing has included continuous outreach to the community's businesses, political leaders and decision-makers of the available opportunities at the CNC." We are the number one job producing base redevelopment project in the history of base closure. The auditors fail to mention that none of these bases has produced as many jobs as the RDA in Charleston. Closed military bases across the country are not considered to be comparable simply because they are closed. The value or market potential of a closed base in California has no relationship to any parcel of real estate in South Carolina. The auditors have come to the conclusion that if closed bases in California and Pennsylvania have websites, brochures, ongoing advertising and other activities that the RDA should use these tools also. This is absurd

Page 16 – How Rent is Determined

The RDA has not established written asking prices when renting its available properties. There are two potential negative effects of not having written "asking rents." First, the number of prospective tenants interested in the naval complex may be reduced because the degree to which the RDA's rents are lower than those at alternative locations may not be widely known. Second, public confidence in the leasing process may be reduced because the process of determining rents is less open and less understandable to the public.

It is important to note that written asking rents would not preclude negotiated discounts based on factors such as jobs or commitments to renovate the properties, as discussed above. Written asking rents would also not preclude negotiated discounts for tenants who lease multiple properties.

RDA Comment:

These are perhaps the most laughable of anything your "experts" have written so far. They seem to be trying to equate our leasing with procurement and it is not. If I understand the way your bureaucrats are rationalizing their pre-conceived notions, it seems that they are saying that by not advertising "asking rents" we are missing out on the companies seeking out cheap space with little or no investment. Also, as I have repeated many times to your auditors, we are not interested in taking business away from local real estate brokers and owners which is exactly what they are suggesting. Businesses will come to the Naval Complex because of its location, not for cut-rate rents. Your auditors continue to ignore the overall obligations of maintenance and other responsibilities that are passed on to our tenants. What is the meaning of their "public confidence" statement? Do any of your auditors even understand how to determine an asking rent? How much does the public know about determining or understanding rents? Asking rents are "negotiated" by real estate professionals. Major businesses looking for sites are not going to look for an "asking rent" they are going to make their own analysis before negotiations begin. Your auditors' "public confidence" statement sounds really profound but it is meaningless nonsense. They also thought it was important that the RDA could still "discount" its asking rents to an even lower rental rate. Perhaps, it has not occurred to them that our ability to negotiate a rate higher than our asking rent for any number of reasons would be very difficult.

Page 16 – How Rent is Determined

Revenue-based rent is more subject to misinterpretation and fraud than fixed rent.

RDA Comment:

Based on nothing more than their personal opinions, your auditors are saying that we should not use percentage leases. Percentage Leases are a bone-fide tool used in the real estate market and are quite manageable, especially if the leases are based on "gross revenues" as these were. Perhaps the auditors were thinking of "net revenues" which are harder to determine. This choice of lease proved to be very innovative and represented a very fair exchange in a market that was undefined.

Page 17 – Controls Over Secondary Subleases

The Mare Island Conversion Division, which is developing a former naval shipyard in California, also requires its tenants to obtain written consent prior to leasing out property . . . .give Mare Island 30 days notice of their intent to sublease . . .pay an administrative fee. In addition, tenants are

not permitted to profit from secondary subleases. Any excess rent tenants receive from secondary subtenants is required to be paid to Mare Island.

RDA Comment:

I mean no offense to the redevelopment team at the City of Vallejo, but to be compared to the Mare Island Conversion Project is insulting. Your auditors assume that the business practices of a closed base in California are relevant and preferred. For your information, a representative of the City of Vallejo came to Charleston as have representatives from Alabama, Guam, Maryland, England, Hungary, Japan and Germany to get tips on how to be successful from our operation. A report by the National Association of Installation Developers (NAID), published in July of 1999, said that the Charleston Naval Complex Redevelopment Authority ***leads the nation in the creation of new jobs (3,441)*** *as compared to all closed bases in the 1990's and backed their findings with published statistics. The Mare Island Project has severe problems concerning its location, use and jurisdiction. That same report lists Mare Island Shipyard at the bottom of the list of 60 bases having created only 293 jobs (200 of them were temporary 9-month movie/tv production jobs). In my prior comments I asked that you include this important information in your report, but I see that you did not.*

Page 18 – Recommendations:

1. If the Redevelopment Authority decides to issue a request for proposals to lease out property in the future, it should require that each company submit a proposal for the same property and offer a specific amount for rental payments.

RDA Comment:

This is a reasonable recommendation. However, the RDA does not intend to require that a proposer offer a specific amount for rental payments. We may leave it to the proposer to define the limits of his financial offer.

2. The Redevelopment Authority should conduct ongoing marketing of naval complex properties available for lease or sale. When establishing a marketing plan, the Redevelopment Authority should consider the merits of a website, print advertisement, brochures, and real estate brokers.

RDA Comment:

On advice from our consultant, the RDA did not waste time and money on extensive marketing prior to reasonable zoning and ownership. However, the time is approaching to begin an organized marketing program. This recommendation is reasonable and the RDA has already approved hiring a consultant to begin the process.

3. When marketing naval complex properties available for lease or sale, the Redevelopment Authority should include written asking rents or asking prices, subject to negotiation.

RDA Comment:

This recommendation does not reflect the comments made in the body of your report. The body of the report speaks in the past tense, saying the RDA "has not adequately marketed the properties." There is a great difference between the past and our future plans for marketing the base. In a controlled setting where the RDA is defining the marketable parcels, the auditor's recommendation is fine. However, the publishing of an asking rent or sales price is optional.

4. The Redevelopment Authority should not base rental payments on revenues generated by tenants.

RDA Comment:

The auditors have provided no convincing arguments or supporting evidence to support this opinion. The RDA disagrees with the recommendation.

5. The Redevelopment Authority should ensure that its tenants obtain written consent before subleasing out property. Also, the Redevelopment Authority should explore methods for monitoring and controlling rental rates charged by tenants to secondary subtenants.

RDA Comment:

Short of stationing an employee on the premises of every business site to monitor day-to-day activities, it is unclear how the LAC proposes that we ensure this written consent for activities of which we are unaware.

Page 20 – Accountability for Equipment

We could find no evidence that the RDA, in either its leasing or inventory process, holds tenants accountable for Navy-owned equipment.

RDA Comment:

*Actually, they have found no evidence to indicate that the RDA does not hold tenants accountable. On July 28, 2000, I submitted a 25-page letter to your auditors documenting our actions to hold tenants accountable in every aspect of their contractual agreement with the RDA. Included in that document was correspondence requiring compensation to the RDA for the damage to two $20,000 roll-up doors and a building elevator. Obviously, your auditors do not define these things as equipment, and are therefore trying to make it seem as though the RDA makes no efforts towards accountability. This is **false**. The simple explanation is that only a few tenants have left the Naval Complex and our accountability for their equipment has been satisfactory.*

> The Redevelopment Authority does not ~~include~~ specifically show how the value of equipment is factored ~~in~~ into determining rent (see page 11). A sound business practice would be to determine the rental value of equipment that accompanies buildings being leased.

RDA Comment:

*After I was able to prove that their original finding was **false**, your auditors modified their finding rather than deleting it, rendering the modified finding meaningless. The rental rates negotiated for existing buildings cover, in part, the rental value of equipment. Many of the old dysfunctional buildings in the shipyard and other areas have little or no value without access to equipment and fixtures.*

> The RDA does not charge tenants for the use of extra equipment relocated from other facilities or for leased items that are damaged or missing. A staff person at a former naval shipyard in California stated that equipment there is leased to tenants at a separate rate based on its original cost, and lease rates are adjusted to reflect any additional equipment the tenant obtains from other facilities. The RDA does not charge tenants for equipment, according to a staff member, because its mission is not “profit-oriented”.

RDA Comment:

What is the benefit of establishing excess rental rates on equipment, like Mare Island in California, when your overall rate structure is not producing tenants and jobs? The auditors have lost sight of the main mission of the RDA to create jobs, not maximize our rental profits. The staff member who is quoted in this “finding” did not participate in lease negotiations and would not have knowledge of how equipment is factored into these negotiations.

Page 21 – Equipment Taken from the Complex

In May 1996, a former employee of one of the RDA's largest tenants arranged to have Navy-owned office furniture moved to his home in Florida, later claiming that Navy personnel had given him permission to do so. However, Navy procedure at the time of base closure required having the furniture screened by the RDA and then disposed of through the Defense Reutilization and Marketing Office (DRMO). The Navy required the former employee to return the furniture. Once it was finally returned, in April 1999, there was no fee charged for the three years the furniture was used outside the complex.

RDA Comment:

Your auditors acknowledge that it was the Navy's responsibility to settle this issue. They attempt to involve the RDA by referring to the DRMO process, but this furniture was not being sold as surplus, it was taken from the Navy illegally, pure and simple. It was the RDA that discovered the missing furniture and arranged for its return. Your auditors continue to use terms like "no evidence" and "no fee charged" to imply RDA involvement. Why couldn't they say simply that the Navy charged no fee for the three years the furniture was used outside the complex? In the second bullet on page 22, again, the RDA discovered the missing boats and arranged for their return. The third bullet is not an example of "Equipment Taken from the Complex." The loans to the City of North Charleston were made on the record and with the knowledge of the Navy and the subject furniture was of great benefit to the law enforcement and other personnel who serve the Naval Complex. They choose the single negative comment on this page for the left-hand margin comments rather than to emphasize the diligence of the RDA in recovering this property. The results of the SLED investigation revealed that the accusations made against the RDA were bogus. In regard to the left-margin comment that tenants sometimes "relocate" equipment from unoccupied facilities without first obtaining approval, exactly what deficiency in our management process causes this occurrence? Are we responsible for the actions of each and every one of our seventy tenants? Would the LAC auditors have us post auditors to monitor day-to-day activities at every business?

Page 24 - Recommendations

6. The Redevelopment Authority should ensure proper identification of the Hydra Sport boat listed on its inventory by attaching a numbered identification tag to the boat.

RDA Comment:

Thank you for your suggestion. We will attach an identification tag to the Hydra Sport boat as soon as practicable.

7. To hold tenants accountable for Navy-owned equipment and other personal property, the Redevelopment Authority should:

Include the rental value of equipment associated with a sublease in determining the rent amount to be paid.

RDA Comment:

The RDA tenants have signed a sublease document that obligates them to account for personal property items. Exactly how does this recommendation further serve to hold a tenant accountable for the use of personal property?

Charge tenants a fee for the use of additional equipment items.

RDA Comment:

See comments above.

Charge tenants for missing equipment.

RDA Comment:

Prior to the expiration or termination of any sublease, we have and will require tenants to correct deficiencies regarding the real or personal property identified in the sublease. The implication by the auditors that this has not been done is ***false****. For example, the termination agreement between the RDA and Carolina Marine Handling and others for Pier Mike included a reconciliation of all deficiencies and damage. This is also true for the termination agreement with Education Redirection and the pending exit of CSI. All are being pursued legally.*

8. The Redevelopment Authority should not loan Navy-owned equipment and furniture to groups outside the complex.

RDA Comment:

We disagree. The loaning of property, on the record, with full knowledge and signed receipts between the parties just makes common sense. Rather than sit in damp and unheated space, these items can be put to good use by agencies that support the RDA.

9. The Redevelopment Authority should explore alternatives for strengthening both internal and external security.

RDA Comment:

This is a good recommendation and the RDA is currently exploring these alternatives.

Page 21 – Possible Conflicts of Interest

While reviewing the RDA's sublease with the State Ports Authority, we found a possible conflict of interest involving the employment of a former SPA official by a private company.

RDA Comment:

To assist the reader, I will repeat my earlier comments. How can your auditors say that the conflict of interest, if one existed, involved the sublease between the RDA and the State Ports Authority? The subject state employee was the chief operating officer for the SPA and was fully empowered to execute the sublease between the RDA and the State Ports Authority with no possible conflict of interest. The possible conflict of interest would only be associated with the secondary sublease between the State Ports Authority and CIP. The RDA was not a party to this secondary sublease. Your auditors continue to make reckless statements. These statements should be corrected immediately.

Page 28 - Recommendation

10. The General Assembly should consider amending S.C. Code 8-13-760 to prohibit employment of a public official by an organization or a person who has benefited from a recent procurement in which the public official directly participated. The General Assembly should consider prohibiting such employment for a specified period of time after the procurement.

RDA Comment:

This recommendation reveals the bias and/or confusion of the LAC auditors. We have no problem with the concept of the recommendation in that it may prevent the abuse, or the appearance of abuse, by companies or individuals doing business with the state. However, this language is incorrect in that ***the leasing activities of the RDA are not procurement and state leasing, in general, is no longer a part of the procurement code***

*Also, for the convenience of readers, I will repeat my earlier comments. We are the RDA, **not the SPA**. Please explain how this "finding" relates to a Management Review of the Charleston Naval Complex Redevelopment Authority. The RDA was unaware of any of these actions that occurred following the execution of the contracts and certainly played no part in them. This irrelevant "finding" implies that the RDA officials were being "bought" or unduly influenced. I requested that your senior auditor insert, at a minimum, a statement that the LAC was not implying any participation or guilt by the RDA. Your failure to insert this statement leads me to assume that you are accusing the RDA of a wrongdoing.*

> Page 29 – RDA Board Member
>
> In the course of reviewing minutes for board meetings, we noted that one RDA board member is a partner in an accounting firm which has provided financial services to several tenants, including CMMC, the RDA's largest tenant, and to the owner of CIP. This member abstains from voting when the board votes on subleases and other matters having to do with these tenants. . . . .The Governor's Office has a procedure for screening nominees to state boards. Part of this procedure consists of a two-page application form, which contains the following questions: "Do you have any interest in any business that has, is, or will do business with the State of South Carolina or the entity for which you are applying?" This board member answered "no" to that question when he applied for re-nomination to the board in 1999. Under state ethics law [S.C. Code 8-13-700(B)(4)], public officials must be excused from voting on matters in which the potential conflict of interest exists. This board member may be less than effective since he cannot participate in board decisions involving major subleases.

RDA Comment:

*These astonishing comments from the LAC auditors lead me to believe that they either do not understand the concept of "business interest" or they simply are intent on making a malicious attack on this RDA board member. In either situation, I hope that the General Assembly will question the LAC in regard to this statement. Any dictionary will define "interest" as "the right, title, or legal share in something." **This member has never had any right, title, or legal share in any business that has, or will do business with the State of South Carolina or the RDA.** His answer to the application was correct. The comment that he may be "less than effective" is totally without merit or support. The auditors never even considered how many of his abstentions occurred during unanimous or majority votes. Further, this member has served two terms with the RDA and has spent hundreds of unpaid hours away from his business to contribute to our success. This section of your report should be deleted in full with an apology from the LAC board to this hard-working volunteer for the State of South Carolina.*

Page 30 – Negotiations With the State Ports Authority

The RDA allowed ~~no~~ inadequate time for public review or comment before it announced it would sublease the central area of the complex to the SPA

RDA Comment:

*Once again, after earlier findings were proven to be **false**, the auditors simply modified their finding rather than withdrawing it. The above statement is purely subjective and has no supporting evidence. Negotiations preceding a contract are not subject to the FOIA. I am not aware of any requirement of the FOIA that mandates public forums on pending activities of a state agency that are legal and proper. Are we to announce every economic development project in advance to get a consensus? The appropriate contacts were made to ensure that the "swap" involving the SPA would be acceptable to the community.*

There may have been interest by other businesses in obtaining subleases of the former CSI properties, and also possible community opposition to any lease between the RDA and the SPA.

RDA Comment:

Once again these comments seem to be formed around the accusations of other businesses rather than actual facts. It is the responsibility of the RDA to make the hard decisions regarding the most appropriate use of naval complex facilities. The majority of the seventy commercial tenants at the Naval Complex are small businesses. Our reasons for dealing with the SC Ports Authority are well documented. Any alternative uses or "interests" would have been piecemeal and therefore a less-productive use of the property. Perhaps the auditors would like to produce the documents supporting this "community opposition" to the sublease between the parties and state why this "community opposition" should outweigh the blessing of the deal by the City Council of the City of North Charleston.

Page 32 – Recommendations

11. Whenever possible, the Redevelopment Authority should discuss leases in public session, especially leases with other public agencies such as the South Carolina State Ports Authority.

RDA Comment:

We agree with the recommendation and the RDA has made a strong effort to do so in the past two years.

12. *In compliance with the FOIA, the Redevelopment Authority should ensure that it responds to written requests within 15 work days as to the public availability of the documents requested.*

RDA Comment:

I agree with the recommendation and the RDA shall make every effort to comply.

Sincerely,

Jack C. Sprott
Executive Director

South Carolina State **PORTS AUTHORITY**

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Chief Financial Officer

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September 11, 2000

Mr. George L. Schroeder
Legislative Audit Council
1331 Elmwood Avenue, Suite 315
Columbia, South Carolina 29201

Dear Mr. Schroeder:

Enclosed please find the South Carolina Ports Authority's comments on your final draft report concerning the Charleston Naval Complex Redevelopment Authority.

If you should have any questions concerning the enclosed comments, you may call me at (843) 577-8140.

Sincerely,

Peter N. Hughes

PNH/gam

Enclosure

Comments of the
South Carolina State Ports Authority
relating to the report prepared by the Legislative Audit Council
"A Management Review of the
Charleston Naval Complex Redevelopment Authority"
Dated September 2000

Summary Comments

The South Carolina State Ports Authority is mandated by statute to develop waterborne commerce and facilities. The Ports Authority considers it the mission of the Charleston Naval Base Redevelopment Authority to identify those entities which can provide the highest and best use for the former Naval Complex. This concept of highest and best use includes the economic impact to the State of South Carolina. The portion of the Naval Complex now under lease to the Ports Authority has for sometime been planned as a maritime cargo facility. The RDA has looked to the only state agency in South Carolina with maritime cargo experience to assure the appropriate use of this asset as a public marine cargo facility.

The mission statement of the Ports Authority is as follows:

> "The mission of the South Carolina State Ports Authority is to contribute to the economic development of the State of South Carolina by fostering and stimulating waterborne commerce and shipment of freight.
>
> In pursuit of this mission, the Authority will develop, operate and maintain competitive, cost-efficient, highly productive cargo handling facilities in a fiscally responsible manner. The Authority will pursue economic opportunities that support and enhance its core business."

By leasing the subject property to the Ports Authority, the RDA has gained assurance that the facility will be used to the economic benefit of South Carolina. The facility, while operated on a daily basis by Charleston International Ports, will be used in the same manner as other Ports Authority facilities. These facilities are for "public use" and are governed by a tariff that is filed with the Federal Maritime Commission. This tariff and its rules provide assurance that common carriers of freight as well as importers and exporters will be treated on a fair and equitable basis. This is in contrast to private shipping terminals where facilities are used to transport limited types of commodities and are not open for public use.

Therefore, the Ports Authority believes the RDA had the economic welfare of South Carolina in mind when it agreed to lease the property to the Ports Authority.

Other areas of comment

- **Relationship between the RDA and the State Ports Authority**

The Legislative Audit Council "noted some areas in which the Ports Authority received preferential treatment from the RDA. In other aspects, however, the RDA has treated the Ports Authority the same as most other tenants at the complex." The Ports Authority is not aware that it was shown any improper preference.

The LAC report states in part that the RDA took action that favored the Ports Authority over other tenants. In particular, the report on page 26 states that " six companies will not be permitted to renew their secondary subleases and will have to leave the property". The Ports Authority is not aware of any promises made to the businesses by the RDA that would require options to stay for a period longer than the initial term of the leases. It should also be noted that these properties constitute a very small part of the complex under lease to the Ports Authority and none of the leases were canceled in order to effect the Ports Authority's lease.

Lease negotiations with the RDA were conducted in good faith and in compliance with FOIA requirements. The applicable provisions of the FOIA are fully appropriate for contract negotiations and serve the best interest of the public. As noted in the report, a public hearing was held prior to final approval.

•Agreement between Charleston International Ports (CIP) and the Ports Authority

CIP approached the Ports Authority with a concept to develop a public cargo facility complementary to existing facilities of the Ports Authority. CIP was prepared to provide the significant capital funds necessary to establish the facility as a public cargo handling facility with the Ports Authority providing oversight as well as marketing services.

The license agreement between the Ports Authority and CIP satisfies the requirements of shippers by providing a public import and export cargo facility. This added facility will have the capability to handle cargoes which otherwise could not have been accommodated at the Port of Charleston. Had the agreement not been acted upon, many shippers may have been faced with using out-of-state facilities to move their cargo because of the unique nature of and land requirements imposed by the cargo. The use and development of this facility by the Ports Authority, through its agreement with CIP, will ultimately inure to the benefit of the citizens of South Carolina.

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