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INSPECTOR GENERAL

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April 13, 2017

Ms. Janelle Chan
Chief of Real Estate
Massachusetts Bay Transportation Authority
Ten Park Plaza, Suite 5720
Boston, MA 02116

Re: The Massachusetts Bay Transportation Authority's Billboard Contract with Clear Channel Outdoor, Inc.

Dear Ms. Chan:

The Internal Special Audit Unit ("ISAU" or "Unit") recently reviewed two aspects of the Massachusetts Bay Transportation Authority's ("MBTA" or "Authority") contract with Clear Channel Outdoor, Inc. ("Clear Channel") for billboard advertising. First, the ISAU reviewed the MBTA's decision to amend the contract to permit Clear Channel to convert up to eighteen billboards to a digital format instead of conducting a new, public procurement for the billboards. Second, the ISAU examined whether the MBTA was required to hold a public meeting before allowing Clear Channel to install a digital billboard on MBTA property in Dorchester.

As set forth below, it is the ISAU's opinion that the MBTA was not required to conduct a new procurement for the eighteen billboards. The ISAU notes, however, that the contract extension – ten years – is longer than the Unit generally recommends. The long extension also may have resulted in untapped future revenue for the Authority. Finally, the ISAU did not find any violation of any public meeting requirements with respect to the billboard in Dorchester.

I. Background

Clear Channel is a global outdoor advertising company that offers a variety of advertising products to retailers, including digital billboards, posters, bulletins and mobile billboards. In 2003, the MBTA entered into a contract with Clear Channel to allow the company to erect 192

outdoor billboards on various MBTA properties.¹ In return, the MBTA receives a portion of the advertising revenue that Clear Channel earns from the billboards. Specifically, the MBTA receives the greater of: (a) a minimum guaranteed fee per billboard; or (b) 20% of gross revenues from the billboards. The MBTA also receives additional benefits, such as the right to display a limited number of public service announcements on the billboards.

The original contract was for a fifteen-year term, expiring on March 3, 2018. The contract grants Clear Channel the exclusive right to install, maintain and operate each outdoor billboard for the contract term. Once the contract expires, Clear Channel must transfer ownership of all existing billboard structures to the MBTA.

On March 18, 2008, the parties amended the contract to add twenty more billboards, bringing the total billboards under contract to 212. These twenty billboards are subject to a slightly different fee structure than all of the other billboards. Pursuant to the amendment, the MBTA receives the greater of (a) a minimum guaranteed fee; or (b) 40% of gross advertising revenues.

The MBTA and Clear Channel revised the contract again on May 15, 2012, this time to permit Clear Channel to convert up to eighteen of the billboards to a digital format. Under the amendment, the MBTA also extended Clear Channel's license to operate the eighteen billboards to March 3, 2028. In exchange, the MBTA receives the greater of (a) a minimum guaranteed fee per digital billboard; or (b) 25% of the gross advertising revenues from the digital billboards.² Further, at the expiration of the contract, the MBTA will own the billboards.

Digital billboards can generate significantly more advertising revenue than standard structures because billboard owners can run multiple advertisements on the same structure.³ This expands the advertising potential for each billboard, thus generating more revenue for the MBTA and Clear Channel. At the end of 2016, for example, fourteen digital billboards were operational. These billboards generated \$1,226,406 in revenue for the MBTA in 2016, compared to \$591,857 in 2011, before the digital conversion.

¹ This does not mean that the billboards are located on 192 separate MBTA sites. Many billboards have two sides and the contract treats each side as a separate billboard.

² Initially, the minimum guaranteed fee was \$90,000 for each digital billboard that is adjacent to an interstate and \$50,000 for each billboard that is not adjacent to an interstate. Thereafter the minimum guaranteed fee increases by 2.5% per year.

³ The digital format rotates multiple advertisements on one computerized screen, which allows Clear Channel to display several different advertisements on a rotating basis. Traditional billboards can only display a single advertisement.

II. The Contract Amendment

The ISAU examined whether the MBTA was required to conduct a new procurement for the eighteen billboards, rather than amending its contract with Clear Channel. Based on the ISAU's review, the MBTA was not required to conduct a new procurement.

The MBTA procurement manual that was in effect in 2012, when the contract was amended, stated:

A contract change that is not within the scope of the original contract is considered a sole source procurement ... If an out of scope change is required, a sole source justification and determination is required and must comply with FTA requirements. Proper MBTA authorization must be granted to process a sole source

In addition, section fifteen of the manual addressed contract extensions:

Consistent with the general tone of the FTA circular, contract time extensions will be considered in light of whether they are permissible changes or impermissible cardinal changes. Once the MBTA awards the third party contract, an extension of the contract term length that amounts to a cardinal change will require a sole source justification.

The MBTA's procurement manual defined a "cardinal change" as adding out-of-scope work to an existing contract. Therefore, the MBTA should have conducted a new, public procurement if (1) either the conversion of the billboards or the ten-year extension added out-of-scope work to the contract; and (2) the agency did not have a valid, sole-source justification for contracting with Clear Channel.

In this case, it is the ISAU's opinion that the amendment was not out of scope and that it did not represent a cardinal change. First, the original contract permitted Clear Channel to install digital billboards; it also contemplated that the parties could add or delete billboard locations during the contract period. Consequently, amending the contract to convert eighteen billboards to a digital format was not out of the scope of the original contract. Second, while the ten-year extension is long, it applies only to the eighteen digital billboards. The remaining 194 billboards are subject to the original contract expiration date (March 3, 2018). Considering these factors, the ISAU does not consider the extension to constitute a cardinal change. Consequently, the MBTA was not required to undertake a public procurement for the digital conversion of up to eighteen billboards.

The ISAU also notes that Clear Channel retained exclusive rights to the billboards until 2018. Therefore, the MBTA could not have put the digital conversion of the billboards out to

bid until the contract with Clear Channel expired in 2018. Alternatively, the MBTA could have terminated the contract, but would have had to pay early termination fees.

Finally, as mentioned, MBTA receives the greater of 25% of gross annual revenues from the digital billboards or a minimum guaranteed fee per digital billboard. Further, Clear Channel paid to convert the billboards and the MBTA will own all existing billboards when the contract expires.⁴ Consequently, the terms of the amendment do not initially appear to be unfavorable for the MBTA.

Nevertheless, the ten-year contract extension is longer than the ISAU typically recommends⁵ and it may not give the MBTA the opportunity to maximize its revenue. Given that Clear Channel could potentially recoup its initial cost to convert the billboards in less than ten years, a shorter extension may have been more favorable to the MBTA.

III. Construction of the Digital Billboard in Dorchester.

In 2014, Clear Channel installed a digital billboard on MBTA property adjacent to Interstate 93 (the Southeast Expressway) north of Columbia Road in Dorchester. The ISAU received a complaint that the MBTA did not hold a public meeting before allowing Clear Channel to construct the billboard. The ISAU could find no statute, regulation or rule requiring the MBTA to hold public meetings before allowing a vendor to install a billboard on its property. Further, the property in question is not in a “Sign-Free” area,⁶ which would prohibit construction of a billboard.

The ISAU also notes that, on September 12, 2013, the Office of Outdoor Advertising held a public hearing before issuing a permit for this billboard. *See, e.g.*, M.G.L c. 93D and 700 CMR 3.00.

IV. Conclusion

Based on the ISAU’s circumscribed review, the MBTA was not required to conduct a public procurement before amending the contract with Clear Channel. Further, while digital billboards should bring in more revenue for the MBTA than static billboards, the ten-year extension is long and ultimately may not be favorable to the MBTA. Finally, the ISAU could

⁴ An agent of Clear Channel reported that it cost \$7 million to convert the fourteen billboards that were fully operational at the end of 2016.

⁵ The MBTA’s standard contract term is five years. Longer contract terms may prevent the MBTA from obtaining the best price for services.

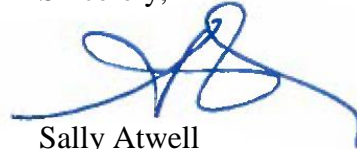
⁶ According to 700 CMR 3.07(10), an area may be designated as “Sign-Free” if it is of historical, architectural, scenic or environmental significance. The Office of Outdoor Advertising does not grant or renew permits for signs in Sign-Free areas or corridors.

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find no law or regulation requiring the MBTA to hold a public meeting before allowing Clear Channel to erect a digital billboard on MBTA property in Dorchester.

Please do not hesitate to contact me should you have any questions or require additional information.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Sally Atwell', with a stylized flourish extending to the right.

Sally Atwell
Director, Internal Special Audit Unit