



Office of the Inspector General

Commonwealth of Massachusetts

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Inspector General

Long-Term Leasing of DEM Skating Rinks

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Long-Term Leasing of DEM Skating Rinks

Introduction

In January 2002, at the request of Senator Brian Joyce and the Department of Environmental Management (DEM), the Office of the Inspector General initiated a limited review of a competitive process to award 25-year leases for 18 state-owned ice skating rinks under DEM's control.¹ The Division of Capital Asset Management (DCAM), in conjunction with DEM, had issued a request for proposals (RFP) in December 2001 for long-term operation and management services and capital improvements to the rinks under 25-year leases. The RFP was issued pursuant to Chapter 88 of the Acts of 2001, §30, which authorized DCAM, on behalf of and in consultation with DEM, to lease and enter into other agreements for one or more rinks, for terms not to exceed 25 years, to provide for the continued use, operation, maintenance, repair and improvement of the 18 rinks named in the legislation. The 18 rinks named in the legislation and covered by the RFP were as follows:

Daniel S. Horgan Memorial Rink, Auburn	John J. Navin Rink, Marlboro
John G. Asiaf Memorial Rink, Brockton	Stephen Hetland Memorial Rink, New Bedford
Arthur R. Driscoll Memorial Rink, Fall River	Henry Graf, Jr. Rink, Newburyport
Veterans Memorial Rink, Franklin	Vietnam Veterans Memorial Rink, North Adams
Gardner Veterans Rink, Gardner	James McVann-Lois O'Keefe Memorial Rink, Peabody
Collins Moylan Memorial Rink, Greenfield	John Armstrong Memorial Rink, Plymouth
Veterans Memorial Rink, Haverhill	Ray Smead Memorial Rink, Springfield
Henry J. Fitzpatrick Rink, Holyoke	Theodore J. Aleixo, Jr. Rink, Taunton
John J. Janas Memorial Rink, Lowell	Charles J. Buffone Rink, Worcester

¹ In a letter to the Office dated January 23, 2002, Senator Joyce requested that the Office review the capacity of the proposed lease agreements to maximize state revenues, maintain full access to skating for the public at reasonable hours and rates, and maintain sufficient oversight to ensure the taxpayers' interests were protected. DEM contacted the Office, at Senator Joyce's request, on January 25.

DEM had first privatized the management and operation of state-owned skating rinks in 1991. At that time, the Office received complaints about the RFP process used by the DEM to select operators for four rinks. After reviewing the RFP and related documents, the Office advised the Executive Office of Environmental Affairs (EOEA) that the procurement process entailed serious flaws that undermined fair competition and the interests of state taxpayers. However, EOEA took issue with the Office's critique of the RFP process.

Four years later, in 1995, DEM requested the Office's comments on two new RFPs for the management and operation of 17 rinks. The Office provided DEM with detailed recommendations for improving the evaluation methodology contained in each RFP. DEM issued the RFPs and executed five-year management and operations permits for the 17 rinks. These permits were subsequently extended for one year, to May 31, 2002. DEM also executed a one-year concession management agreement with North Adams State College for the operation of an eighteenth rink. This agreement was renewed each year until May 31, 2002.

Review Scope and Process

Between January and April 2002, the Office conducted a limited review of the RFP and lease, the existing permits to manage and operate the rinks, the most recent financial statements for each rink, and questions and answers posted on the state's on-line procurement website (Comm-PASS) regarding the procurement process for the leases. The Office also met with DCAM and DEM officials on two occasions and provided them with oral and written recommendations regarding the RFP and lease.

The Office provided initial comments on the RFP and lease in a letter dated February 19, 2002. (A copy of the Office's February 19, 2002 letter is provided in Appendix A.) In the letter, the Office identified serious flaws and omissions in the RFP and lease. The Office also recommended corrective actions and amendments to reduce the risks and protect the public interest in the competitive selection and leasing process. The Office's letter noted:

Such leases and operating agreements must, in addition to fulfilling other objectives, help ensure contractor performance in accordance with their proposals, require contractors to provide information and access necessary for state oversight, and ensure that skating rink facilities will be returned to the Commonwealth at the end of the term in good condition.

To give proposers sufficient opportunity to review and respond to the amended documents, the Office recommended that DCAM extend the proposal submission date of March 1, 2002 by at least 30 days.

On March 11, 2002, staff of the Office met with DCAM and DEM officials to discuss the concerns raised in the Office's February 19 letter. During that meeting, DCAM and DEM officials advised the Office that they had rejected the proposals received on March 1, 2002.² They stated that they planned to amend and reissue the RFP and lease in response to the Office's recommendations, and that proposers that had responded to the original RFP would be permitted to amend and resubmit their proposals.

On March 26, 2002, DCAM provided the Office with revised versions of the RFP and lease incorporating the Office's major recommendations. At a second meeting, staff of the Office provided DCAM and DEM officials with a memorandum dated April 1, 2002, summarizing the Office's comments on the revised documents. (A copy of the Office's April 1 memorandum is provided in Appendix A.)

On April 8, 2002, DCAM reissued the RFP and lease. The final RFP and lease incorporated the Office's most recent comments. Proposals were received on May 3, 2002.

Major Issues and Recommendations

This section discusses the major issues identified by the Office and recommendations provided to DCAM and DEM by the Office during the course of this review. The

² The officials said that the proposals had been opened and that a list of proposers for each rink had been made. However, the proposals were not evaluated before being rejected.

changes made to the RFP and lease in response to the Office's recommendations are also summarized below.

Lease Term

The original RFP and lease specified a 25-year lease term. In the February 19, 2002 letter to DEM, the Office noted:

The Office recognizes that longer-term leases and operating agreements might provide incentives for larger private capital investment. However, this advantage must be balanced against the disadvantages of relinquishing public control and forgoing market-driven competition for longer periods, as well as greater performance risks. Therefore, the Commonwealth must, at the outset, promote competition and pay careful attention to the qualifications of proposers, their financial backing, their management plans, and their promised capital investments.

On March 11, 2002, Office staff met with DCAM and DEM officials to discuss the rationale for the 25-year lease term as well as other issues raised in the Office's February 19 letter. The officials advised the Office that most of the rinks required major reconstruction work that could cost millions of dollars and that a 25-year lease period would give rink operators the best opportunity for obtaining financing for capital improvements with reasonable payback terms. DCAM subsequently redrafted the RFP and lease, specifying an initial 13-year lease term with an option to extend the lease for an additional 12-year period. However, in a letter to the Office dated March 26, 2002, DCAM's Deputy General Counsel for Real Estate stated that DCAM and DEM officials were also considering two alternatives: specifying a 15-year term with a 10-year option to extend, or leaving the lease term at 25 years, as originally planned.

The Office then recommended that DCAM specify a 15-year lease term with a 10-year option to extend, unless DCAM and DEM concluded that a 15-year lease term was not economically feasible. The final RFP and lease specified a 25-year lease term, reflecting DCAM and DEM's conclusion that, given the extensive capital improvements required, a 25-year term was necessary in order to generate adequate competition for the rink leases.

Completion of Capital Repair and Replacement Program

The original RFP required each proposer to propose a program of capital repairs and replacements for the life of the lease term and provided that the capital program would be attached to and incorporated into the skating rink lease. However, the original lease document contained no reference to the proposed capital program.

The Office expressed concern that the lease did not require the rink operator to complete the capital repair and replacement program proposed by the rink operator and evaluated by DCAM and DEM as a basis for the lease award. Rather, the lease appeared to commit the rink operator only to completing “Minimum Initial Improvements,” which were not defined or explained in the RFP or lease. The Office’s letter concluded:

Clearly, it is not in the Commonwealth’s interest to enter into 25-year leases without binding contractual assurances that the rink operators will complete the capital improvements set forth in their proposals.

Moreover, the RFP did not provide prospective proposers with information concerning the conditions of the DEM rinks for which proposers were required to propose detailed capital improvements. Although the RFP indicated that information about each rink was available to proposers, DEM’s Deputy Commissioner advised the Office that this information was not being provided to prospective proposers and that facility inspections were being offered instead. DEM’s Deputy Commissioner also stated that the agency had received no inquiries concerning the condition of the rinks.

In the February 19 letter, the Office stated:

We recommend that DCAM and DEM provide prospective proposers with available information regarding the condition of the rinks and their systems and equipment, thereby assisting proposers in developing realistic cost estimates for capital improvements. Ensuring that proposers have the basic information they need to submit responsive proposals is a fundamental principle of best value contracting. In this Office’s view, it is also advisable to require each proposer to conduct a detailed inspection of each rink for which a proposal was submitted.

In response to these recommendations, DCAM added new language to the lease requiring the rink operator to perform and complete the capital program set forth in its proposal in a timely manner.

DCAM attached an appendix to the RFP containing information on the condition of the major systems, structures, and equipment at each rink and specifying minimum required capital repairs and improvements to be completed in the first five years of the lease term. DCAM also added a provision to the RFP requiring that the capital program proposed for each rink include the minimum repairs and improvements specified in the appendix. For example, these minimum repairs and improvements included the required replacement of ice slabs in 14 of the rinks, refrigeration units in 13 rinks, roofs in 12 rinks, and ice resurfacing machines and edgers in 16 rinks. All of these repairs and improvements had to be completed within the first five years of the lease term.

In April 2002, the Office received a complaint from Representative Paul Tirone alleging that the minimum required capital repairs and improvements specified in the revised RFP were unreasonably onerous because they required replacement of ice slabs and refrigeration units for two rinks within the first year of the lease. In a letter dated April 18, 2002, the Office advised Representative Tirone that the Office had recommended to DCAM and DEM that they re-examine the minimum required capital repairs and improvements specified in the RFP and, if necessary, clarify requirements for individual rinks. (A copy of the Office's April 18, 2002 letter is provided in Appendix A.) The final RFP modified the minimum requirements for the two rinks that were the subject of the complaint: instead of requiring replacement of ice slabs and refrigeration units in the first year of the lease for the two rinks, the RFP required that these improvements be made within the first five years of the lease.

Performance Bonds for Construction Work

While the original lease required the rink operator to provide a \$50,000 performance bond per rink to ensure continued operation of the rinks, it did not require a performance bond for the capital improvements undertaken by the rink operator. The Office recommended that the lease require rink operators to obtain performance bonds for rink

construction work undertaken under the capital program and that all performance bonds be issued by a surety licensed to do business in Massachusetts.

In response, DCAM added a provision to the lease requiring the rink operator to provide a construction performance bond issued by a surety licensed in Massachusetts for each component, stage, or phase of the capital program.

M.G.L. c. 149 Applicability to Construction

Chapter 88 of the Acts of 2001, §30, the legislation under which DCAM and DEM awarded the skating rink leases, states:

Such leases and other agreements shall be on terms acceptable to the commissioner of capital asset management and maintenance after consultation with the commissioner of environmental management and, **notwithstanding any general or special law to the contrary, shall provide for the lessees to manage, operate, improve, repair and maintain the properties.** [Emphasis added.]

In the view of the Office, it is unclear whether this language exempts the rink construction work to be undertaken by the rink operators from the requirements of M.G.L. c. 149, §§44A-M, which governs all public contracts for the construction, reconstruction, installation, demolition, maintenance, or repair of a building at an estimated cost of more than \$25,000.

The Office recommended that DCAM consult the Office of Attorney General and the Division of Occupational Safety regarding the potential applicability of M.G.L. c. 149 requirements – such as those provisions requiring advertising, bidding, and payment of prevailing wages – to the construction work to be undertaken by the selected rink operators. In response to the recommendation, DCAM’s Deputy General Counsel for Real Estate advised the Office that DCAM’s legal staff had reviewed the issue and concluded that the M.G. L. c. 149 did not apply to the construction work to be performed under the leases.

Supervision of Construction Work

Although the original RFP solicited resumes and position descriptions of personnel who would be assigned by each proposer to the rink program, it did not solicit information regarding these proposers' construction experience. The Office recommended that the RFP solicit resumes of key personnel who would be assigned by the proposers to supervise the construction work to be undertaken under the lease.

In response, DCAM added a provision to the RFP requiring each proposal to include resumes and position descriptions of those individuals who would be assigned to supervise the rink construction work specified in the proposer's capital program.

Rink Condition After the 25-Year Lease Term

The original lease listed certain maintenance obligations relating to litter, snow and ice removal, sewage disposal, blacktopped pavement, and restrooms. It also committed the rink operator to spending at least \$20,000 or 1.5 percent of revenues, whichever was higher, to comply with these obligations. However, the lease did not require the rink operator to maintain, repair, or replace major capital equipment or systems over the 25-year lease term. The Office expressed concern that the lease provided no assurance that the condition of each rink would be substantially improved when the rinks reverted back to the Commonwealth at the end of the 25-year lease term. The Office recommended that DCAM revise the lease to correct this omission, thereby ensuring that the Commonwealth would obtain improved rink facilities after 25 years.

In response, DCAM amended the lease to state that the rink operator's obligations under the lease would include:

The maintenance, repair, and replacement of major capital equipment and systems, including, without limitation, Building, Building Equipment, and ice-resurfacing machines and edgers (provided that the replacement of any ice-resurfacing machine and edger shall be with a non-fossil-fuel-consuming ice-resurfacing machine and edger), **it being the intent of this Lease that Landlord obtain improved facilities at the end of the Term.** [Emphasis added.]

Proposers' Financial Capacity

The original RFP required the proposer to provide “audited firm statements for Proposer’s last fiscal year, a reasonable substitute, or an explanation why one is not available.” The Office expressed the view that these submission requirements appeared inadequate to provide DCAM and DEM with sufficient information to accurately evaluate each proposer’s capacity to finance its proposal. The Office noted that there seemed to be no justification for awarding a 25-year lease to a proposer that was unable to produce either an audited financial statement or a reasonable substitute. The Office recommended that the RFP be clarified and amended to require audited financial statements for the proposer’s last fiscal year or a reasonable substitute deemed acceptable to DEM and DCAM, as well as an explanation of why audited financial statements were unavailable.

In response, DCAM amended the RFP to require that proposers submit audited financial statements for the last fiscal year, or a reasonable substitute and an explanation of why audited statements were not available.

Cash Management Procedures

Although the original RFP required proposers to describe certain aspects of their proposed management approaches, such as their marketing strategies and maintenance programs, the RFP solicited no information regarding proposers’ cash management or internal control procedures. The Office noted that since the selected proposers would be responsible for accepting, managing, and reporting millions of dollars in rink revenues, a portion of which would be paid to the Commonwealth, sound cash management procedures would be necessary to ensure accurate reporting of revenues and reduce the risks of error and fraud. The Office recommended that the RFP be amended to solicit information that would enable DCAM and DEM to evaluate the proposers’ capacity and plans to handle and account for rink revenues.

In response to the Office’s recommendation, a provision was added to the RFP requiring each proposer to submit a detailed description of the proposer’s cash

management and internal control procedures. The RFP was also revised to state that these cash management and internal control procedures would be evaluated in the selection process. DCAM also added a provision to the RFP requiring proposals to include resumes and position descriptions of those overseeing the proposers' cash management and internal control procedures.

Rent Paid to the Commonwealth

The original lease specified that the rink operators would pay a "percentage rent" to DEM based on the actual gross revenues ("premises revenues") from all sources, including subtenants and licensees. The lease, however, excluded four categories of rink revenues in computing the percentage rent:

- (a) service fees or rental fees charged to rink operator's subtenants or licensees;
- (b) the sale (but not the redemption) of gift certificates;
- (c) gross-receipts, sales, and value-added taxes collected from consumers and paid to a governmental taxing authority; and
- (d) sales to employees at discount.

The Office stated that of the four categories of excluded revenues, only (b) appeared justifiable. The Office noted that it was unclear why the Commonwealth should not share in the fees paid to the rink operator by subtenants and concessionaires and that exclusion (a) created an incentive for the rink operator to sublease space in order to shield rink revenues from the percentage rent to be paid to the Commonwealth. The Office also argued that by allowing the rink operator to exclude sales and other taxes, exclusion (c) would unnecessarily increase the auditing burden on DCAM and DEM. The Office questioned the rationale for exclusion (d), which excluded sales to employees at discount from the calculation of percentage rent.

After considering the Office's recommendations, DCAM deleted exclusion (d) from the final lease.

Verification and Auditing of Rink Revenues

Although the original lease required rink operators to submit financial statements to DEM on a yearly basis, the language of the lease did not ensure that the Commonwealth would receive the information necessary to verify each rink operator's reported gross revenues, exclusions from computations of rent to the Commonwealth,³ and maintenance expenditures. The Office recommended that the lease be amended to require the inclusion of this information in the audited financial statements submitted by the rink operators.

The Office also expressed concern that a provision of the lease, which concerned verification and audit of the premises revenues reported by the rink operator, was excessively vague. The lease provision stated:

The Premises Revenues and the method of reporting the Premises Revenues for Percentage Rent purposes shall be subject to verification and audit by DEM.

The Office recommended that this language be replaced by specific reporting and audit requirements that ensured regular, systematic verification by the Commonwealth of the revenues reported and paid by the rink operators.

In response, DCAM made a number of changes to the lease. DCAM added a provision requiring rink operators to submit monthly as well as annual financial statements to DEM, and requiring that the annual financial statements be audited financial statements. The revised lease also required that both the monthly and annual audited financial statements be prepared and submitted in accordance with generally accepted accounting principles and that they must include the sources and amounts of premises revenues for each rink, exclusions from computations of percentage rent permitted by the lease, and capital program and maintenance expenditures by the rink operator.

³ The RFP required the proposers to specify a percentage of the annual gross rink revenues to be paid to the Commonwealth.

Waivers of RFP Provisions and Proposal Negotiations

The original RFP contained a provision that would have allowed DCAM and DEM to negotiate combinations of all or portions of different proposals with proposers and to waive portions of the RFP. The Office raised strong objections to this provision, stating in the February 19 letter:

This provision, if invoked, has the potential to undermine the fairness and relevance of the RFP process. While minor informalities could and should be waived, the substantive submission requirements and evaluation criteria should not be waivable. Similarly, while some proposal negotiations might be necessary, such negotiations should be limited rather than open-ended in scope. We therefore recommend that the overly broad language cited above be amended to ensure that substantive RFP requirements are not waived and that the major terms and conditions of the draft lease are not significantly changed in the negotiation process.

In response, DCAM revised the RFP to eliminate the language allowing DCAM and DEM to waive portions of the RFP. The revised RFP also allowed proposers to modify their proposals to include any rinks for which no acceptable proposals had been received.

Reported Outcomes

As of September 2002, 17 of the 18 rinks were being operated under 25-year leases signed with two private companies and two cities, according to DCAM's Deputy General Counsel for Real Estate. The eighteenth rink was being operated under a one-year license agreement with the Massachusetts College of Liberal Arts (formerly North Adams State College). Under the new leases, one company was operating 13 of the rinks (including 10 it had previously operated under management and operations permits issued by DEM), and the other company was continuing to operate the two rinks it had been operating under a previous management and operations permit issued by DEM.

According to the Deputy General Counsel, DCAM received no responsive proposals for three rinks; consequently, the proposers that had submitted responsive proposals for

other rinks were invited to submit proposals for the three remaining rinks. One company, which had submitted responsive proposals for ten rinks, submitted responsive proposals for the three additional rinks and was awarded the leases for those rinks, according to the Deputy General Counsel.

The Deputy General Counsel advised the Office that DCAM's negotiations with the selected proposers did not result in major changes in the lease terms contained in the final lease document advertised by DCAM. She stated that all the executed leases contained the provisions recommended by the Office governing completion of the capital repair and replacement program, rink condition after the 25-year lease term, performance bonds for construction work, and verification and auditing of rink revenues.

Conclusion

As a result of the Office's review and cooperative working relationship with DCAM and DEM, the final RFP and leases for 17 skating rinks incorporated important public protections that were lacking in earlier versions of these documents. These protections will benefit taxpayers and rink customers by helping to ensure that the private rink operators leasing the rinks for the next 25 years will complete needed improvements to the rinks, operate the rinks in a manner that supports the Commonwealth's objectives, and return the rinks in an improved condition when the leases expire.

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Appendix A: Correspondence from the Office of the Inspector General

1. Letter dated February 19, 2002 to Susan W. Frechette, Deputy Commissioner of the Department of Environmental Management.
2. Memorandum dated April 1, 2002 to the Division of Capital Asset Management and the Department of Environmental Management.
3. Letter dated April 18, 2002 to Representative Paul E. Tirone.

Note: The attached letters have been formatted for electronic publication.



The Commonwealth of Massachusetts
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February 19, 2002

Susan W. Frechette
Deputy Commissioner
Department of Environmental Management
251 Causeway Street, Suite 600-700
Boston, MA 02114-2104

Dear Deputy Commissioner Frechette:

At your request, this Office has reviewed the Request for Proposals to Provide Long-Term Operation and Management Services and Capital Improvements for State-Owned Ice Skating Rinks (RFP) and the accompanying draft lease forwarded to this Office on January 24, 2002. We have also reviewed the sample rink package you forwarded on February 7, 2002. This procurement is being conducted pursuant to Chapter 88 of the Acts of 2001, §30, which authorizes the Division of Capital Asset Management and Maintenance (DCAM), on behalf of and in consultation with the Department of Environmental Management (DEM), to lease 18 public skating rinks for terms not to exceed 25 years. DCAM and DEM have, in fact, elected to lease the rinks for the maximum 25-year term allowable under Chapter 88. I would like to meet with you, at your convenience, to discuss the rationale for the 25-year lease term.

According to the RFP, the Commonwealth's goal is:

to enter into a 25-year Skating-Rink Lease for each Rink with a tenant who will reconstruct and/or rehabilitate the Rink to meet state-of-the-art ice-skating-facility standards and will provide cost-effective, high-quality skating operations in a manner that is sensitive to public recreational needs and reflects the Commonwealth's goal of providing affordable recreation for the public.

This Office recognizes that longer-term leases and operating agreements may provide incentives for larger private capital investment. However, this advantage must be balanced against the disadvantages of relinquishing public control and

forgoing market-driven competition for longer periods, as well as greater performance risks. Therefore, the Commonwealth must, at the outset, promote competition and pay careful attention to the qualifications of proposers, their financial backing, their management plans, and their promised capital investments. Such leases and operating agreements must, in addition to fulfilling other objectives, help ensure contractor performance in accordance with their proposals, require contractors to provide information and access necessary for state oversight, and ensure that facilities will be returned to the Commonwealth at the end of the term in good condition.

Our preliminary review of the RFP and the draft lease has identified serious flaws and omissions that should be addressed and corrected before DCAM receives and evaluates proposals to lease the rinks. This letter summarizes these deficiencies and recommends corrective amendments and actions that would reduce the risks and protect the public interest in the competitive selection and leasing process.

Request for Proposals

Section II. Rinks

Section II of the RFP states that each Rink Package includes "information regarding Rink structures and equipment." However, your letter of February 7, 2002 stated that this information is not being provided to prospective proposers and that "the decision was made to offer facility inspections instead." (The materials you forwarded to the Office did not include an addendum reflecting this change to the RFP.) Your letter also indicated that the designated staff person responsible for handling questions regarding the procurement has received no inquiries concerning detailed facility conditions.

We recommend that DCAM and DEM provide prospective proposers with available information regarding the condition of the rinks and their systems and equipment, thereby assisting proposers in developing realistic cost estimates for capital improvements. Ensuring that proposers have the basic information they need to submit responsive proposals is a fundamental principle of best value contracting. In this Office's view, it is also advisable to require each proposer to conduct a detailed inspection of each rink for which a proposal is submitted.

Section IV. Requirements for Capital Improvements and Maintenance

Section IV of the RFP requires each proposer to propose a program of capital repairs and replacements for the 25-year lease term (the "Capital Program"). Section 9 of the draft lease concerns "Minimum Initial Improvements" to be undertaken by the "Tenant" and indicates that the plans for the Minimum Initial Improvements will be included in Exhibit G of the executed lease. You have advised this Office that the Minimum Initial Improvements will be proposed by

competing proposers and evaluated by DCAM and DEM. However, the RFP contains no reference to or explanation of the Minimum Initial Improvements or their relationship to the proposed Capital Program. Accordingly, we recommend that the RFP be amended to clarify the proposal submission requirements relating to the Minimum Initial Improvements referenced in the draft lease.

Section IX. Required Proposal Contents

Since the selected proposers will be responsible for accepting, managing, and reporting millions of dollars in rink revenues, a portion of which will be paid to the Commonwealth, sound cash management procedures will be necessary to ensure accurate accounting of revenues and reduce the risks of error and fraud. However, although Section IX requires proposers to describe other aspects of their proposed management approaches, such as their marketing strategies and maintenance programs, Section IX solicits no information regarding proposers' cash management or internal control procedures. We recommend that the RFP be amended to solicit information that will enable DCAM and DEM to evaluate proposers' capacity and plans to handle and account for rink revenues. Alternatively, the RFP should specify minimum cash management and internal control procedures to be instituted by all tenants, and such procedures should be included in the lease.

Similarly, the Commonwealth's evaluation of proposers' financial capacity is an extremely important component of the selection process for these long-term rink leases. However, the proposal submission requirements contained in the RFP appear inadequate to provide DCAM and DEM with sufficient information to enable an accurate determination of each proposer's capacity to finance the lease or leases sought by the proposer. Item J of Section IX, Financial Management and Budget, states that the proposer must provide "audited firm statements for Proposer's last fiscal year, a reasonable substitute, or an explanation why one is not available." There would seem to be no justification for awarding a 25-year lease to a proposer that is unable to produce either an audited financial statement or a reasonable substitute. We therefore recommend that the RFP be clarified and amended to require audited financial statements for the proposer's last fiscal year or a reasonable substitute deemed acceptable to DEM and DCAM and an explanation of why audited financial statements are unavailable.

In addition, this section of the RFP does not require proposers to submit banking references, although Section XI states that DCAM and DEM will use banking references as a basis for evaluating each proposer's financial strength. Accordingly, we recommend that Section IX of the RFP be amended to specify the number and type of banking references to be submitted by proposers for evaluation purposes.

Section XI. Evaluation Criteria and Selection Process

The evaluation criteria cited in Section XI do not include or refer to proposers' cash management and internal control procedures (discussed in the previous section of this letter). We recommend that this section of the RFP be amended to include these important evaluation criteria.

In addition, Section XI states:

In the selection process, DCAM and DEM reserve the right to negotiate with any or all proposers (including, without limitation, by **negotiating the combination of all or portions of different proposals**, by requesting that certain proposers agree to lease one or more rinks for which no proposals were submitted), **to waive portions of the RFP**, to waive any informalities in proposals, to reject any or all proposals and to reject portions of proposals and to select other proposals [Emphasis added.]

This provision, if invoked, has the potential to undermine the fairness and relevance of the RFP process. While minor proposal informalities can and should be waived, the substantive submission requirements and evaluation criteria should not be waivable. Similarly, while some proposal negotiations may be necessary, such negotiations should be limited rather than open-ended in scope. We therefore recommend that the overly broad language cited above be amended to ensure that substantive RFP requirements are not waived and that the major terms and conditions of the draft lease are not significantly changed in the negotiation process.

Lease

This Office has three fundamental concerns regarding the draft lease. First, the draft lease does not appear to obligate the tenant to complete the full capital repair and replacement program proposed by the tenant and evaluated by DCAM and DEM as a basis for award of the lease. The RFP requires each proposer to propose a "program of capital repairs and replacements for the life of the lease term ("Capital Program")" and provides: "Said Capital Program shall be attached to and incorporated into the Skating-Rink Lease for the Rink." However, this Office has been unable to find any lease provision that explicitly requires the tenant to complete its proposed Capital Program, and the draft lease contains no reference to any attachment containing the proposed Capital Program. Section 2 appears to commit the tenant only to performing the work financed by an initial investment projected by the tenant, "all as set forth in Tenant's Proposal and delineated on Exhibit G." Exhibit G is labeled "Description of Minimum Initial Improvements."

It thus appears that the draft lease commits the tenant to completing the Minimum Initial Improvements to be included in Exhibit G (further discussed below) but not to completing the Capital Program set forth in the tenant's

proposal. Clearly, it is not in the Commonwealth's interest to enter into 25-year leases without binding contractual assurances that the tenants will complete the capital improvements set forth in their proposals. Accordingly, we recommend that the draft lease be revised to include such contractual provisions.

Second, the draft lease provides no assurance that the condition of each rink at the end of the 25-year lease term will be substantially improved. The draft lease does detail certain maintenance obligations relating to litter, snow and ice removal, sewage disposal, blacktopped pavement, and restrooms. The draft lease also commits the tenant to spending at least \$20,000 or 1.5 percent of revenues, whichever is higher, to comply with these obligations. However, the draft lease does not require the tenant to maintain, repair, and replace major capital equipment and systems. If the intent of the draft lease is to obtain improved facilities for the Commonwealth at the end of the lease term, then we recommend that the draft lease be revised accordingly.

Third, the draft lease imposes a major auditing burden on DCAM and DEM. According to the draft lease, the "percentage rent" to be paid by each tenant will be based upon the actual gross receipts – the "premises revenues" – which will exclude four categories of revenues received by the tenant. (Three of the four exclusions appear unwarranted, as will be discussed.) The task of verifying the accuracy of the "premises revenues" reported by each tenant will therefore require a significant investment of staff resources, as will the task of verifying each tenant's maintenance expenditures each year. However, the draft lease does not commit DCAM or DEM to performing these tasks, which are essential to protecting the Commonwealth's financial interests over the 25-year lease period. The draft lease should be amended to simplify the procedures for computing the "premises revenues" and to specify the audit and verification procedures to be implemented by the Commonwealth.

Also, Chapter 88 of the Acts of 2001, §30 provides:

Every effort shall be made to balance the ice allocation needs of long-established youth organizations and newly formed youth organizations in a manner that provides equal opportunity and equal access for youths of each gender.

To ensure that the draft lease is consistent with Chapter 88, we recommend that similar language be incorporated into the draft lease.

This Office has also identified inconsistencies, omissions, and unfavorable provisions in the draft lease. Our section-by-section comments are provided below.

Section 1. Definitions

Both Chapter 88 of the Acts of 2001 and the RFP provide that general public skating must be booked at a minimum of 16 hours per week. However, Section 1 of the draft lease states, under "Permitted Uses (c) Allocation of Ice-Time to User-Groups," that general public skating must be booked at a minimum of 14 hours per week. We recommend the draft lease be corrected to state the statutorily mandated minimum requirement of 16 hours.

Section 1, under "Permitted Uses (j) "Ice-Time Fees and Charges," states: "After the first thirty-six months of the Term, fees shall be set by Tenant, subject to the prior written approval of DEM, which approval shall not be unreasonably withheld, conditioned, or delayed." This provision is significantly less restrictive than the RFP provision governing ice-time rates, which states:

If a Rink tenant proposes to increase ice time rates, the Rink tenant shall submit a letter of request to DEM. In considering each request, DEM will consider all factors it deems relevant, including, without limitation, the following:

- Capital investments made by the Rink tenant to the Rink for which the request is made.
- Ice-time rates charged by other rinks (public and private) within reasonable proximity of the Rink for which the request is made.
- The length of time since the last rate increase, if any.
- Rates charged at other Rinks, it being the goal of DEM to ensure that rates at the Rinks are consistent.

To ensure that ice-time rate increases over the 25-year lease term are controlled by the systematic, documented process described in the RFP, we recommend that the current provision in the draft lease governing increases in ice-time rates be stricken and replaced by the RFP language quoted above.

In addition, Section 1, under "(m) Annual Reports," states: "A fiscal-year (July through June) statistical report and a fiscal-year financial statement, each for the fiscal year most recently ended, shall be submitted by Tenant to DEM no later than September 1. Each fiscal-year financial statement shall be prepared and attested to by a certified public accountant." We recommend that the draft lease be amended to specify the required contents of the "statistical report." Moreover,

it is unclear whether the financial statement is intended to provide the Commonwealth with the information necessary to verify the proposer's reported gross revenues (as referenced in the definition of "Premises Revenues," also referred to in Section 4.1 as gross receipts), exclusions from computations of percentage rent (as defined in Section 4.1.2), and maintenance expenditures (as discussed in Section 8.3). We recommend that the draft lease be amended to state that the audited financial statement must include this information.

Although this section of the draft lease is labeled "Definitions," it contains a number of substantive contract provisions, including the three contract provisions discussed above. To prevent confusion or future disputes, we recommend reorganizing the draft lease so that the "Definitions" section is limited to definitions of lease terms.

Section 4. Rent

Section 4.1.2, "Exclusions from Computations of Percentage Rent," sets forth four exclusions from the computation of percentage rent to be paid to the Commonwealth by the tenant. The four exclusions are:

- (a) service fees or rental fees charged to Tenant's subtenants or licensees,
- (b) the sale (but not the redemption) of gift certificates
- (c) gross-receipts, sales, and value-added taxes collected from consumers and paid to a governmental taxing authority, and
- (d) sales to employees at discount.

Of these, only (b) appears justifiable. It is unclear why the Commonwealth should not share the fees paid to the tenant by concessionaires and subtenants. Exclusion (a) creates an incentive for the tenant to sublease space in order to shield rink revenues from the percentage rent to be paid to the Commonwealth. Moreover, by allowing the tenant to exclude sales and other taxes, (b) unnecessarily increases the auditing burden on DCAM and DEM. This Office is unable to determine the rationale for (d), which would allow the tenant to exclude "sales to employees at discount." We therefore recommend that this provision be amended such that only (b) may be excluded from the computation of percentage rent owed by the tenant.

Section 4.1.3, "Verification and Audit" states: "The Premises Revenues and the method of reporting the Premises Revenues for Percentage Rent purposes shall be subject to verification and audit by DEM." As previously discussed, the structure of the draft lease imposes a major audit obligation on the Commonwealth to ensure that each tenant accurately reports rink revenues. Accordingly, this excessively vague provision in the draft lease should be

replaced by specific reporting and audit requirements that ensure regular, systematic verification by the Commonwealth of the revenues reported and paid by the rink tenants.

Section 6. Surrender on Termination

Section 6.2 states: "During the Term, title to the Building and Building Equipment shall be in Tenant." The reason for this provision is unclear to this Office. Absent a compelling justification for this language, we recommend that the draft lease be amended to provide that the Commonwealth retain title to the rinks throughout the lease period.

Section 8. Tenant's Duty to Maintain

Section 8.4(g) provides that any matter requiring DCAM's and/or DEM's consent or approval under Section 8.4 shall be deemed granted if both DCAM and DEM fail to respond in writing within 20 days after the tenant's request for DCAM's and DEM's consent and approval. Administrative inaction is not an acceptable substitute for and should not be equated with affirmative consent and approval by responsible state agencies. This risky and inappropriate provision should be stricken from the draft lease. We also recommend striking similar provisions appearing elsewhere in the draft lease, including in Section 9.2 and Section 20.1.3(a).

Section 9. Minimum Initial Improvements

This section of the draft lease concerns Minimum Initial Improvements set forth in Exhibit G ("Description of Minimum Initial Improvements") of the lease. You have advised this Office that Exhibit G will consist of Minimum Initial Improvements proposed by the selected tenant. However, as previously discussed, the RFP contains no reference to or explanation of Minimum Initial Improvements.

Section 9.2 states that within 30 days after the execution of the lease, the tenant shall provide plans and specifications for the Minimum Initial Improvements to both DCAM and DEM for review and approval. However, the same section also states:

At or prior to the completion date of the Minimum Initial Improvements, Tenant shall deliver to both DCAM and DEM true copies, in duplicate, of the final Plans and Specifications, including all amendments to the Plans and Specifications.

The intent of this provision is unclear to this Office. If the intent is to enable the Commonwealth to review or approve the final plans and specifications in advance, it is unclear why this provision states that they will be submitted upon completion of the work. If the intent is to require the submission of as-built drawings, it is unclear why this provision states that they will be submitted at or

prior to completion of the work. We recommend that this provision of the draft lease be clarified to reflect the intent.

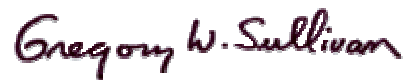
15. Assignment, Subletting, Mortgage

Section 15.2 provides that if the lease is assigned, DEM “may and is empowered to collect rent from the assignee.” It is unclear to this Office why DEM would want to collect rent from the assignee. In our view, it would be preferable to require unequivocally that, if the lease is assigned, the tenant will be responsible for collecting and paying to the Commonwealth the rent owed under the assigned lease.

This Office is continuing to review the competitive procurement process and the draft lease for the 18 rinks. In the meantime, this Office strongly recommends that DCAM and DEM amend the RFP and the draft lease in accordance with the recommendations contained in this letter. We further recommend that the addendum issued by DCAM and DEM extend the proposal submission date of March 1, 2002 by at least 30 days in order to ensure that proposers are given sufficient opportunity to review and respond to the amended RFP and draft lease.

I hope these comments are helpful. I look forward to meeting with you to discuss the 25-year lease term. Please contact Dan Ahern of my staff with any questions you may have.

Sincerely,



Gregory W. Sullivan
Acting Inspector General

cc: Senator Brian A. Joyce
Commissioner David B. Perini, DCAM

To: Division of Capital Asset Management and Maintenance
Department of Environmental Management

From: Office of the Inspector General

Subject: Request for Proposals and Draft Lease for Long-Term Skating Rink Operation
and Maintenance Services and Capital Improvements

Date: April 1, 2002

The revised request for proposals (RFP) and draft lease address many of the recommendations set forth in the Office of the Inspector General's letter dated February 19, 2002. The Office's major remaining recommendations for amending the request for proposals and draft lease document are summarized below. This summary is not intended to represent a comprehensive critique of these documents.

Lease term. The Office recommends a 15-year term with a 10-year renewal option unless DCAM and DEM conclude that a 15-year lease term is not economically feasible.

Alternates. If proposals on alternate lease terms are solicited, the RFP should state a clear decision rule for selection.

M.G.L. c. 149 applicability. It is unclear to this Office whether Chapter 88 of the Acts of 2001, §30 exempts the construction work to be undertaken by rink tenants from the requirements of M.G.L. c. 149. Accordingly, the Office recommends that DCAM and DEM seek opinions from the Office of the Attorney General and the Division of Occupational Safety regarding the applicability of M.G.L. c. 149 requirements, including advertising, bidding, and payment of prevailing wages, to construction work undertaken by the selected tenants.

Performance bond requirement. The Office recommends that the RFP and lease require tenants to obtain performance bonds for rink construction work undertaken under the capital program and that all performance bonds be issued by a surety licensed to do business in Massachusetts.

Construction supervision. The Office recommends that the RFP solicit resumes of key personnel who will be assigned by proposers to supervise construction as well as operate the rinks and provide financial supervision.

Improved condition at end of lease term. The stated goal of improved facilities at the end of the lease term should be incorporated into the evaluation criteria listed in Section XI of the RFP.

User fees. If user fees will be evaluated, Section XI should so state.

Ice time allocation. Although the RFP states that ice time allocation for uses other than general public skating will be subject to DEM's prior written approval, the draft lease contains no parallel provision. The Office recommends that the lease require the operator to obtain advance written approval from DEM of ice time allocation for uses other than general public skating and specify the timetable for submitting and obtaining such approval.

Audited financial statements. The Office again recommends that the RFP require proposers to submit audited financial statements for proposer's last fiscal year or a reasonable substitute deemed acceptable to DCAM and DEM and an explanation of why audited financial statements are not available. In addition, Section 2.2 (n) and Section 4.1.3 of the draft lease require submission of fiscal year and monthly financial statements, but the RFP does not reference monthly financial statements. This discrepancy should be corrected. The draft lease should clarify the entity for which financial statements must be submitted.

Statistical reports. The Office recommends that Sections 2.2(n) and Section 4.1.3 of the draft lease be amended to state that the fiscal year and monthly statistical reports shall be submitted in a form provided by DEM. It is unclear how the statistical reports relate to (o) and (q).

Option to extend term. Section 3.2 of the draft lease should be revised to ensure that the exercise of the option is conditional on approval by DCAM and DEM of the proposed capital program for the extended term and on a determination by DCAM and DEM that the tenant's performance under the lease has been satisfactory.

Exclusions from computations of percentage rent. The Office continues to recommend against the complex exclusions allowed in Section 4.1.2 of the draft lease. In the Office's view, the computation of percentage rent should be simplified by deleting all exclusions except exclusion (b). While this change could cause proposers to lower their percentage rent proposals, it is also likely to result in lower audit costs for rink tenants and a substantially reduced audit burden on DEM.

Audit and verification by DEM. The Office again recommends that the vague language of 4.1.3 be replaced by specific audit procedures that will ensure regular, systematic verification by the Commonwealth of the revenues reported by rink tenants.



The Commonwealth of Massachusetts
Office of the Inspector General

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April 18, 2002

Representative Paul E. Tirone
State House, Room 443
Boston, MA 02133

Dear Representative Tirone:

I am writing in response to your letter of April 12, 2002, concerning the reissued request for proposals (RFP) for long-term operation and maintenance service and capital improvements of Department of Environmental Management (DEM) rinks. DEM and the Division of Capital Asset Management and Maintenance (DCAM) reissued the RFP.

In your letter, which you delivered and discussed with staff of this Office on April 16, you raised a concern about the timing of required capital repairs and improvements. Specifically, you are concerned that the operators of the Lowell and Newburyport rinks would be required to replace slabs and refrigeration equipment during the first year of the lease, whereas other rink operators would not be required to replace the slabs and refrigeration in the first year of operation.

We have reviewed the RFP and have determined that operators would be required to replace slabs and refrigeration equipment in the first year at five rinks; slabs and refrigeration equipment would have to be replaced within the first five years of operation at nine rinks; and no mention is made of a requirement to replace slabs and refrigeration equipment at four rinks. This Office had previously recommended that DEM clearly identify the capital repairs and improvements they will require under the agreements. Differences in timing of required capital repairs and improvements among rinks do not provide any competitive advantages or disadvantages for potential operators submitting proposals on the individual rinks. Such differences should be determined by capital needs, and this Office is not in a position to question DEM's judgement regarding the extent and timing of required capital repairs and improvements.

In reviewing the RFP in response to your complaint, however, we did notice that the RFP might not be sufficiently clear about the requirements in some cases. For example, Appendix E of the RFP states that the slab in Taunton is "[c]lassified as needing replacement in the next five years." However, slab replacement is not listed under "Minimum Required Capital

Representative Tirone
April 18, 2002
Page 2

Repairs/Improvements." Yet, questions and answers about the RFP posted on the DEM and Comm-Pass web sites include the following:

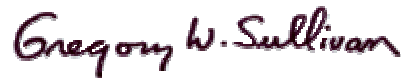
2. On page 47 of the RFP, there is no Minimum Required Capital Repairs/Improvements listed for the Taunton Rink for years 1-5. There are requirements for Year 1 only. Is this correct?

ANSWER: YES

Notwithstanding this question and response, given the apparently contradictory information contained in Appendix E in this and a few other instances, this Office has recommended to DCAM and DEM that they reexamine Appendix E and, if necessary, clarify the requirements for capital improvements at the individual rinks.

This Office has reviewed your remaining concerns. The RFP invited questions during the proposal period, and some questions and answers have been posted on the DEM and Comm-Pass web sites. Responsibility for writing and interpreting the RFP, and for evaluating proposals, rests with DEM and DCAM. Consequently, any additional clarifications should come from DEM and DCAM. You provided copies of your August 12 letter to this Office to DEM and DCAM so they can address the issues that you raised as they deem appropriate.

Sincerely,



Gregory W. Sullivan
Acting Inspector General

Cc: Secretary Robert Durand
Secretary Kevin Sullivan
Commissioner David Perini
Deputy Commissioner Susan Frechette