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**INDEPENDENT STATE AUDITOR'S REPORT
ON THE ACQUISITION OF THE
MEDFORD STREET TERMINAL BY THE
MASSACHUSETTS PORT AUTHORITY
DECEMBER 1, 1986 TO JULY 31, 2001**

**OFFICIAL AUDIT
REPORT
DECEMBER 3, 2001**

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Chapter 465 of the Acts of 1956 established the Massachusetts Port Authority (Massport) on June 25, 1956. Massport controls, operates, and manages three projects: the Airport Properties, including Boston-Logan International Airport and Lawrence G. Hanscom Field; the Maurice J. Tobin Bridge; and the facilities comprising the Port of Boston. The Port of Boston facilities consist primarily of piers, buildings, and land that are located in several of the city's neighborhoods, including Boston proper, South Boston, East Boston, and Charlestown. Several of the buildings and piers are in need of extensive repair or replacement. Massport is in the midst of a series of long- and short-term development programs formulated to bring about port revitalization and subsequent economic development. One attempt at revitalization and economic development was the acquisition of the Medford Street Terminal in Charlestown.

The purpose of this audit was to determine how Massport acquires real estate and whether property that has been purchased is being managed and utilized properly. Our audit was conducted in accordance with applicable generally accepted government auditing standards for performance audits. The records examined included project files, consultant studies and internal analyses, property and rental reports, internal memoranda, financial statements and reports, general correspondence, and ground leases.

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Operating under its broad mission of operating and managing the Port of Boston, Massport acted prematurely and spent millions of dollars on property for which it has yet to find long-term water-dependent industrial uses. The first parcel of approximately 18 acres, located on the banks of the Mystic River in Charlestown with direct access to the ocean, was a former sugar refinery and was purchased in 1986 for \$6,000,430. The second parcel of approximately 3.5 acres, a former storage area for a lumber company, is located next to the sugar refinery and was purchased in 1990 for \$1,398,962. Both parcels were purchased to control and preserve them for water-dependent uses and to land-bank the properties, if necessary, until suitable uses could be found. However, Massport purchased the property without a plan for development and at a price greater than that recommended by its staff as well as the property's true value.

As a result, Massport incurred unnecessary costs for property that has very limited uses. Because the property is in a designated port area, it can only be used for water-dependent industrial use or certain accessory or supporting uses. Since November 2000, it has been used for the storage of imported automobiles. As of January 2001,

the total cost to acquire, maintain, and clean up the property, net of rental income was estimated to be \$12,151,497. It was further noted that had Massport invested its funds in traditional securities instead of purchasing the Medford Street terminal, it would have earned \$13,841,196 in interest income.

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We recommend that Massport renew its efforts to determine whether market conditions have improved for economical development, other than the storage of automobiles, and consider alternative strategies for long-term use of the property, if appropriate. Selling the property to recover some of its costs is an option that should be considered. We also recommend that Massports Board and the Legislature examine whether Massport's mission of managing and controlling the Port of Boston should include the purchase of property for preservation or land-banking to ensure water-dependent use, or whether the Department of Environmental Protection has the responsibility for this area and has adequate controls for this purpose. We also recommend that Massport prepare written policies and procedures for the acquisition of property.

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INTRODUCTION

Background

Chapter 465 of the Acts of 1956 established the Massachusetts Port Authority (Massport) on June 25, 1956. Massport controls, operates, and manages three projects: the Airport Properties, including Boston-Logan International Airport and Lawrence G. Hanscom Field; the Maurice J. Tobin Bridge, and the facilities comprising the Port of Boston. The Port of Boston facilities consist primarily of piers, buildings, and land that are located in several of the city's neighborhoods, including Boston proper, South Boston, East Boston, and Charlestown. Massport is in the midst of a series of long- and short-term development programs for the Port of Boston. These programs are part of one of several plans formulated to bring about port revitalization and subsequent economic development for Massachusetts and the surrounding region.

The Enabling Act provides for Massport to have seven board members appointed by the governor for seven-year terms, with the term of one member expiring on June 30 of each year. A staff headed by an Executive Director, who is appointed by and reports directly to the board members, carries out the management of Massport and its operations.

Massport is authorized and empowered to acquire, hold, and dispose of real property in the exercise of its powers and duties. Section 4 of the Enabling Act specifically authorizes Massport to purchase any land, property rights, rights of way, franchises, easements, and other interests in lands, as it may deem expedient, necessary, or convenient for the construction or operation of any project at reasonable price and terms. "Project" refers to the Tobin Bridge, the airport properties, the port properties, or any additional facility, including a trade and transportation center, financed or acquired under the Act.

Although the Enabling Act authorizes Massport to purchase property deemed expedient or necessary for its projects, neither the Act nor Massport policies establish further criteria to justify the purchase of property. In fact, Massport has no written procedures or policies on the

acquisition of property. However, we were advised that Massport would not purchase property unless there is a connection between the purchase and Massport's mission.

Operating under its authority to control, operate, and manage the Port of Boston, Massport in 1986 and 1990 purchased two pieces of property on the Boston waterfront. In December 1986, Massport purchased property owned by the Revere Sugar Company located on the banks of the Mystic River in Charlestown with direct access to the ocean. The property consisted of 18.19 acres, of which approximately 5.19 acres is tidal (i.e., sometimes under water); 15 buildings; and two wharves and piers constructed mostly in the 1900s. The property had been used to import partially treated refined sugar and complete the refining process at these facilities. In October 1990, Massport purchased an additional 3.5 acres of land that is adjacent to the 18.19 acres purchased from the Revere Sugar Company. This property was owned by the Somerville Lumber Company and had been used primarily for storage.

Massport indicated that it purchased these properties to preserve them for water-dependent uses and to land-bank the properties, if necessary, until suitable uses could be found. We were advised that Massport did not want to lose these waterfront sites and wanted to ensure that they would remain an integral part of the working Port of Boston. The combined property is known as the Medford Street Terminal and is in an area classified as a Designated Port Area (DPA) by Department of Environmental Protection (DEP) regulations under Chapter 91 of the Massachusetts General Laws. This means that the property can only be used for water-dependent industrial uses or certain accessory or supporting uses.

Although Chapter 91 applies to Massport, the DEP has agreed that projects consisting entirely of water-dependent industrial uses would not require a DEP license, but projects consisting of other uses would. These agreements are reflected in the DEP waterways regulations, 310 Code of Massachusetts Regulations (CMR) 9.03 (3). Although in 1990 Massport and the DEP agreed to adopt a memorandum of understanding (MOU) to further clarify DEP jurisdiction over other Massport projects, Massport negotiates MOUs on an as-needed basis. As of June 2001, Massport has concluded one MOU for its South Boston property and is negotiating a second for selected East Boston property.

Audit Scope, Objectives, and Methodology

The objectives of this performance audit were to determine how Massport acquires its real estate property and whether the property that has been purchased is being managed and utilized properly. Our audit, which covered the period December 1, 1986 to July 31, 2001, was conducted in accordance with applicable generally accepted government auditing standards for performance audits.

We examined Massport records, including project files, consultant studies and internal analyses, property and rental reports, internal memoranda, financial statements and reports, general correspondence, and ground leases. We also reviewed the Massachusetts Enabling Act with members of Massport's Legal Department and examined the minutes of the meetings of the Massport Board of Trustees and the Finance and Business Development Committee.

We also interviewed key officials in Massport's Administration and Finance Department, the Capital Program and Maritime departments, and the Environmental and Fire Chief offices. In addition, we visited both properties and obtained information from officials of the Office of Coastal Zone Management (CZM).

AUDIT RESULTS

MASSPORT PURCHASED PROPERTY FOR A COST IN EXCESS OF MARKET VALUE WITHOUT A CLEAR PLAN FOR DEVELOPMENT

In an effort to preserve waterfront sites and develop the Port of Boston, the Massachusetts Port Authority (Massport) purchased two waterfront properties, known as the Medford Street Terminal, prematurely, without a development plan and without determining what the eventual cost would be. Massport's expectation that this property would promote maritime activity in the Port of Boston has not materialized.

The reason given by Massport officials for purchasing these two properties is that Massport, which is responsible for the Port of Boston, did not want to lose waterfront sites. When these sites became available, they were purchased to preserve them for water-dependent industrial uses and to land-bank them, if necessary, until suitable uses could be found. Furthermore, Massport wanted to ensure that the properties would remain an integral part of the working Port of Boston and made several efforts to find suitable maritime industrial uses.

Massport purchased the first property without a plan to develop the property or recover costs, and at a price greater than that recommended by its staff or by consultant reports indicating the property's true worth. Moreover, the purchase was done prematurely and without any apparent consideration of the information that was available before the purchase indicating that there were limitations regarding the use of the property. Further, had a consultant cost-benefit study on the best use of the property been done before the purchase, instead of 18 months later, it is difficult to see how Massport would have purchased the property at all. Currently, Massport's plans for the property are to lease it for storage of imported automobiles.

a. Price Paid for the Property Exceeded Its Valuation

Massport became interested in the first property in October 1985, when it learned that the owners were in bankruptcy proceedings and were contemplating the sale of its waterfront property in Charlestown. The property consisted of 18.19 acres, 15 buildings, wharves, and piers. Massport contacted the firm and stated that it had the property appraised and would make an offer. The appraisal report, which was received in December 1985, valued the property at \$4.5 million. This report indicated that machinery and equipment had been removed from the buildings and that structural repairs were needed. The report also noted that Massport had not requested environmental information and its conclusions were based on the assumption that there was full compliance with the environmental laws and regulations. Moreover, prior to the purchases, a second consultant was hired to determine the property's condition. The consultant's report concluded that the buildings contained asbestos, which would cost between \$1.5 and \$2 million for removal and disposal.

Also, prior to the purchase, Massport's Maritime Operating Department prepared an internal cost-benefit analysis to determine the condition of the property and an appropriate offering price. Maritime Department staff worked with staff from Massport's Legal, Engineering, Planning, and Budget departments and evaluated potential uses, revenues, and costs to arrive at a price. The analysis indicated that the most profitable use would be to demolish the buildings and use the property for salt, cement, and lumber storage. The analysis concluded that the potential revenues from the best use for the property (after capital expenditures of approximately \$2 million to make the facility operable) would sustain a purchase offer of \$3.5 million. On February 21, 1986, these results were presented to Massport's Finance Committee, and an offering price of \$3.5 million was suggested. However, one day earlier, on February 20, 1986, Massport's Board of Trustees had already authorized the Executive Director to make an offer for the property not to exceed \$5.5 million.

Surprisingly, Massport subsequently made an offer that even exceeded this amount and submitted a purchase and sale agreement to the owner in July 1986 for \$6,250,000. However, in November 1986, the purchase price was reduced by \$249,570 to \$6,000,430 to reflect the costs to abate some of the property's pollution problems. Massport officials felt

that the negotiated price was as low as the seller would be willing to sell the property for considering the amount of debt that burdened the property. Nevertheless, the negotiated price was still \$2.5 million more than the February 1986 valuation of the property by the internal analysts and \$1.5 million more than the December 1985 valuation by the consultants. In addition, Massport purchased the adjacent property of 3.5 acres in 1990 when it became available for sale.

b. Property Has Limited Use

Massport immediately experienced difficulty in leasing and developing the property it purchased, which is not surprising given the results of the three consultant studies that were done after the property was acquired. The first study analyzed alternative maritime use options and recommended specific development plans. The report, dated November 1987, noted that the market was highly competitive in terms of competing ports, volume of terminal capacity available, and cost and efficiency of operations. The report concluded that the opportunities for the property were limited to a few high-growth or high-potential cargoes (e.g., salt, lumber, iron, steel).

The second study, which was conducted 18 months after the property was purchased, concluded that the property was unsuitable for either redevelopment or demolition. The report, dated August 1988, noted that the property had limited alternative uses deemed to be economically feasible. The report concluded that the market did not, at that point, justify either redevelopment or demolition of the buildings. Rather, it recommended that the buildings be secured until the real estate market justified the necessary expenditure for redevelopment or demolition. The third study estimated the cost of mothballing the property. In summary, a review of the consultant studies shows that Massport management's action to purchase the property was inconsistent not only with the property's value at the time of the purchase but also with the property's subsequently determined limited potential use. The Appendix contains a listing of the eight studies that have been made on this property.

In 1988, part of the property was placed under a 10-year lease to the Massachusetts Water Resources Authority (MWRA) as indicated in Report No. 93-4026-3. However, our office later determined that the MWRA did not need the property, and the lease was terminated in 1994, saving the MWRA millions of dollars. The second parcel of property was rented for approximately five of the 10 years it was owned by Massport. Although the rental income lessened the impact on Massport's overall operating costs for the properties, the overall net operating income was only slightly positive.

In 1993 and 1996, Massport initiated an effort to lease and develop both parcels of properties and was unsuccessful. A Request for Proposals (RFP) was issued for the lease and development of the properties in November 1993 and again in April 1996. In July 1996, however, Massport notified prospective respondents that the project was facing substantial delays and that the RFP process was to be delayed until further notice because the buildings on the property were being demolished. Massport officials were unable to provide us with any information regarding the responses to these RFPs because these records could not be located.

One reason why Massport was unable to rent the buildings on the property was that they contained asbestos. When asbestos becomes loose and enters the air, it becomes "friable," a condition in which asbestos becomes airborne and poses a danger to human health. According to Massport fire officials, since the buildings with asbestos could become friable, it is unlikely that Massport would have been able to rent the property without first removing the asbestos.

In November 2000, Massport began using the Medford Street Terminal, under its lease agreement with Boston Autoport LLC, to store imported automobiles until they could be delivered to respective automobile dealers. According to Massport officials, the adjacent Moran Terminal was used for such storage purposes but could no longer accommodate the increase in imports. Massport was concerned at the prospect of losing the Moran Terminal business and adopted a long-range plan to use the Medford Street Terminal property to store additional automobiles. Currently, Massport is working with Boston Autoport to conduct a

feasibility study and pursue grants for the construction of a parking structure at Moran Terminal that would house up to 5,000 cars. We were advised that the storage of imported vehicles is both the short- and long-term plan for the Medford Street Terminal property.

c. DEP Regulations Limit the Use of Property in a Designated Port Area

Another possible constraint in the development of the Medford Street Terminal is Chapter 91 of the Massachusetts General Laws and Department of Environmental Protection (DEP) regulations, which restrict the use of the property in a designated port area. Some uses (such as those that involve water-dependent industrial uses) are clearly stated and agreed to by the DEP and present no problem. Massport projects involving uses other than water-dependent industrial use, according to the DEP, require a license. For Massport projects that involve both water-dependent industrial and non-water-dependent industrial use, the regulations require Massport and the DEP to adopt a memorandum of understanding.

d. Cost of the Medford Street Terminal

As of January 2001, we estimate that the total cost to Massport to acquire, maintain, and clean up the two properties that comprise the Medford Street Terminal to be \$12,151,497, net of rental income. This does not include the cost of the consultant studies noted in the appendix because the cost data is no longer available according to Massport. It was further noted that if Massport had invested its funds in traditional securities instead of purchasing the Medford Street terminal, it would have earned \$13,841,196 in interest income in addition to the principal of \$7,399,392. It is unlikely that these amounts will ever be recovered. In January 2000, Massport's consulting engineers estimated the replacement value of the Medford Street Terminal, not including the land, at \$8,475,000. Massport's residential engineers added an additional \$900,000 to this value for MWRA's dock, which has been moved and is now being used elsewhere, thus establishing a total value of \$9,375,000.

	<u>Estimated Costs of the Medford Marine Terminal</u>		
	<u>1st Parcel</u>	<u>2nd Parcel</u>	<u>Total</u>
Acquisition	\$ 6,000,430	\$1,398,962	\$ 7,399,392
Maintenance & Security	297,995	-	297,995
Pollution Abatement	181,642	-	181,642
Demolition	4,586,561	-	4,586,561
Net Rental Income	<u>(314,093)</u>	<u>-</u>	<u>(314,093)</u>
Total Cost of Property	<u>\$10,752,535</u>	<u>\$1,398,962</u>	<u>\$12,151,497</u>
Estimated Interest Income	<u>\$12,126,387</u>	<u>\$1,714,809</u>	<u>\$13,841,196</u>

As noted in the preceding table, \$4,586,561 was spent on demolition costs. After eight years of ownership, the buildings located on the first property, which were already in poor condition when purchased, deteriorated to the point in which they presented a public health and safety concern. In 1994, the State Fire Marshal's Office and Massport's Fire Chief's Office recommended that all of the buildings, wharves, and piers be demolished since they posed a fire, health, and safety threat. Massport agreed and demolished the buildings, piers, and wharves, and a consultant was hired to ensure compliance with the environmental rules and regulations for the clean-up of hazardous sites.

Another cost incurred was the cost of operating the properties. As noted earlier, Massport was able to lease parts of the property (mostly the outside space) for approximately 10 of the 15 years it owned them. Tenants included a salt company, the MWRA, Raytheon Engineers and Constructors, Inc., and Boston Autoport. As of June 1, 2001, for the 10 years of rental activity, Massport received overall net revenue of \$314,093.

e. Potential Income Totaling \$13,841,196 Could Have Been Earned from Traditional Investments

Massport purchased the Medford Street Terminal with internally generated funds. Had Massport instead invested those funds in financial instruments, such as government

securities, it would have received a greater return on its investment. Massport normally invests its funds in U.S. Treasury notes. Through the Federal Reserve Bank, we obtained historical data on interest rates of One-Year Treasury notes for each year beginning in 1987 and ending in 2000. To determine the income that would have been earned by Massport had it invested in U.S. Treasury notes, we used the annual interest rates for our calculations.

Massport acquired the first parcel of property in December 1986 and the second in November 1990; therefore, as of January 1, 2001, Massport owned the properties for 14 and 10 years, respectively. We used the interest rates for 14 and 10 years in our calculations and estimated that the interest that would have been earned was approximately \$12,126,387 for the first parcel and \$1,714,809 for the second parcel for a total of \$13,841,196.

f. The MWRA and Other Related Costs

Although renting property to the MWRA proved to be a poor investment for the MWRA, Massport did benefit. As noted earlier, in August 1988, Massport entered into a 10-year lease agreement with the MWRA to run from August 1, 1988 through July 31, 1998. However, the lease was terminated in October 1994 as a result of an OSA report that found that the MWRA did not need to rent the property (the MWRA had not used the property the first five years of the lease and in the sixth year, against the advice of its consultants, constructed a \$5.4 million facility that was not needed). Thus, the lease was terminated before the 10-year expiration date and the MWRA saved about \$3.3 million. Massport now owns the \$5.4 million facility.

g. Current Status of the Property

In May 2000, Massport leased approximately eight acres of the Medford Street Terminal to Raytheon Engineers and Constructors, Inc., and in May 2000 agreed to amend its lease with Boston Autoport for the Moran Terminal to include approximately six acres of Medford Street Terminal space.

Massport should charge Raytheon a monthly rent of \$60,040, or \$1,050,700 over its 17 1/2-month lease.

In addition, Massport as of June 1, 2001, collected \$113,040 in rent from Boston Autoport. This lease is also tied to an escalation clause. In all, Massport expects to receive about \$2 million for the Medford Street Terminal over the next two years. The lease with Boston Autoport expires in 2008 and is primarily for the rental of Moran Terminal.

CONCLUSIONS AND RECOMMENDATIONS

Operating under its authority to control, operate, and manage the Port of Boston, Massport's purchase of two parcels of waterfront property in 1986 and 1990 was imprudent and not well thought out. Moreover, management did not follow the advice of its consultants and internal analysts and paid several million dollars more for the first parcel of property than what was recommended.

The Board and management did not give proper weight to the many problems associated with the property and acted before they had all available information that would impact the decision. For example, management did not request that the environmental status of the property be part of the appraisal report and, more significantly, did not have a cost-benefit study done until 18 months after the first parcel was purchased (rather than before). The study gave solid information that the property was in need of extensive work and was of limited use and therefore was not a very good purchase. The Board exercised poor business judgment by not conducting studies to determine all costs and conditions before they purchased this property.

Massport's purchase illustrates an ineffective and uneconomical use of resources and raises questions about Massport's management philosophy and mission that allows the acquisition of property to be preserved for water-dependent industrial use for the eventual development of the Port of Boston. These parcels were purchased for the broad goal of managing and operating the Port of Boston in order to enhance economic growth but without plans for their use and development.

Massport's mission statement includes economic development through effective planning and management of short- and long-term capital resources. However, to accomplish this goal by buying waterfront property when it becomes available and hoping to later find a satisfactory long-term economical use is not a sound business approach to development. In fact, the management philosophy of buying property for the preservation of the Port of Boston and land-banking the property, if necessary, until possible uses could be found is costly and potentially flawed because Massachusetts General Laws and DEP regulations may

preclude the use of property in a Designated Port Area (DPA) for anything but water-dependent industrial use unless a license is obtained from DEP. The licensing process is the state's way of assuring that the intent of the law (Chapter 91) and DEP regulations are fulfilled; namely to preserve DPAs for water-dependent industrial uses. Thus, there are already controls in place to preserve the use of property in a DPA for water-dependent industrial uses, and any owner of these parcels would face the same restrictions as to its use, thereby limiting economic opportunities.

Massport's ownership of these properties covers 15 and 11 years, respectively, and transcends the stewardship of five Executive Directors, yet the property has been fully utilized only a portion of the time.

Recommendation

Massport should clarify the aforementioned discrepancies by accomplishing the following:

- Examine its goal of operating, managing, and controlling the Port of Boston and determine whether buying property for preservation or land-banking to ensure water-dependent industrial use is an appropriate part of its mission or whether the DEP has responsibility for this area and adequate controls for this purpose.
- Establish written criteria, policies, and procedures with respect to the acquisition of property stipulating the use of cost-benefit analyses and all appropriate relevant studies to justify the acquisition of property before it is purchased.
- Renew its efforts to determine whether market conditions for economical development other than the Boston Autoport expansion have improved and consider alternative strategies for long-term uses of the property.
- Consider selling the property to recover some of its costs and allow the private sector to develop the property.

Auditee Response

In response, Massport stated, in part:

The decisions by Massport to purchase the property were made well over a decade ago (transactions in 1986 and 1990) under different leadership. Economic and real estate conditions were also different from the current climate, and the intervening years included a very difficult financial period. These economic factors complicated

the development of the property until fairly recently. Nonetheless, we believe that Massport's ownership of this property today is fully consistent with the Authority's mission and greatly enhances our efforts to support the regional economy by keeping the Port of Boston productive.

Our response...demonstrates that: 1) the purchase of the property is consistent with Massport's mission and business plan; 2) the property is being utilized effectively by an important tenant of the Port of Boston; 3) there is a role for Massport in preserving property for maritime industrial uses; 4) the value of the property far exceeds the purchase price; and 5) the current Massport Board employs a careful systematic approach to the acquisition of property.

The current Massport Board views the selective and strategic acquisition of property to be an essential power of the Authority, one that, as the Auditor recognizes, is provided in the Authority's Enabling Act. All of Massport's transportation facilities are constrained in land area and lie in close proximity to residential areas. Appropriate land purchases can enhance constrained transportation facilities and help to buffer the effects of our facilities on the surrounding communities. To cite recent examples, Massport has recently purchased three properties, one adjacent to Logan Airport that will be used for airport development, and two in outlying communities that will house remote "park and ride" facilities.

Auditor's Reply

This report does not address property purchased and used for Logan Airport but questions the purchase of the Medford Street Terminal in Charlestown for land-banking purposes to ensure that it would be preserved for maritime industrial use. Also, we do not believe that the purchase of the Medford Street Terminal property was necessary to achieve Massport's mission of developing, promoting, and managing the seaport or that it enhances constrained transportation facilities, as indicated in Massport's response.

Auditee's Response (Continued)

The report underestimates the significance of both the real estate parcel and the business currently located there to the local and regional economy. Medford Street Terminal is one of the few real estate parcels in the Port of Boston that has both a deep water berth and an active rail line. Its major tenant, the Autoport, is one of the port's success stories: automobile import and processing volumes continue to rise steadily (exceeding 100,000 cars last year). The operation generates more than 500 local jobs and contributes more than \$20 million annually to the local economy. Viewed in the overall context of the challenges of successfully marketing the Port of Boston amid less costly competitors, and maintaining its benefits for the local and regional economy, this was an important achievement. This is a clear example of how land banking on the waterfront can have a regional benefit and also generate income to the Authority.

Auditor's Reply

The purchase of the Medford Street Terminal is not a good example of the benefits of land banking to the region or generating income. To date the only benefits to the region are marginal and will accrue when the lease that Massport has with Boston Autoport is fully implemented, and this lease materialized only after 15 years of ownership. The income generated from the property is approximately \$2 million, which Massport expects to receive over the next two years from two property leases; one with Raytheon and the other with the Boston Autoport. It cannot be determined whether this revenue will continue to be generated when the leases expire.

The increase in local jobs and contribution to the economy referred to by Massport are not the result of the use of the Medford Street Terminal but the result of Boston Autoport's use of the Moran Terminal and Mystic Pier.

Auditee's Response (Continued)

The report states a reasonable assumption that the DEP Chapter 91 regulations should protect land located in Designated Port Areas (DPAs) from non-maritime industrial development. However, numerous examples of non-maritime industrial development throughout the Port of Boston, particularly along the Mystic and Chelsea Rivers, suggest that the regulations do not reliably protect these areas for future maritime industrial uses. Several of the properties adjacent to Medford Street Terminal, all of which are located within the DPA, are currently being used or planned for non-maritime industrial development. For this reason, we restate our belief that strategic land acquisition by Massport is a critical element in preserving waterfront property for current and future maritime industrial uses.

Auditor's Reply

The position that the DEP Chapter 91 regulations do not reliably protect land located in a DPA from non-maritime industrial development is disturbing, if accurate, and will be brought to the attention of the DEP and the legislature for their information and determination of whether increased enforcement is needed. Further, the position that strategic land acquisition is a critical element in a Massport plan to preserve waterfront property for maritime industrial use is potentially flawed and costly as previously indicated. It also raises the question of whether strategic land acquisition should be part of Massport's

mission or is the responsibility of DEP. Rather than have Massport use its funds for this purpose, the more appropriate and cost-effective solution would be for DEP to enforce the law and regulations in this area.

Auditee's Response (Continued)

We disagree with this cost estimate for two reasons. First, we believe the Authority paid a reasonable price for the property...an analysis by an expert real estate appraiser...concludes, "Based on our analysis...the investment value of the asset to Massport both then (\$10 million to \$12.6 million) and now (\$12.1 million to \$16 million) far exceeds what was originally expended to acquire the property (\$7.4 million)." Second, the imputed interest approach taken by the Auditor has no relation to Massport's capital funding structure. If the Authority had not purchased Medford Street Terminal, the funds would have been used for other capital requirements, not invested in securities for the purpose of earning interest.

Auditor's Reply

Although the current Massport appraisal values the property at the time of purchase at between \$10 million and \$12 million, in December 1985 when the property was actually purchased, the appraised value for part of the property was \$4.5 million, and in May 1990, the appraised value for the remaining part was \$1.5 million to \$1.8 million. Thus, the total appraised value of the property was between \$6.0 million and \$6.3 million, or about \$1.1 to \$1.4 million less than Massport's purchase price. Based on these earlier appraisals, which differ significantly with the current appraisals, we disagree that the purchase price was justified.

The calculation of interest revenue that was lost on money spent on this project is a method of determining the future value of money. There are other methods that can be used that might yield higher or lower results. However, the concept is important in business decisions in order to measure the cost-benefits of a project before an investment is made. Had Massport compared the expected benefits of the project with the future value of the money to be spent at the time of purchase, the true costs of the project would have been revealed to cast a completely different perspective on the purchase decision.

Auditee's Response (Continued)

The current Massport Board shares the view that a prudent approach is necessary when committing funds of the Authority. Consistent with the Board's overall careful approach to financial management, any potential purchase receives detailed scrutiny, is accompanied by a business plan, and is analyzed by at least one independent appraiser. The Auditor is correct in pointing out that there do not exist detailed written procedures for this process. As part of our ongoing comprehensive review and revision of Authority procedures, we are evaluating written guidelines that would reflect the detailed, analytical manner in which the current Board approaches such matters.

Auditor's Reply

Massport's acknowledgement that written procedures need to be developed and the action taken to develop detailed, analytical processes to be followed in acquiring property in the future are steps in the right direction. We will evaluate these processes in future audits to determine their effectiveness.

APPENDIX

Consultant and Internal Studies Conducted on the Medford Street Terminal

Date of Report	Purpose	Results
December 1985	To appraise the property	Value estimated at \$4.5 million.
February 1986	Massport internal analysis to determine the condition of the property and an appropriate price	Benefit-cost analysis based on five potential use scenarios – automobile importing, salt, cement and lumber storage, and other uses (Marina, etc.). The most profitable use would be to demolish most of the buildings and use the property for storing salt, cement, and lumber. The potential revenues from this operation would cover capital expenditures of \$2 million and a purchase price of \$3.5 million.
December 1986 (Interim Report), February 1987 (Final Report)	To determine the costs to remove, dispose of, and decontaminate all asbestos-containing materials in all buildings	Based on a walk through appraisal and visual inspection the study estimated that the removal, disposition and decontamination of all asbestos containing materials would total \$1.5 to \$2 million.
November 1987	To analyze and develop alternative maritime re-use options for the Revere Sugar Terminal and to recommend specific development plans for the facility consistent with Massport's objectives	Study indicated that the market is highly competitive in terms of port competing, volume of terminal capacity available, and cost and efficiency of operations. Thus, the opportunities for the property are limited to a few potential cargoes (e.g., salt, lumber, iron, steel).
August 1988	To identify potential development alternatives for the property, consistent appropriate uses, and sound real estate economic principles	Study indicated that the market did not, at that point, justify either development or demolition of the buildings and recommended that the buildings be made secure until either the real estate or maritime market reaches a point that will justify the necessary expenditure for redevelopment or demolition.
November 1988 (Interim Report), April, 1993 (Final Report)	To determine requirements to mothball the buildings	The consultant estimated the cost of securing the buildings would be in excess of \$1 million.

November 1996	To document conditions following the identification of a release of oil to the environment on a portion of the property	Massport satisfied two elements of a Massachusetts Contingencies Plan.
December 1998	To evaluate the extent of contamination at the property	The information the consultant has prepared is to be considered part of the imminent demolition activities.