



**THE PORT
OF LOS ANGELES**
Executive Director's
Report to the
Board of Harbor Commissioners

DATE: DECEMBER 10, 2010

FROM: EXECUTIVE OFFICES

SUBJECT: GAMBOL INDUSTRIES, INC., MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO NEGOTIATE, DATED JUNE 29, 2009; SUPPLEMENT TO JULY 26, 2010 STAFF REPORT; BOARD HEARING CONTINUED FROM JULY 28, 2010 AND NOVEMBER 4, 2010

INTRODUCTION:

Staff's July 26, 2010 report provided analysis of and recommendations on the proposals of Gambol Industries, Inc. ("Gambol") to designate the former Southwest Marine site for future use as a shipyard, and to select Gambol to operate that shipyard.¹ Staff presented its report and recommendations at the July 28, 2010 meeting of the Board of Harbor Commissioners ("Board"). At that meeting, following a presentation from the Deputy Executive Director, Development, the Board granted Gambol's request to postpone further consideration of the report and recommendations to allow Gambol additional time to formulate a response. Subsequently, at the Board's November 4, 2010 meeting, Gambol provided a presentation regarding its business plan.

This supplement to staff's July 26, 2010 report updates the Board on developments relative to key matters affecting Gambol's proposal that have occurred following the Board's July 28, 2010 meeting.

DISCUSSION:

1. The Main Channel Deepening Project Is Underway, and On-Schedule.

The Main Channel Deepening Project ("MCDP") is a federally-authorized construction project intended to deepen the Main Channel and berthing areas of the Port of Los Angeles ("POLA") to a 53-foot depth to accommodate larger container vessels. The U.S. Army Corps of Engineers ("USACE") has undertaken construction of the MCDP since the project's inception in 2002, with the Harbor Department serving as the project's local sponsor.

¹A copy of staff's July 26, 2010 report and a video of the Board's July 28, 2010 meeting are available at <http://www.portoflosangeles.org/commission/videos.asp>. The July 26, 2010 report defines the terms and acronyms (e.g., USACE, MHRP, MCDP, etc.) used in this supplement.

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The MOU between the City of Los Angeles (acting through the Board) ("City"), Gambol and the Los Angeles Conservancy ("MOU") concerns the final phase of the MCDP, which will dredge the East Basin portion of the Main Channel and portions of the berths at the Yang Ming, TraPac, Evergreen and Yusen container terminals and create disposal facilities for the resultant dredge material. USACE's contractor commenced construction of the MCDP's final phase on July 7, 2010. Construction activities remain on schedule. At the Southwest Marine site, a significant amount of heavy demolition already has occurred. Saw-cutting of major wharf and pier structures started on December 6, 2010.

The current construction schedule (dated October 5, 2010 and provided to Gambol on October 7, 2010²) calls for the following activities at the Southwest Marine site, the location where Gambol proposes to develop its shipyard:

Activity at SW Marine	Start Date	End Date	Itemized and Running Costs³
Sawcut and Demolish Wharves, Pier; Remove Piles	October 13, 2010	May 5, 2011	\$8.4 Million (\$8.4M/\$35M)
Excavate Keyway Trench, Build Toe Berm	May 11, 2011	August 27, 2011	\$1.8 Million (\$10.2M/\$35M)
Construct Rock Dike	June 22, 2011	November 22, 2011	\$8.3 Million (\$18.5M/\$35M)
Place Contaminated MCDP Dredge Material Behind Rock Dike	August 6, 2011	January 16, 2012	\$4.3 Million (\$22.8M/\$35M)
Place China Shipping Surcharge Behind Rock Dike	July 21, 2011	August 11, 2012	\$12.2 Million (\$35M/\$35M)
Place Remainder of China Shipping Surcharge at Cabrillo Shallow Water Habitat	September 18, 2012	November 9, 2012	Not a CDF cost, but critical to China Shipping expansion.

² A copy of the October 5, 2010 baseline schedule released by USACE and its construction contractor and provided to Gambol on October 7, 2010, is attached hereto as Transmittal 21.

³The contract price of the rock dike CDF is \$35,026,199. The un-parenthesized cost figures in this column depict estimated costs for the activity(ies) noted. The parenthesized cost figures depict a running subtotal of costs relative to the \$35,026,199 estimated total.

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2. The MHRP Is Not a Disposal Option for Contaminated MCDP Dredge Material.

On June 29, 2010, in response to a formal application process opened by the Port of Long Beach ("POLB"), the Harbor Department applied to place within the Middle Harbor Redevelopment Project ("MHRP") approximately 630,000 cubic yards ("CY") of MCDP dredge material. Such dredge material has three sources: (a) Source 1, roughly 160,000 CY of contaminated dredge material from the Berths 243-245 slips; (b) Source 2, roughly 163,000 CY of contaminated dredge material from project dredging; and (c) Source 3, roughly 307,000 CY of clean material presently used as surcharge on recently created China Shipping backland.⁴

The Harbor Department submitted its application to pursue the potential cost savings⁵ that could result if the MHRP could accept the dredge material destined for the Southwest Marine site when the MCDP called for disposal of that material.⁶ Notwithstanding this pursuit, at the point when the Harbor Department submitted its application, substantial doubt existed as to whether the MCDP and MHRP schedules would facilitate one another, as detailed in staff's July 26, 2010 report at pages 21-22.

Following an August 26, 2010 request for additional information from POLB⁷, to which the Harbor Department responded on September 9, 2010⁸, POLB rejected the contaminated MCDP dredge material from Source 1 and Source 2 above, and conditionally accepted the clean China Shipping surcharge material from Source 3.⁹ As

⁴ This application is one of four applications collectively attached as Transmittal 6 of the July 26, 2010 report. The MHRP is discussed in some detail on pages 6 and 7 of staff's July 26, 2010 report.

⁵ Staff believes that the maximum theoretical cost savings represented by MHRP disposal of MCDP dredge material consists of approximately \$12 million, as detailed in the City Attorney's Office's November 1, 2010 letter to Gambol's counsel, attached hereto as Transmittal 22. Gambol asserts in an October 27, 2010 letter, a copy of which is attached as Transmittal 23, that the MHRP disposal of MCDP dredge material could result in cost savings of \$30-\$35 million, but has provided no backup to support this assertion.

⁶ Under the current MCDP schedule, placement of this dredge material commences in August of 2011.

⁷ A copy of POLB's August 26, 2010 request for additional information is attached hereto as Transmittal 24.

⁸ A copy of the Harbor Department's September 9, 2010 response to POLB's request for additional information, and some of its enclosures (voluminous sampling and other technical data have been omitted) are attached as Transmittal 25.

⁹ A copy of POLB's October 18, 2010 response to the Harbor Department's application (which POLB transmitted to the Harbor Department on October 19, 2010) is attached hereto as Transmittal 26.

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to the rejection of the Source 1 and Source 2 contaminated dredge material, POLB stated:

A key purpose for providing this fill opportunity to third parties is to facilitate the dredging and safe sequestration of contaminated sediments which, if not for this project, would not have a feasible disposal option. Because Source 1 and Source 2 have an available disposal option, with all entitlements, and would displace contaminated material that would otherwise remain in the environment, acceptance of Source 1 and Source 2 would not be consistent with a key objective of this fill.

POLB clarified its response in a letter dated November 9, 2010 and reiterated its reasoning that:¹⁰

. . . [t]he material from the Southwest Marine Site and the Main Channel Sites has an available disposal option, with all entitlements. Acceptance of this material by POLB would displace other contaminated material in the fill, resulting in that other material remaining in the environment. Consequently, acceptance of this material would not be consistent with POLB's criteria and objectives for the fill, or consistent with the regional goals of the Contaminated Sediments Task Force. Therefore the material was not accepted.

POLB's letter further advises that "both the Southwest Marine Material and the Main Channel Material did not qualify for placement in the Middle Harbor Fill for several reasons, each of which individually would have been sufficient to disqualify the material from the fill."

On November 17, 2010, POLB hosted a meeting of the Contaminated Sediments Task Force ("CSTF")¹¹ at which it presented its plan for the MHRP fill. No CSTF

¹⁰ A copy of POLB's November 9, 2010 letter is attached hereto as Transmittal 27.

¹¹ As noted in staff's July 26, 2010 report, the CSTF is a multi-agency body established pursuant to SB 673 with the goal of creating a long-term strategy for managing contaminated sediments in parts of Los Angeles and Long Beach. It is comprised of representatives from the Coastal Commission, USACE, the Los Angeles Regional Water Quality Control Board, the U.S. Environmental Protection Agency, the California Department of Fish and Game, the Harbor Department, the Los Angeles County Department of Beaches and Harbors, Heal the Bay, and the Port of Long Beach.

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member agency objected to POLB's plan.¹² On December 3, 2010, Gambol submitted a comment letter to POLB in connection with the November 17 CSTF meeting.¹³

POLB's rejection of Sources 1 and 2 above leaves the rock dike CDF currently being built at the Southwest Marine site as the one and only permitted disposal site for contaminated MCDP dredge material.

3. The Fundamental Problems that Confronted Gambol's Proposal to Substitute Version 4.2 for the Rock Dike CDF in July Continue to Exist.

a. The Viability of a Steel Wall CDF to House Contaminated Sediment Remains Unknown.

As fully permitted and entitled, the MCDP contemplates construction of a confined disposal facility constructed by separating the Berths 243-245 slips at the Southwest Marine site from waters of the Main Channel with a rock dike, depositing dredge material behind that dike, and then capping the resultant land fill ("rock dike CDF"). As detailed on pages 8 through 16 of staff's July 26, 2010 report, Gambol proposes to delete the rock dike CDF from the MCDP and substitute in its place a vertical steel-walled CDF (termed "Version 4.2"), which would maximize the preserved water area of the Berths 243-245 slips for use by floating dry docks in shipyard operations.

Staff's July 26, 2010 report details Gambol's failure to convince the third-party agencies that must approve Version 4.2 before it could be built that, from a general technical perspective, a steel-walled vertical structure can and will segregate contaminated sediments in perpetuity, and that Version 4.2, specifically, will, indeed, segregate contaminated sediments in perpetuity.

Almost four months later, these third-party agencies remain unconvinced. Since the July 28, 2010 Board meeting, no facts have surfaced to confirm the viability of Version 4.2. On September 2, 2010, staff of the California Coastal Commission ("Coastal Commission") responded to Gambol's July 27, 2010 submittal of a memorandum and supporting documentation purporting to prove that the steel wall CDF could segregate contaminated sediments from ocean waters in perpetuity, a

¹² On November 30, 2010, POLB circulated draft meeting minutes for the November 17, 2010 CSTF meeting, which include comments provided by meeting attendees. A copy of these minutes is attached hereto as Transmittal 28.

¹³ A copy of Gambol's December 3, 2010 comment letter to POLB is attached hereto as Transmittal 29.

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requirement that Coastal Commission staff repeatedly had emphasized. The response from Coastal Commission staff states, in part:

In conclusion, the submitted document does not provide evidence that the Open Cell technology¹⁴ has been used to successfully and permanently isolate and contain contaminated sediments in the marine environment. Five projects using sheet pile walls to contain contaminated sediments were referenced but insufficient information was provided to undertake a substantive evaluation of those projects, their success, or their similarities to the POLA Berths 243-245 project site (Minamata Bay, Japan; Waukegan Harbor, IL; Everett, MA; Cleveland, OH; Brown County, WI), or if conclusions could be drawn that could be applicable to the Open Cell technology.¹⁵

This remains the position of the Coastal Commission.

b. Even in the Best-Case Scenario, Substituting Version 4.2 for the Rock Dike CDF Would Substantially Delay the MCDP Schedule, Resulting in Significant Cost Impacts.

Staff's July 26, 2010 report lists the entitlements required to build Version 4.2, analyzes why obtaining them would take years, and concludes that, if undertaken, this process would materially and substantially delay the MCDP schedule. In response, Gambol has asserted that a "supplemental analysis" of Version 4.2's substitution for the rock dike CDF could suffice as USACE's required analysis under the federal National Environmental Policy Act ("NEPA") and, in so doing, could compress the entitlements timeline sufficiently to achieve schedule consistency with the MCDP.¹⁶

USACE regulatory and legal staff disagrees with Gambol's assertion. USACE advises that a supplemental analysis, if pursued, would take at least six months to complete. However, USACE additionally state, based on the information Gambol has provided on Version 4.2, that such a supplemental analysis in all likelihood would fail to constitute a sufficient NEPA analysis, and that a supplemental EIS, which would take an estimated 24 to 36 months to complete, would likely be necessary to satisfy NEPA.¹⁷

¹⁴ The Open Cell Technology is the proprietary design on which Version 4.2 is based.

¹⁵ A copy of the December 6, 2010 e-mail from Larry Simon of Coastal Commission staff to the City Attorney's Office, which attached his September 2, 2010 communication to Gambol's counsel is attached hereto as Transmittal 30.

¹⁶ The July 26, 2010 report addresses this scenario at pages 11-14.

¹⁷ A copy of the letter from USACE's Office of Counsel dated December 9, 2010 regarding the supplemental analysis process is attached hereto as Transmittal 31.

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It bears noting that, even if one were to ignore USACE's input and provide Gambol every benefit of the doubt with respect to design, entitlements, pre-construction and construction, substituting Version 4.2 for the rock dike CDF would delay the Harbor Department's ability to deposit contaminated MCDP dredge material in a CDF at the Southwest Marine site by almost 12 months, and would delay overall MCDP completion by approximately six months.¹⁸

As to costs, as noted in staff's July 26, 2010 report, Gambol and the Harbor Department essentially agree that Version 4.2 would cost roughly \$41 million to build, in comparison to the rock dike CDF's contract price of \$35.5 million. As such, Gambol's proposal to substitute Version 4.2 for the rock dike CDF would add approximately \$5.5 million in MCDP costs. This analysis remains unchanged.

Also as to costs, as noted in staff's July 26, 2010 report on pages 15 and 16, any delays to the MCDP's completion have actual and significant economic consequences. The Harbor Department will lose an estimated \$447,000 in rental income for every month it cannot deliver 18 acres of backland to China Shipping, which backlands presently are covered with surcharge material that will be disposed of in the MCDP. Also, extending the duration of the MCDP beyond its scheduled completion date will cost \$4,170 per calendar day, under the construction contract. As such, from the standpoint of these two factors alone, late completion of the MCDP will cost the Harbor

¹⁸ USACE's contractor, which has built numerous in-water steel sheet-pile structures and which currently is involved in a project using a steel sheet-pile structure designed by the same firm that would design Version 4.2, opines that construction would take 398 working days.

Assuming, for the sake of argument, that, (a) on December 16, 2010, Gambol starts the final design process for Version 4.2 (Gambol still has not generated a final design for Version 4.2), (b) a supplemental analysis can suffice as full NEPA analysis of the substitution of Version 4.2 for the rock dike CDF, notwithstanding USACE's recent input, (c) Gambol obtains every entitlement necessary to construct Version 4.2 within the six months identified by USACE as a theoretical time frame in which the likely insufficient supplemental analysis could complete, (d) Gambol completes necessary pre-construction activities within the durations listed in its own July 13, 2010 schedule (geotechnical and design work (110 working days), USACE's negotiation of the contract modification to substitute Version 4.2 for the rock dike CDF (90 working days), and procurement and delivery of materials to construct Version 4.2 (95 working days)), and (e) then builds Version 4.2 in the 398 working days estimated by USACE's construction contractor, Version 4.2 could start accepting contaminated MCDP dredge material on August 2, 2012, and the MCDP would complete on May 21, 2013. Under the MCDP's current schedule, the rock dike CDF will start accepting contaminated dredge material on August 6, 2011, and the MCDP would complete on November 9, 2012. This equates to a delay of the Harbor Department's ability to deposit contaminated MCDP dredge material in a CDF at the Southwest Marine site of almost 12 months, and a delay of overall MCDP completion of approximately six months.

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Department approximately \$19,070 per day ($\$447,000 \div 30 \text{ days} = \$14,900/\text{day}$. $\$14,900/\text{day} + \$4,170/\text{day} = \$19,070$). Delaying the MCDP's completion by the six months noted above would cost the Harbor Department roughly \$3.43 million.

4. Continued Review and Discussion of Basic Facility-Related Tasks to Develop a Shipyard Has Failed to Dissuade Staff from its Conclusion that Gambol Has Underestimated Development Costs by Approximately \$56 Million.

Staff's July 26, 2010 report details on pages 16 and 17, and in Transmittal 20, Gambol's failure to identify approximately \$60 million of necessary facility-related costs in its business plan. Following the July 28, 2010 Board meeting, staff and AECOM continued that analysis. AECOM's updated report generated in October of 2010 indicates approximately \$56 million in facility-related costs that Gambol's business plan either does not account for, or underestimates, consistent with its earlier estimate.¹⁹

At its November 4, 2010 meeting, the Board requested that staff and Gambol meet to discuss Gambol's business plan and, particularly, the differences in their views on development costs and on the likelihood of commercial viability/success for the proposed shipyard development. On November 12, 2010, Gambol and staff met for approximately four hours to discuss development costs. Following that meeting, the positions of staff and Gambol on development costs remain, for the most part, unchanged. Staff continues to view Gambol's business plan as failing to account for tens of millions of dollars of development costs, as well as failing to support with verifying facts and data the costs assertions in its business plan.²⁰ Gambol disputes these views, and claims that its business plan and subsequent analyses²¹ accurately state the costs necessary to develop a shipyard at the Southwest Marine site.

¹⁹ A copy of AECOM's October 21, 2010 report is attached hereto as Transmittal 32.

²⁰ Gambol and the Harbor Department exchanged correspondence on development costs following the November 12, 2010 meeting. A copy of Gambol's letter dated November 18, 2010 is attached hereto as Transmittal 33, and a copy of the Harbor Department's letter dated November 30, 2010 is attached hereto as Transmittal 34.

²¹ Gambol provided comments on staff's development costs analyses on November 30, 2010. A copy of those comments is attached hereto as Transmittal 35.

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5. Continued Review and Discussion of Market and Economic Issues Has Failed to Allay Staff's Significant Concerns Regarding the Commercial Viability of Gambol's Proposed Shipyard.

Staff's July 26, 2010 report sets forth specific concerns regarding the market and economic analysis and assertions in Gambol's business plan. Gambol responded to these concerns with a presentation provided at the November 4, 2010 Board meeting. On November 30, 2010, staff and Gambol met to continue discussion of staff's concerns.

As to the outcome of these discussions, in summary, Gambol remains confident in its abilities to develop a shipyard, capture market and operate a business as depicted in its business plan. Staff, on the other hand, continues to possess substantial concerns regarding the existence of the basis for such confidence, and Gambol's repeated inability to support that confidence with verifiable facts and data.

6. An October, 2010 Industry Presentation Underscores the MCDP's Critical Importance to the Harbor Department.

On October 6, 2010, the CSULB's Center for International Trade and Transportation held a symposium entitled "Panama Canal Expansion: The Battle for Jobs and Cargo."²² The symposium focused on the 2014 opening of the \$5.5 billion Panama Canal expansion, which will increase the maximum vessel size the canal can handle from 4,500 TEUs to 12,000 TEUs, and outlined how that expansion threatens diversion of discretionary cargo (cargo for ultimate delivery to a destination outside California) currently handled by the San Pedro Bay ports.

Apart from the information presented at the symposium, it is clear that the Harbor Department's competitors are in the midst of a major expansion boom, in large part to compete for a class of large ships that will be able to transit the Panama Canal after 2014. To illustrate, the Port of Halifax, Nova Scotia will shortly embark on a project to add up to 2.5 million TEUs of annual capacity that will directly target the U.S. Midwest market served by the Harbor Department. The Port Authority of New York will expand its on/near dock rail capacity to 1 million TEUs and, by 2012, will possess water depth of 52 feet. The Port of Virginia, at Norfolk, Virginia has projects underway to add 3 million TEUs of capacity. Proposed projects would add capacity of an additional 3.5 million TEUs. The Port of Virginia's water depth is 56 feet. The ports of Charleston, Savannah, Mobile and Jacksonville all are pursuing or building terminal projects that, if

²² Available at <http://www.mettrans.org/pointcounterpoint/index.html>.

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realized, will add close to 5 million TEUs of aggregate capacity. The Port of Houston is constructing the \$1.4 billion Bayport Terminal, that will add 2.3 million TEUs of capacity.

Nearer to the Harbor Department, the Prince Rupert Port Authority in British Columbia has approximately \$2.3 billion of infrastructure projects underway to help it better serve the U.S. Midwest market. The Port of Seattle plans approximately \$1 billion of capital projects over the next 10 years, including terminal expansions and dredging projects to accommodate the next generation of larger cargo ships. In September of 2009, the Port of Oakland completed a \$432 million dredging project to obtain 50 feet of depth. And, as we know, POLB has approved and is preparing to commence the 10-year, \$750 million MHRP.

To retain and, hopefully, to grow market share, and to continue to generate well-paying jobs²³, POLA must effectively compete for the large vessels that contain both local and discretionary cargo. The number and scope of the infrastructure projects underway in rival ports ensures that competition for these large vessels will be fierce. Completion of the MCDP clearly will facilitate the Harbor Department's (and its tenants') ability to succeed in that competition.

CONCLUSION:

Staff will be available at the Board's December 16, 2010 meeting to address questions or comments the Board may have.

²³Goods movement through POLA supports approximately 5,000 direct and 9,000 discretionary jobs for every 1 million TEUs of cargo handled. The expansion projects the Harbor Department presently plans will increase POLA's capacity to 22 million TEUs, which would ultimately support 110,000 direct and 198,000 secondary jobs in the region at capacity. The logistics industries provide blue-collar jobs that can replace the region's rapidly depleting manufacturing jobs. Like manufacturing jobs, entry-level logistics jobs do not require significant training or college degrees, and provide entry-level pay with on-the-job training and a defined career ladder. Also, logistics jobs pay almost twice the median regional salary.

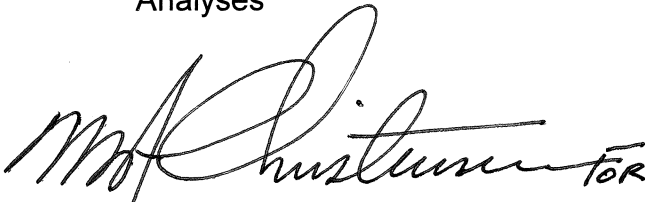
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TRANSMITTALS:

21. October 5, 2010 Baseline Schedule from USACE and Its Contractor
22. November 1, 2010 Letter from City Attorney's Office to Gambol Counsel
23. October 27, 2010 Letter from Gambol Counsel to City Attorney's Office
24. August 26, 2010 Request for Additional Information from POLB to POLA
25. September 9, 2010 Letter from POLA to POLB re MHRP Application - MCDP
26. October 18, 2010 Letter from POLB to POLA re MHRP Application - MCDP
27. November 9, 2010 Letter from POLB to POLA re MHRP Application - MCDP
28. Draft Minutes of November 17, 2010 CSTF Meeting Prepared by POLB
29. December 3, 2010 Letter from Gambol Counsel to POLB
30. December 6, 2010 E-Mail from Larry Simon of Coastal Commission to City Attorney's Office
31. December 9, 2010 Letter from USACE's Office of Counsel re Supplemental Analysis Process
32. October 21, 2010 Report Prepared by AECOM
33. November 18, 2010 Letter from Gambol Counsel to POLA re Development Costs
34. November 30, 2010 Letter from City Attorney's Office to Gambol Counsel re Development Costs
35. November 30, 2010 Comments from Gambol to Staff's Development Costs Analyses



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