



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

DATE: JULY 26, 2010

FROM: EXECUTIVE OFFICES

**SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009**

SUMMARY:

On June 29, 2009, the Harbor Department entered into a "Memorandum of Understanding for Exclusive Right to Negotiate" with Gambol Industries, Inc. ("Gambol"), and the Los Angeles Conservancy ("MOU").¹ Among other things, the MOU created a one-year exclusive negotiating period for Gambol to attempt to convince the Harbor Department to designate the former Southwest Marine premises ("Southwest Marine site") along the Main Channel of the Port of Los Angeles ("POLA") for future use as a shipyard, and then to select Gambol to operate that shipyard.

The MOU establishes how Gambol's proposed shipyard project must be submitted to and acted upon by the Harbor Department:

- First, before the end of the one-year exclusive negotiating period, Gambol must submit a "Conceptual Project Description" and a "Proposed Business Plan." The MOU also requires that the Harbor Department and Gambol work collaboratively during that period to try to minimize fill, and to preserve water area of the Berths 243-245 slips at the Southwest Marine site.
- Second, staff must review Gambol's proposed project and provide recommendations in a single report to the Board of Harbor Commissioners ("Board").

¹ A copy of the MOU is attached hereto as Transmittal 1.

DATE: JULY 26, 2010

PAGE 2 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

- Third, the Board must decide whether to designate the Southwest Marine site for future use as a shipyard. In making this decision, "the Board retains its full discretion to proceed in any manner it deems best at such time."
- Fourth, if the Board designates the Southwest Marine site for future use as a shipyard, it then must determine whether facts exist to support findings that issuing a sole-source shipyard lease to Gambol is in the best interests of the Harbor Department.

The one-year exclusive negotiation period will expire upon the Board action noted in the third item above. Gambol submitted its "Conceptual Project Description" on January 22, 2010. It submitted a portion of its "Proposed Business Plan" on June 28, 2010 and designated the bulk of it confidential. Staff has reviewed both these submittals, and the rest of the information comprising Gambol's proposed project.

As such, the first and second phases of the process above have been completed, triggering the need to commence the third phase. Pursuant to Section 2(g) of the MOU, this report sets forth staff's analysis of Gambol's proposal, and provides recommendations to the Board.

Staff's recommendations are based on significant flaws in Gambol's proposal to preserve water area at the Berths 243-245 slips. That proposal would delay the Main Channel Deepening Project by a minimum of 16 months, and would result in millions of dollars of additional costs, in material violation of fundamental provisions of the MOU. Additionally, such delay would likely impact ongoing terminal developments at the China Shipping and TraPac terminals, resulting in both monetary and operational damage.

Staff's recommendations also are based on Gambol's failure to provide persuasive evidence of the commercial viability of the proposed shipyard. The economic scope of Gambol's misstatement of the tasks necessary to physically build the shipyard it desires -- it omits or underestimates close to \$60 million worth of work -- renders the feasibility of its project doubtful. Furthermore, Gambol's business plan does not establish a convincing strategic and financial case for the Harbor Department to depart at this time from its present long-range planning for the site.

On these grounds, which are discussed in detail below, staff recommends that the Board decline to designate the Southwest Marine site for future use as a shipyard at this time, and decline to direct staff to commence lease negotiations with Gambol. The Board should note that such actions would leave the land use of that site and any

DATE: JULY 26, 2010

PAGE 3 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

landfills created thereon through the Main Channel Deepening Project open and available for future designation as the Board sees fit, and would not permanently foreclose on the possibility of a shipyard use at the Southwest Marine site, or Gambol as its operator. Rather, such actions would end the MOU-created exclusive relationship with Gambol that, for the past year, has required the Harbor Department to entertain in a single proposal, for a single use at the Southwest Marine site. In so doing, they would return land use planning for the Southwest Marine site to the norm consistent with the Charter, the Harbor Department's leasing policy, and the Harbor Department's role as a trustee for public lands, which require land use decisions be made based on a public and wide-ranging assessment of potential uses open to all entities interested in operating within POLA.

RECOMMENDATIONS:

It is recommended that the Board:

1. Decline to designate the Southwest Marine site for future use as a shipyard, pursuant to Section 2(g) of the MOU;
2. In connection with the foregoing, also decline to direct the commencement of negotiations with Gambol for a lease of the Southwest Marine site for purposes of operating a shipyard, also pursuant to Section 2(g) of the MOU; and
3. Adopt Resolution No. _____.

DISCUSSION:

1. BACKGROUND

The Board held a public meeting on May 18, 2010 to discuss the then-current status of Gambol's proposal. Staff's report for that public meeting, which is incorporated herein by reference, contained a detailed summary of facts. The subsections below do not repeat that detailed discussion, but highlight facts key to staff's analysis, and update items that have developed or changed since the May 18, 2010 Board meeting.

a. The MCDP

The Main Channel Deepening Project ("MCDP") is a federally-authorized construction project that started in 2002. The purpose of the project was and is to

DATE: JULY 26, 2010

PAGE 4 OF 26

**SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009**

deepen the Main Channel and berthing areas of POLA to a 53-foot depth to accommodate the growing size of existing and future container vessels.

Pursuant to a formal Project Cooperation Agreement, 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. The final phase of the MCDP -- which is the subject of the MOU -- includes: dredging of the East Basin portion of the Main Channel and portions of the berths at the Yang Ming, TraPac, Evergreen and Yusen container terminals to a 53-foot depth; removal and disposal of dredge surcharge material at the China Shipping premises; and the creation of disposal facilities for the dredge material that results from that deepening (up to 3 million cubic yards).

The MCDP is critically important to the Harbor Department. In fiscal year 2008/2009, the Harbor Department derived 74% of its overall revenues from its container terminals (\$286 million of \$402 million). Thus, it does not overstate matters to say that the Main Channel effectively constitutes the Harbor Department's lifeline, and that timely completion of the MCDP is critical to preserving the competitive positions of both the Harbor Department and its tenants, and to allowing POLA to continue to serve the many communities and interests that rely on it. To illustrate this point, the MCDP will facilitate delivery of 18 acres of backland to China Shipping, and five acres of backland to TraPac. These deliveries of land conform with obligations in the operative lease documents between the Harbor Department and these two tenants, and will materially improve operational efficiencies, and economics, once accomplished.

The final phase of the MCDP possesses all necessary permits and entitlements to construct. USACE and its contractor have executed the contract documents necessary to start construction, and construction has started.²

The Southwest Marine site plays a key role in the final phase of the MCDP. The two slips at Berths 243-245 are to be demolished, and physically separated from the Main Channel through construction of a rock dike, thereby creating a confined disposal facility ("rock dike CDF"). It is the project's only disposal facility designed to house dredge material not suitable for ocean disposal, which currently is estimated at 163,000 cubic yards ("CY"). Rock dike CDFs have been employed successfully to segregate contaminated sediments from ocean waters for many years, and, because of this track

² A copy of the contract modification, formally termed an "Amendment of Solicitation/Modification of Contract" and dated July 7, 2010, is attached hereto as Transmittal 2. Actual project construction started on July 22, 2010 with placement of rock at the Cabrillo shallow water habitat.

DATE: JULY 26, 2010

PAGE 5 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

record, have received routine approval by the resource agencies with jurisdiction over such sediments. Most of these agencies are members of the Contaminated Sediments Task Force ("CSTF").³

The creation of disposal capacity for MCDP dredge material is not the only benefit of the rock dike CDF. It also solves a substantial pre-existing environmental problem by entombing and capping legacy shipyard contamination at the bottom of the slips which are the subject of a remedial action order issued by the Department of Toxic Substances Control ("DTSC"). Additionally, the landfill resulting from the rock dike CDF creates eight acres of new, revenue-generating land that has significant strategic importance to the Harbor Department, as discussed below.

b. The FSEIS/FSEIR and the MOU

Following a five-year environmental review process, on April 29, 2009, the Board certified the Final Supplemental Environmental Impact Statement/Final Supplemental Environmental Impact Report ("FSEIS/FSEIR") for the final phase of the MCDP, and subsequently approved Amendment 24 to the Port Master Plan ("PMPA 24"). These two actions were among the last steps necessary to construct the final phase of the MCDP.

In May of 2009, Gambol and the Los Angeles Conservancy ("LAC") appealed the Board's certification of the FSEIS/FSEIR to the Los Angeles City Council, and contested approval of PMPA 24 to the California Coastal Commission, arguing that the Harbor Department had failed to evaluate alternatives to filling the slips at the Southwest Marine site and failed to assess the viability of a shipyard use on that property. On June 29, 2009, the Harbor Department, Gambol and LAC entered into the MOU. Among other things, the MOU resolved the disputes then-pending among the parties and resulted in withdrawal of the appeals.

³ The CSTF is a multi-agency body established pursuant to SB 673, formed to create 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.

DATE: JULY 26, 2010

PAGE 6 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

c. The Southwest Marine Site Has Significant Strategic Importance to the Harbor Department

The eight new acres of land the rock dike CDF would create, and the Southwest Marine site in general, are linchpins of the Harbor Department's tentative long-term strategic planning for revitalizing Terminal Island. That strategic planning process commenced in 2007 with the Harbor Department's \$27.7 million acquisition of the 117-acre parcel then-occupied by Los Angeles Export Terminal, Inc. ("LAXT") through a negotiated permit termination.

At present, the Harbor Department plans to use the Southwest Marine site to relocate commercial fishing to allow development of a rail facility on the former LAXT premises and the surrounding area, and a future 25-acre landfill for backland container-handling uses.⁴ This rail facility, if developed, would add on-dock rail capacity that would optimize cargo-handling efficiency at the terminals on and adjacent to Terminal Island, including the Evergreen, YTI and APL terminals. The 25-acre landfill in Fish Harbor would directly increase cargo handling capabilities. At present, this Terminal Island plan is projected to accommodate the handling of an additional 1 million twenty-foot equivalent units ("TEUs") annually, which would result in the creation of approximately 4,000 new jobs. In addition, the Southwest Marine site will be used to relocate a marine fueling station from an area adjacent to Ports O' Call Village⁵

The Board should note that the foregoing strategic planning is conceptual only. Eventual development will require the Harbor Department to obtain the appropriate permitting and entitlements pursuant to, among other things, the California Coastal Act ("Coastal Act") and the California Environmental Quality Act ("CEQA").

d. The Port of Long Beach's Middle Harbor Redevelopment Project

On May 26, 2010, the Port of Long Beach ("POLB") released a solicitation seeking applications from interested parties able to deliver dredge material to assist POLB in the construction of 65 acres of new land (equivalent to 2.5 million CY of dredge material) for ultimate use as a container terminal or terminals.⁶ This project is called

⁴ Gambol was advised of these plans in March of 2009, in the Harbor Department's written denial of its application (submitted in February of 2009) to develop a ship repair facility, to house commercial fishing operations relocated from Fish Harbor, and to conduct motion picture and television filming, a copy of which is attached hereto as Transmittal 3.

⁵ An aerial photograph of Fish Harbor attached hereto as Transmittal 4.

⁶ A copy of POLB's solicitation for deposit of dredge material in its MHRP is attached hereto as Transmittal 5.

DATE: JULY 26, 2010

PAGE 7 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

the Middle Harbor Redevelopment Project ("MHRP"). POLB's website, as of July 16, 2010, stated that construction of the MHRP is expected to begin in late 2010. POLB's solicitation indicated that it planned to start accepting dredge material in early 2011 and to close the fill in mid to late 2012.

On June 29, 2010, the Harbor Department submitted four separate applications to POLB, one of which seeks to deposit in the MHRP the totality of dredge material currently destined for disposal at Berths 243-245, plus an additional estimated quantity representing the contaminated sediment that would need to be dredged from the bottom of the Berths 243-245 slips if they are left open, rather than filled and capped.⁷ If POLB grants the Harbor Department's application, and if the MHRP can accept all of the dredge material from Berths 243-245 without adversely impacting the MCDP schedule, a possibility exists that no CDF would need to be built at the Southwest Marine site. As discussed below, how, and under what timeframes, these two variables will resolve is substantially uncertain at present.

2. GAMBOL'S PROPOSED PROJECT

The substance of Gambol's proposed project is set forth in three sources: (a) the "Conceptual Project Description" it submitted on January 22, 2010;⁸ (b) the portion of its "Proposed Business Plan" it submitted on June 28, 2010;⁹ and (c) the information underlying what has come to be known as "Version 4.2" of the steel wall CDF. In general terms, Gambol's proposed project consists of:

- Gambol's desire to alter the MCDP as currently permitted and entitled, to substitute a steel-walled vertical containment system ("steel wall CDF") in place of the rock dike CDF, at the Berths 243-245 slips;

⁷ A copy of the Harbor Department's four applications, including the one regarding the dredge material currently destined for Berths 243-245 of the Southwest Marine site, are collectively attached hereto as Transmittal 6.

⁸ A copy of Gambol's January 22, 2010 "Conceptual Project Description" is attached hereto as Transmittal 7.

⁹ A redacted copy of the portion of its "Proposed Business Plan" it submitted on June 28, 2010 is attached hereto as Transmittal 8. Gambol has designated the bulk of its "Proposed Business Plan" as confidential, preventing the Harbor Department from publicly disclosing most of its contents. In December of 2009, Gambol submitted a Market Analysis, a copy of which is attached as Transmittal 6 to staff's May 13, 2010 report. Gambol bases its "Proposed Business Plan" in part on the content of this Market Study.

DATE: JULY 26, 2010

PAGE 8 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

- Gambol's desire to reuse and, where necessary, refurbish, redevelop or construct infrastructure on the existing Southwest Marine site to develop a state-of-the-art shipyard; and
- Gambol's contention that it can develop, operate and maintain a commercially viable shipbuilding and ship repair business at the Southwest Marine site.

This report analyzes each of these components of Gambol's proposed project below.

3. ANALYSIS OF GAMBOL'S PROPOSED PROJECT

a. Substituting Version 4.2 for the Rock Dike CDF, as Proposed by Gambol, Would Result in Material Violations of the MOU.

Gambol proposes to substitute the steel wall CDF for the rock dike CDF in order to maximize the water area in the Berths 243-245 slips so it can use floating drydocks in its shipyard operations.¹⁰ In comparison to the rock dike CDF,¹¹ the steel wall CDF maximizes water area in two ways: through a vertical structure (as opposed to the rock dike CDF's pyramid-shaped structure); and through a reduced footprint -- the steel wall CDF fills only a portion of the slips (4.2 acres), which the rock dike CDF, as permitted and entitled, would completely fill (8 acres).

Over the course of the MOU's exclusive negotiating period, Gambol evolved its concept for the steel wall CDF to accommodate greater volumes of dredge material and to lower costs, to the point where it now proposes to substitute Version 4.2 of the steel wall CDF ("Version 4.2") for the rock dike CDF.¹² Section 6 of the MOU requires Gambol to demonstrate that substitution of Version 4.2 for the rock dike CDF will neither (a) delay the MCDP schedule, nor (b) add costs in addition to those that would be spent to build the rock dike CDF. As discussed below, Gambol has failed on both counts.

¹⁰ Section 5 of the MOU requires Gambol and the Harbor Department to "engage in a collaborative process" to develop an acceptable method to maximize the water area in the slips. In discharging its obligations under Section 5, Harbor Department staff, among other things: (a) devoted thousands of hours of staff and consultant time working with Gambol on its design for the steel wall CDF; (b) provided Gambol access to thousands of pages of documents related to the MCDP; and (c) reached out to and arranged meetings on Gambol's behalf with numerous resource and permitting agencies involved in the MCDP, including USACE, the CSTF, the California Coastal Commission and the Department of Toxic Substances Control, as well as the project's contractor.

¹¹ A drawing of the rock dike CDF is attached hereto as Transmittal 9.

¹² A conceptual drawing of Version 4.2 is attached hereto as Transmittal 10.

DATE: JULY 26, 2010

PAGE 9 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

1. Substituting Version 4.2 for the Rock Dike CDF Would Significantly Delay the MCDP Schedule.

On July 13, 2010, Gambol submitted an updated schedule for the permitting, entitlement, design and construction of Version 4.2 that reflects consistency with MCDP scheduling, but that contains errors, omissions and misrepresentations of such magnitude that they render the schedule functionally worthless.¹³ The reality is, based on staff's analysis, current facts, and input received from the CSTF, the California Coastal Commission ("Coastal Commission") and USACE, the substitution of Version 4.2 for the rock dike CDF will result in years of delay to the MCDP.

a. Gambol's Failures to Convince Resource Agencies of the Viability of the Steel Wall CDF Methodology and to Generate a Final Design of Version 4.2 Prejudice Any Ability to Obtain the Necessary Permitting and Entitlements.

Gambol's concept for using a steel-walled vertical structure to build a CDF that will segregate contaminated sediments from ocean waters in perpetuity is novel.¹⁴ While steel-walled structures of the type proposed by Gambol have been used to construct wharves, bulkheads and landfills, they never (to the knowledge of Gambol, the Harbor Department, USACE and the numerous other resource agencies to whom Gambol has presented the concept) have been used to construct a CDF meant to permanently house contaminated sediment.

Two key prerequisites exist for obtaining the necessary permits, entitlements and approvals to substitute Version 4.2 for the rock dike CDF: (a) convincing the issuing agencies that, from a general technical perspective, a steel-walled vertical structure can and will segregate contaminated sediments in perpetuity; and (b) convincing those same issuing agencies that Version 4.2, as specifically designed and proposed to be built at the Southwest Marine site, will, indeed, segregate contaminated sediments in perpetuity.

¹³ A copy of Gambol's July 13, 2010 schedule is attached hereto as Transmittal 11.

¹⁴ The Al Larson Boat Shop ("ALBS") plans to implement a steel walled vertical structure to house contaminated sediment in a potential new development at its current site in POLA. The CSTF has approved use of this structure, in large part because the sediment behind the steel wall will be cement-fixed, which essentially will convert the contaminated sediment into a solid fixed block. Gambol has confirmed that it will not cement fix the sediments in connection with Version 4.2.

DATE: JULY 26, 2010

PAGE 10 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

Regarding the first prerequisite, the resource agencies with jurisdiction over the MCDP, while open to receiving information from Gambol, presently remain unconvinced that a steel wall CDF can segregate contaminated sediments from ocean waters in perpetuity.¹⁵ Staff of the Coastal Commission expressed this very sentiment in its April 8, 2010 letter to the Harbor Department and Gambol,¹⁶ and reiterated its position on July 21, 2010.¹⁷ While Gambol represented months ago to Coastal Commission staff that it would transmit data to support the viability of the steel wall CDF methodology, Gambol to date has failed to follow through; Coastal Commission staff has received no such supporting data from Gambol.

Regarding the second prerequisite, Gambol to date has failed to generate a final design for Version 4.2. Its design remains at the same conceptual level as it was on May 18, 2010, when Gambol presented it to the Board as the successor to Version 4.1 of the steel wall CDF.¹⁸ While Gambol's schedule depicts final design of the steel wall CDF starting at 60% completion on June 11, 2010, this misrepresents the facts. Its schedule also depicts final design ending on September 18, 2010, which is highly unlikely, given Gambol's failure to perform necessary geotechnical work¹⁹ to support a final design, and the evolutionary process usually required to generate final engineering designs.

Gambol's two failures, until rectified, will significantly prejudice, if not eradicate the ability to obtain the necessary permits and entitlements to substitute Version 4.2 for the rock dike CDF. The reality is that permits, entitlements and approvals to build a

¹⁵ These resource agencies are identified in the "Resource Agency Coordination" section of the FSEIS/FSEIR (Sec. 1.12), attached hereto as Transmittal 12, and include the CSTF agencies, US Fish and Wildlife Service, NOAA Fisheries, and the California Department of Fish and Game.

¹⁶ A copy of the April 8, 2010 letter from Coastal Commission staff to the Harbor Department is attached hereto as Transmittal 13.

¹⁷ A copy of the July 21, 2010 letter from Coastal Commission staff to the Harbor Department and Gambol is attached hereto as Transmittal 14.

¹⁸ As is the case with Version 4.2, Gambol generated conceptual designs only for Version 4.1.

¹⁹ Building sheet-pile structures like Version 4.2 requires a geotechnical test-pile program, in which steel sheets like those intended to be used to build the steel wall, are driven into the areas around the site to determine the necessary sheet dimensions to incorporate into a final design, and key construction metrics such as pile-driving criteria, production times and rates. Gambol recognizes the importance of such a test-pile program to its proposed project, as it lists the program on its schedule. The problem, however, is that Gambol's schedule depicts the test-pile program as having started on June 11, 2010 and having completed on June 20, 2010, 10 working days later. In fact, Gambol has not yet commenced a test-pile program, and the statements on its schedule regarding the test-pile program misrepresent reality.

DATE: JULY 26, 2010

PAGE 11 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

structure using a system in an unproven application, and which has not been fully designed, are very unlikely to be issued.

b. The Necessary Permits and Entitlements to Effect the Substitution of Version 4.2 for the Rock Dike CDF Will Take Years to Obtain.

The permitting and entitlement process for the final phase of the MCDP took USACE and the Harbor Department five years to complete. Altering the MCDP by deleting the rock dike CDF and building Version 4.2 in its place, as proposed by Gambol, would undo those existing permits and entitlements, and require a brand new set of approvals, none of which presently exist.²⁰ The information provided to date by the agencies with jurisdiction indicates that not months, but years will be consumed in pursuing these new permits and entitlements. This clearly would result in schedule delays in violation of Section 6 of the MOU. While Gambol's July 13, 2010 schedule depicts a permitting process for Version 4.2 with a timetable consistent with MCDP scheduling, this is inconsistent with reality.

By way of background, the MCDP possesses permitting under both CEQA and the federal National Environmental Policy Act ("NEPA"). Since project inception, the Harbor Department has addressed CEQA processes, while USACE addressed NEPA processes. Substituting Version 4.2 for the rock dike CDF would trigger the need for both CEQA and NEPA analyses.

The Harbor Department has tentatively decided to handle its CEQA analysis of the substitution through an addendum to the FSEIS/FSEIR, pursuant to Section 15164 of the CEQA guidelines, and has partially drafted that document. After receipt of all requisite information, if a decision is made to pursue an addendum, the addendum process would not require public circulation, and would take approximately 7-10 days to complete.

²⁰ The full portfolio of permits and entitlements necessary to effect the substitution of Version 4.2 for the rock dike CDF includes: (a) issuance of a CEQA entitlement by the Harbor Department; (b) issuance of a NEPA entitlement by USACE; (c) approval of an amendment of the Port Master Plan by the Coastal Commission; (d) issuance by the Regional Water Quality Control Board of a permit under Section 401 of the California Clean Water Act; (e) issuance by USACE of a permit under Section 404 of the federal Clean Water Act; and (f) a consistency determination issued by the Coastal Commission.

DATE: JULY 26, 2010

PAGE 12 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

Regarding the necessary NEPA analysis, USACE has repeatedly advised Gambol and the Harbor Department, most recently on July 23, 2010,²¹ that it would need to account for the substitution through a supplemental EIS, which likely would need to assess both the new CDF structure, and the operation of a shipyard at the Southwest Marine site.²² USACE, which has not started its NEPA process, estimated that this process could take between 24 and 36 months to complete.²³ Gambol has attempted to convince USACE legal and regulatory staff to implement a "supplemental analysis" (in Gambol's view, a rough analog to a CEQA addendum that would not require public circulation) instead of a supplemental EIS to comply with NEPA. USACE has not indicated agreement with Gambol's request regarding a "supplemental analysis."

After completion of both the CEQA and NEPA processes (and not earlier), the remaining necessary permits and entitlements for the substitution could then be processed and issued by the applicable resource agencies. These permits and entitlements are: approval of an amendment of the Port Master Plan by the Coastal Commission; issuance of a permit under Section 401 of the California Clean Water Act by the Regional Water Quality Control Board; issuance of a permit under Section 404 of the federal Clean Water Act by USACE; and a consistency determination submitted by USACE and approved by the Coastal Commission. As to the Port Master Plan amendment and the consistency determination, Coastal Commission staff advises in Transmittals 13 and 14 that it would not recommend approval of either of these entitlements at this time, in view of the present unknowns regarding the viability of the steel wall CDF.²⁴

²¹ A copy of the July 23, 2010 letter from Lawrence N. Minch, USACE District Counsel, to counsels for the Harbor Department and Gambol, is attached hereto as Transmittal 15.

²² It bears noting that Gambol's July 13, 2010 schedule completely omits reference to any CEQA or NEPA process. How Gambol could overlook this critical matter is unknown. Gambol has attended numerous meetings with the Harbor Department and USACE (most of which were arranged on Gambol's behalf) to discuss the CEQA and NEPA processes related to Version 4.2, and has debated the issues related to those processes at length. For instance, attached as Transmittal 16 is a copy of a June 24, 2010 letter from Gambol's counsel to counsels for the Harbor Department and USACE regarding the CEQA and NEPA processing of Version 4.2 and the MHRP.

²³ Staff believes this estimate could be conservative. NEPA assessment of a shipyard use at the Southwest Marine site, if based on a baseline of zero, which is a possibility given the inactivity at the site over the past several years, will require a significant amount of analysis.

²⁴ While Gambol has provided a draft of a Port Master Plan amendment to the Harbor Department, its failure to this point to resolve the open questions regarding the steel wall CDF's viability, discussed above and in Transmittals 13 and 14 from Coastal Commission staff, have prevented processing of that document.

DATE: JULY 26, 2010

PAGE 13 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

**c. Conclusions Regarding the Overall Impact of the
Proposed Substitution on the MCDP Schedule.**

The detailed discussion of scheduling above²⁵ provides a substantial amount of data. This subsection seeks to organize that data and to apply it to two scenarios for purposes of illustrating the basis of staff's conclusions on schedule-related issues generally, and, more specifically, on the impacts substituting Version 4.2 for the rock dike CDF inflicts on the MCDP schedule. To do so, this subsection assumes that the CDF at the Southwest Marine site will need to accept dredge material no later than October 1, 2011, which is consistent with the MCDP schedule provided by USACE.

First, Gambol's July 13, 2010 schedule is totally bereft of merit and should be disregarded. Its identification of certain processes that have not yet started, as being completed (e.g., test-pile program), and its total omission of CEQA and NEPA analysis, two clearly-required components of the entitlement process, drain that document of any credibility.

Second, if one assumes that Gambol starts the final design process for Version 4.2 on July 28, 2010 (the date of the Board meeting), and from that date (a) plots forward the tasks necessary to construct Version 4.2 (completion of geotechnical and design work for Version 4.2, USACE's negotiation of the contract modification to substitute Version 4.2 for the rock dike CDF, procurement and delivery of materials to construct Version 4.2, and actual construction) according to the durations listed on Gambol's own schedule, and (b) completely omits CEQA and NEPA permitting from the analysis, Version 4.2 still would not be able to accept dredge material by October 1, 2011. Rather, Version 4.2 would accept that material in mid-January of 2012.²⁶ What is telling from this scenario is that it assumes much quicker CEQA and NEPA processing than what Gambol currently requests from the Harbor Department and USACE (no CEQA or NEPA processing, versus CEQA addendum and NEPA "supplemental analysis"), and still results in a material delay in the MCDP schedule.

Third, if one assumes that Gambol starts the final design process for Version 4.2 on July 28, 2010, and plots forward the same four tasks noted above, using the durations from Gambol's own schedule, and adds CEQA and NEPA permitting to the analysis (including USACE's advice that the NEPA process for Version 4.2 could take

²⁵ Gambol estimates that construction of Version 4.2 will take 100 days. The Harbor Department, based on input provided by AECOM, and USACE's contractor, Manson Construction Co., estimates that Version 4.2 would take 168 working (not calendar) days to construct.

²⁶ See the Version 4.2 Schedule Analysis attached hereto as Transmittal 17.

DATE: JULY 26, 2010

PAGE 14 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

on the order of 24 months), Version 4.2 of the CDF would not be able to accept dredge material until August of 2013. This scenario, in staff's view, represents reality, but provides Gambol with substantial benefits of the doubt, in that it includes a permitting and entitlement process, but limits its duration to 24 months, which would assume that each and every of the entitlements necessary to build Version 4.2 could be obtained in the time USACE estimates the NEPA process alone would take. Under such a scenario, the Harbor Department believes that the end date of the entire MCDP, currently identified as December 1, 2012 (not including scheduled-contemplated delays for weather), would be extended by a minimum of 16 months to April of 2014.²⁷

This analysis and these scenarios demonstrate that Gambol's proposal to substitute Version 4.2 for the rock dike CDF delays the MCDP, in material violation of Section 6 of the MOU. Such delay would inflict material and actual damage to the Harbor Department and its tenants. For one thing, it would prevent the Harbor Department from timely delivering 18 acres of backlands to China Shipping pursuant to its lease document. China Shipping's lease document requires the Harbor Department to deliver 18 acres of backland currently covered by a surcharge, which would be removed and disposed of as part of the MCDP. For another, it would potentially jeopardize the Harbor Department's ability to timely deliver five new acres of backland to TraPac as required by its lease document. These five acres are intended to allow TraPac to fully utilize the Berth 136 area by providing the area necessary to operate the berth in a safe and efficient manner. Finally, it would prejudice ongoing discussions with YTI regarding the expansion of its terminal, a project that would involve modernization of its wharf for the purpose of more efficiently berthing and handling larger, modern container vessels.

2. Substituting Version 4.2 for the Rock Dike CDF Would Increase the Cost of the MCDP.

Staff estimates that Version 4.2 will cost at least \$5.5 million more to build than the rock dike CDF.²⁸ As noted above, USACE and its contractor have agreed to contract documents for the final phase of the MCDP, so costs for the rock dike CDF --

²⁷ See the Version 4.2 Schedule Analysis attached hereto as Transmittal 18. The Panama Canal is slated to become operational for deep draft, post-Panamax vessels in approximately 2013. Timely completion of the MCDP is critical to the Harbor Department's ability to maintain its competitive position, especially in light of this upcoming new option for shippers and vessel owners. Additionally, inserting an assumed 24-month NEPA process results in "only" a 16-month delay because construction tasks on the MCDP may be pursued in parallel, rather than serially, in relation to the permitting process.

²⁸ Copies of cost estimates for Version 4.2, and for the rock dike CDF are collectively attached hereto as Transmittal 19.

DATE: JULY 26, 2010

PAGE 15 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

\$35,026,199 -- are certain and clear. The estimate for Version 4.2 -- \$40,577,113 -- is based in part upon unit prices and from these same contract documents. Staff has reviewed this estimate in detail with Gambol's engineering team.

Apart from direct construction-related costs, substitution of Version 4.2 triggers a variety of indirect costs not included in the \$5.5 million overage noted above.

First, in comparison to the rock dike CDF, Version 4.2 is a steel structure which would be deployed in a highly corrosive marine environment, with the expectation that it would contain contaminated sediments in perpetuity. To do so, this structure will require a robust inspection and maintenance regimen in order to maximize its effective life, which a rock dike CDF would not require. The necessary maintenance and repair work for Version 4.2 would include, at minimum, underwater inspections every two years to evaluate the structure for the integrity of the steel protective coatings and cathodic protection systems, and to assess damage resulting from vessel interaction. The aforementioned coatings and passive cathodic protection systems generally will require replacement every 20-25 years, if not sooner. A conservative estimate for the average annual cost to inspect and properly maintain this structure is on the order of \$175,000 per year,²⁹ \$5.25 million over 30 years.³⁰ Again, rock dike CDFs do not trigger such inspection and maintenance needs, and would trigger insignificant maintenance costs in comparison.

Second, because Version 4.2 is volume-constrained, the Harbor Department will lose the opportunity to dispose of dredge material from other maintenance or remediation projects. The most immediate need involves the sediments along the face of the wharf at Berth 240 which are known to be contaminated and are subject to the Remedial Action Order issued by the DTSC. Although the dredging and disposal of these sediments is not part of the FSEIS/FSEIR, if the sediments prove suitable for disposal in a CDF, available capacity in the rock dike CDF could facilitate a very economic remediation project. Implementing the steel wall CDF forfeits that opportunity and likely adds significant additional cost to this remediation and, potentially, other future projects that generate contaminated sediments, such as maintenance dredging.

²⁹ The \$175,000 per year figure was calculated assuming a 2% per-year maintenance cost assessed against the structural improvement capital cost (\$8 million), plus an estimated \$15,000 per year in underwater inspection (diver) costs.

³⁰ The extent and expense of maintenance and repair will increase over time. Thus, assuming a flat \$175,000 expense over all 30 years, of an assumed 30-year period, provides Gambol with a significant benefit of the doubt.

DATE: JULY 26, 2010

PAGE 16 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

Third, implementing Version 4.2 exposes the Harbor Department to losing an estimated \$447,000 in rental income for every month the Harbor Department cannot deliver the 18 acres of backland to China Shipping, as discussed above.³¹

Finally, extending the duration of the MCDP to accommodate substitution of the steel wall CDF adds to the construction costs, as the contractor's extended project overhead costs accrue by \$4,170 per calendar day. As noted above, substituting Version 4.2 for the rock dike CDF could delay the end date of the MCDP by 16 months. Such delay could result in extended overhead costs of over \$2 million.

b. Gambol Grossly Misstates Its Ability to Reuse and/or Refurbish Existing Infrastructure on the Southwest Marine Site for Use In Its Proposed Shipyard Operations.

Gambol's "Conceptual Project Description" (Transmittal 7) identifies the premises-related tasks it believes necessary to develop a state-of-the-art shipyard on the Southwest Marine site as follows:

- Refurbish eight of the 10 existing buildings³² on the Southwest Marine site to suit relevant codes and shipyard uses, and restore the exteriors of such buildings to their pre-1946 condition;
- Construct new concrete piers and wharves outlining the Berths 243-245 slips;
- Rebuild and relocate three or four of the six existing historically significant cranes, and the single non-historically significant crane on the Southwest Marine site to current safety and operational requirements, and construct new trackage for the cranes;

³¹ In 2009, pursuant to its lease, China Shipping paid the Harbor Department \$298,000 per acre. As such, in 2009, these 18 acres would have represented \$5,364,000 in rent revenue to the Harbor Department. Based on this information, each month of delay in delivering these 18 acres to China Shipping could cost the Harbor Department \$447,000 in lost rent revenue.

³² The Board should note that BAE Systems, not the Harbor Department, holds title to these buildings and the other improvements on the Southwest Marine site. Future development of the Southwest Marine site, whether for a shipyard or otherwise, will require acquisition of title to these improvements.

DATE: JULY 26, 2010

PAGE 17 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

- Grade and pave the entire Southwest Marine site, and construct new storm water drainage and treatment facilities, and perform environmental mitigation as necessary;
- Construct new site infrastructure and shipyard facilities, including new entry roads, a parking structure, new electrical substations, lighting, pier utilities and underwater structures necessary to operate drydocks; and
- Construct up to three new floating drydocks.

Gambol's "Proposed Business Plan" provides a general discussion of the work it believes necessary to accomplish each task, and provides an itemized breakdown of estimated costs, but has designated such information as confidential. Staff, with the assistance of its consultant, AECOM, has reviewed Gambol's analysis and has performed its own independent review of the various assertions made. That review indicates that Gambol has underestimated the site-related costs necessary to build its proposed shipyard by approximately \$60 million.³³

c. Gambol's Proposed Business Plan Fails to Prove the Viability of the Shipbuilding and Ship Repair Facility It Proposes to Develop at the Southwest Marine Site.

Gambol designated the majority of its business plan as confidential, preventing public disclosure and open discussion of many of its details, including its development budget and pro forma financial statements. Staff, with the assistance of outside financial consultants, has presented its evaluation and recommendations to the Board in a separate confidential memorandum. Staff's evaluation is summarized, without revealing the confidential elements of Gambol's business plan, as follows.

1. Ship Construction and Repair Is a Mature, Low Growth Industry Subject to Intense Competition.

Ship construction and repair is a mature, low growth industry. Total industry revenues grew just 3.6% per year since 2005 and are anticipated to grow at just 1.8% percent per year through 2015. Roughly 85% of industry revenue is attributable to new vessel construction and roughly 70% of that construction is attributable to Navy combatants, a market segment that suffered serious declines since the end of the Cold

³³ A copy of AECOM's July 21, 2010 report is attached hereto as Transmittal 20.

DATE: JULY 26, 2010

PAGE 18 OF 26

**SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009**

War. The construction of large commercial vessels is restricted to vessels that are protected by the Jones Act, which prohibits foreign-built vessels from trading between U.S. ports. Vessels that do not require such protection are constructed in foreign yards.

Only seven shipyards in the U.S. are capable of constructing large vessels: Avondale Industries in Louisiana; Bath Iron Works in Maine; Electric Boat in Connecticut; Ingalls Shipbuilding in Mississippi; Newport News Shipbuilding in Virginia; National Steel & Shipbuilding in California; and the Aker Philadelphia Shipyard in Pennsylvania. Competition has resulted in significant consolidation and rationalization of this segment. Six of the big seven shipyards are owned by just two companies, Northrop Grumman and General Dynamics. Rationalization in this segment is ongoing. Just this month, Northrop Grumman announced plans to close its Avondale shipyard in Louisiana and to consolidate operations at its yard in Mississippi, and that it is considering selling or spinning off its entire naval business.

The near term outlooks for National Steel & Shipbuilding and Aker Philadelphia, the leaders in commercial vessel construction, also are dire. In June of this year, National Steel & Shipbuilding announced the elimination of 560 California jobs. Aker Philadelphia Shipyard, which is completing construction of three product tankers this year, has no new orders and is predicting layoffs among its 1,000 workers.

In its recent annual report, Todd Pacific Shipyards, the largest shipyard operator in the Pacific Northwest described the competitive environment as follows:

Competition in the domestic ship repair and overhaul industry is intense. The reduced size of the Government's active duty fleet has resulted in a significant decline in the total amount of Government business available to private sector shipyards, creating excess shipyard capacity and acute price competition. We compete for commercial and Government work with a number of other shipyards in a severely cost conscious environment. Our competitors for repair, maintenance and overhaul work include non-union shipyards and shipyards with excess capacity. Our competitors for new construction work, in addition to West Coast competitors, include Gulf Coast and East Coast shipyards with lower wage structures, substantial financial resources or significant investments in productivity enhancing facilities. Competition for domestic construction

DATE: JULY 26, 2010

PAGE 19 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

and repair opportunities will continue to be intense as some of our larger competitors have more modern facilities, lower labor cost structures, or access to greater financial resources.

2. Gambol Predicts That It Will Capture A Significant Share Of The Market Which, In The Absence of Market Expansion, It Must Take From Its Competitors.

Neither Gambol nor the Harbor Department is able to quantify the West Coast ship construction and repair market in terms of dollar volume. However, several indicators reveal that Gambol believes it can capture a significant share of the market. For instance, Gambol proposes to provide 21% of all the vessel haul-out facilities in California, and 11% of the facilities on the entire West Coast. Gambol's proposal to employ between 1,000 and 1,250 workers puts its operation on a par with BAE Systems San Diego Ship Repair which employs about 1,100 people, and Todd Pacific Shipyard which employs 800. By way of comparison, Aker Philadelphia Shipyard, which delivered three 600-foot-long product tankers in 2009, only employs 656. As previously reported, in its last few years of operation, Southwest Marine employed fewer than 100. Al Larson Boat Shop, the Harbor Department's tenant, employs about 85.

The optimism shown by the employment figures is reflected in Gambol's anticipated share of new vessel construction and in its predicted revenues, the details of which cannot be revealed here. It is clear, however, that Gambol intends to become the dominant player on the U.S. West Coast.

In spite of these indicators, Gambol describes its business plan as extremely conservative. However, the business plan is based on an idealized or surrogate market, constructed from predictions of the number of vessels operating on the West Coast and assumptions about the frequency of those vessels' needed repairs and/or replacement (new construction). Gambol assumes it will capture a "conservative" percentage of the perceived opportunities and assigns a dollar value to the presumed repair or replacement to yield anticipated revenue. Applying conservative capture rates to an overly optimistic perception of the market still yields a very aggressive business plan. And, as previously reported, the Harbor Department questions Gambol's ability to penetrate the Pacific Northwest market. Even though Gambol predicts a low capture rate for non-local vessels, non-local vessels nonetheless comprise more than half of Gambol's anticipated business.

DATE: JULY 26, 2010

PAGE 20 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

3. It Is Not Clear How Gambol Intends To Take Business Away From Its Competitors.

Gambol does not predict any significant new demand in the ship construction and repair market, and therefore will have to take market share away from its competitors in a fiercely competitive environment. The business plan does not describe how Gambol will accomplish this, but rather identifies several generally intangible factors such as the length to beam ratio of Gambol's proposed dry docks, Southern California's favorable weather, and the scheduling flexibility provided by Gambol's numerous dry docks and vessel transfer system.

The competitor that will be most directly affected is the Al Larson Boat Shop, the Harbor Department's longest existing tenant. The Al Larson Boat Shop services vessels up to 260 feet in length with a floating dry dock and four marine railways. The Harbor Department is currently processing a development application from Al Larson Boat Shop which contemplates replacing its three small marine railways with a marine travel lift, and increasing its repair capacity. A very large percentage of the repair business anticipated in Gambol's business plan targets vessels that can be handled by the Al Larson Boat Shop. Gambol will be in direct competition.

4. Gambol Predicts Extraordinary Financial Returns In A Fiercely Competitive Environment.

The profitability and financial returns depicted on Gambol's pro forma financial statements are a) inconsistent with those of similarly sized yards for which data is available and b) not reflective of the competitiveness of the market and the fact Gambol will be attempting to capture market share from established businesses. As discussed above, Gambol has grossly underestimated the capital investment required in infrastructure, building rehabilitation and equipment, and is overestimating the profitability of the work. Gambol forecasts operating margins that are roughly triple those of Todd and Aker Philadelphia Shipyard. Absent a large labor cost differential or the implementation of some proprietary processes, neither of which is suggested, there is no support for Gambol's extraordinary returns.

DATE: JULY 26, 2010

PAGE 21 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

d. The Recommended Board Action Does Not Prevent the Harbor Department from Pursuing Disposal of Dredge Material Through POLB's Middle Harbor Project.

As noted above, if all of the MCDP dredge material currently destined for the Southwest Marine site can be disposed of in the MHRP in a manner consistent with the MCDP's schedule, the need to construct any CDF may disappear, potentially saving the Harbor Department millions of dollars. The Harbor Department is aggressively searching for ways to coordinate the schedules of the MCDP and the MHRP. With that said, the Board should note that substantial doubt and uncertainty presently exists as to whether the schedules for the MCDP and the MHRP facilitate one another, for three reasons.

First, notwithstanding the statement in POLB's May 26, 2010 solicitation that fill could commence in early 2011, the date when MHRP construction and fill actually will commence is uncertain. For one thing, POLB has not yet started the process to hire a construction contractor to build the MHRP. Using POLA's experience for similar projects as a baseline, this process could take 5-6 months to complete, if no delays (e.g., bid protests) occurred. For another, staff understands that POLB has not concluded lease negotiations with the tenants of the 65-acre fill that will be created through the MHRP. POLB staff indicates that ongoing business discussions with its tenants will affect the MHRP start date.

Second, even if POLB grants the Harbor Department's application, no guarantees exist as to whether POLB could accept all the dredge material currently destined for the Southwest Marine site immediately, or at one time.³⁴ Such dredge material consists of a mix of clean and contaminated material with varying structural qualities. POLB has advised that how it sequences MHRP fill tasks will depend on the relationship of the physical and chemical qualities of the dredge materials accepted to POLB's construction needs and flexibility at the particular time when dredge materials become available. If POLB grants the Harbor Department's application, POLB very well could have immediate ability to place some of the materials currently destined for the Southwest Marine site, and a much later ability to place other materials.

Third, disposal of the dredge material currently destined for the Southwest Marine site in the MHRP would change the MCDP sufficiently to require new permitting

³⁴ The application process is open to all interested parties. It is unknown at this point how many applications POLB has received, or the relative strength of the Harbor Department's applications in relation thereto.

DATE: JULY 26, 2010

PAGE 22 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

and entitlements. The Harbor Department has initiated a study of air impacts to assist in determining what level of CEQA analysis it might have to undertake. Critically, USACE advised on June 17, 2010 that a supplemental EIS would be required to account for the project change. While this NEPA process, in all likelihood, would not be as extensive as the NEPA analysis necessary to assess Version 4.2, it still will take many months, likely over a year, to complete once it is started.

MCDP construction has started. The same cannot be said about the MHRP. At this point, nobody knows when MHRP construction and fill will start, when POLB might grant the Harbor Department's application, or when (assuming the granting of the Harbor Department's application) POLB might accept the Harbor Department's dredge material for placement in the MHRP, or how much it might accept. Aside from these uncertainties, present information indicates that the necessary permitting and entitlement process will take months, if not years, to complete.

Because of the major uncertainties that presently exist as to whether the Harbor Department can take advantage of the MHRP at all, let alone in a timeframe that facilitates the MCDP, no basis exists for the Harbor Department to delay or stop the MCDP to pursue the MHRP at this time. Such delay or stoppage would come with no guarantees of a payoff. Indeed, the facts show that the MCDP presently is so far ahead of the MHRP that it is likely that the two projects' schedules never will intersect such that the MCDP can take advantage of the MHRP's disposal opportunity. With that said, after MCDP construction commences, staff will continue to aggressively pursue the MHRP and will take any opportunity it can to leverage that project. Given the certainty of future maintenance dredging projects and the need to find disposal sites for the resultant dredge material (especially in view of the closure of the Anchorage Road disposal site), any new disposal option that becomes available is a welcome development.

Finally the Board should note that the recommended action has no impact, deleterious or otherwise, on the Harbor Department's desire and ability to pursue the MHRP. The land use designation of the Southwest Marine site, and the existence or lack thereof of an exclusive relationship between Gambol and the Harbor Department are not linked whatsoever to the MHRP.

e. The Recommended Board Action Will Allow for Better Decision-Making about the Future Use of the Southwest Marine Site.

Clarity should exist about the consequences of the recommended Board action.

DATE: JULY 26, 2010

PAGE 23 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

First, the land use of the Southwest Marine site and any landfills created thereon through the MCDP would remain open and available for future designation as the Board sees fit. The current land use of the Southwest Marine site, pursuant to PMPA 24, is "other," which in essence constitutes a placeholder designation for land which has not undergone a full planning process.

The recommended Board action would allow the Harbor Department to further analyze and, if the Board deems it appropriate, to pursue entitlements for the redevelopment of Terminal Island, which, as presently conceived, relies heavily on using the Southwest Marine site as a relocation area. It also would allow the Board to consider other land use alternatives, and to hold a full, comprehensive and open consideration of the site's use in a manner consistent with the Charter, the Harbor Department's leasing policy, and the Harbor Department's role as a trustee under the Tidelands Trust.

The MOU required the Harbor Department, for one year, to communicate with Gambol, and Gambol alone, about the idea of developing one use -- a shipyard -- at the Southwest Marine site. While the recommended Board action will end the relationship of exclusivity with Gambol, it does not end the potential for analyzing the appropriateness of a shipyard use, or other uses, at that site.

For the many reasons discussed above, sufficient facts do not exist at this time for the Board to designate the Southwest Marine site for future use as a shipyard. And, the Harbor Department's long-term planning for the site in relation to a larger Terminal Island redevelopment, while promising, is still conceptual only. It is premature to designate the Southwest Marine site for any specific future land use at this time. The recommended Board action will allow for further analysis of the various land use options available, which ultimately will result in better decision-making.

4. CONCLUSION

The Harbor Department is defined by its infrastructure. With state-of-the-art infrastructure, it can be, and has been, many things to many people. Without it, it risks degrading a competitive position that has taken generations to develop, and forfeiting its status as one of the world's most successful ports and the wellspring of commercial activity and jobs that have made it the region's foremost economic engine.

DATE: JULY 26, 2010

PAGE 24 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

The MCDP and the Harbor Department's tentative long-term planning for the Southwest Marine site focus on improving POLA's infrastructure to grow its core business of moving cargo. This is not merely a parochial concern. The MCDP commenced as a result of federal legislation that found a national need for a deep enough Main Channel to accommodate future container vessels.

Through the MOU, Gambol received a one-year exclusive negotiating period in which to convince the Harbor Department to designate the Southwest Marine site for future use as a shipyard. While Gambol has devoted significant resources to this task, its proposed project violates material and fundamental provisions of the MOU, and fails to provide a convincing business case for developing a shipyard at the Southwest Marine site at this time. For this reason, and for the reasons discussed above and in the other files and records of this matter, staff recommends that the Board decline to designate the Southwest Marine site for future use as a shipyard, and decline to commence negotiations with Gambol for a lease of the Southwest Marine site for purposes of operating a shipyard.

ENVIRONMENTAL ASSESSMENT:

The proposed action is Board deliberation on the denial to designate the Southwest Marine site for future use as a shipyard at this time, and denial to commence negotiations with Gambol for a lease of the Southwest Marine site for purposes of operating a shipyard, pursuant to Section 2(g) of the MOU. As such, the Director of Environmental Management has determined that the proposed action is exempt from the requirements of CEQA under Article II, Section 2(j) of the Los Angeles City CEQA Guidelines.

FINANCIAL IMPACT:

There are several possible potential fiscal impacts to the Harbor Department that should be considered with the Gambol plan of business. One of the financial effects to the Harbor Department lies with the revenues that may be received under a lease. As the terms of a lease remain to be negotiated, the potential amount of lease rent would differ depending on whether the lease agreement was fixed or based on percentage of gross receipts. The range of potential receipts may vary widely, from a minimum rent if revenue projections fell short to a high level of gross receipts that would increase rent. In dollar terms, the rent receipts may possibly range from low to high six figures each year. However, it may be possible that a new shipyard might affect the rent receipts from existing tenants who are in similar businesses. If there is a dilutive effect, it will

DATE: JULY 26, 2010

PAGE 25 OF 26

**SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009**

reduce the percentage of gross obtained elsewhere, offsetting to an unknown extent, the positive impact of a new shipyard tenant. Overall, the potential additional revenues from a lease would be relatively minimal.

If a shipyard is viewed an option for the property, it is unclear whether the financial plan advanced by Gambol is the most efficient or effective plan as no competitive plans have been solicited. Regardless of the merits of the plan as a shipyard, comparing the projected financial results of the business plan put forth by Gambol against publicly available financial data for shipyards indicates that the data put forth is optimistic and aggressive.

ECONOMIC BENEFITS:

The recommended Board action, to decline to designate the Southwest Marine site for future use as a shipyard, would leave the land use of such site undetermined and open for future Board decision making. Because the actual uses to which the site will be devoted in the future are unknown, stating the economic benefits of the recommended Board action with any specificity, at this time, is premature. The likely economic benefits associated with the Gambol shipyard are also unknown, due to questions about the viability of the proposed facility.

CITY ATTORNEY:

The City Attorney has reviewed staff's recommendations in connection with the MOU, and provided advice thereon.

TRANSMITTALS:

1. MOU between the Harbor Department, Gambol Industries, Inc., and the Los Angeles Conservancy
2. Amendment of Solicitation/Modification of Contract Dated July 7, 2010
3. Harbor Department's March 2009 Denial of Gambol's Application Submitted in February 2009
4. Aerial Photo of Fish Harbor
5. POLB's Solicitation for Deposit of Dredge Material in its MHRP
6. Harbor Department's Four Applications to POLB for Deposit of Dredge Material in its MHRP
7. Gambol's January 22, 2010 "Conceptual Project Description"

DATE: JULY 26, 2010

PAGE 26 OF 26

SUBJECT: RESOLUTION NO. _____ - GAMBOL INDUSTRIES, INC.
MEMORANDUM OF UNDERSTANDING FOR EXCLUSIVE RIGHT TO
NEGOTIATE, DATED JUNE 29, 2009

TRANSMITTALS (Cont.):

8. Redacted Copy of Non-Confidential Portion of Gambol's "Proposed Business Plan" Submitted June 28, 2010
9. Drawing of Rock Dike CDF
10. Conceptual Drawing of Steel Wall CDF
11. Gambol's July 13, 2010 Schedule
12. Resource Agencies Identified in the "Resource Agency Coordination" Section of the FSEIS/FSEIR
13. April 8, 2010 Letter from Coastal Commission Staff to the Harbor Department
14. July 21, 2010 Letter from Coastal Commission Staff to the Harbor Department
15. July 23, 2010 Letter from Lawrence N. Minch, USACE District Counsel, to Counsels for the Harbor Department and Gambol
16. June 24, 2010 Letter from Gambol's Counsel to Counsels for Harbor Department and USACE re: CEQA and NEPA Processing of Version 4.2 and MHRP
17. Version 4.2 Schedule Analysis
18. Version 4.2 Schedule Analysis with NEPA
19. Cost Estimates for Version 4.2 and Rock Dike CDF
20. AECOM's July 21, 2010 Report


GERALDINE KNATZ, Ph.D.
Executive Director

SYO/dls
Author: S.Otera