



# MISSISSIPPI OFFICE OF THE STATE AUDITOR

PHIL BRYANT, AUDITOR

PERFORMANCE AUDIT DIVISION UPDATE

## *Bond Monitoring Program: Mississippi Beef Processors*

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In October 2000, an initial meeting was conducted by state officials to explore the feasibility of subsidizing the construction of a regional cattle slaughter facility to be located in Yalobusha County in north central Mississippi. More than four years and \$43 million later, the facility is still not fully operational and remains plagued by serious issues that are threatening to force the facility to shut down.

### **Background**

The project was initiated both to help make Mississippi beef producers more competitive and to create over 400 new jobs. A series of closures of federally inspected cattle slaughter plants over the past decade has made the only reasonable options for producers the facilities located in Georgia and Texas.

Beef processing plants must operate as efficiently as possible to achieve a profit in an industry where profit margins are thin. Under these highly competitive market conditions, utilization of industry experts by state boards such as Land, Water and Timber at the outset of projects like this one has shown itself to be absolutely essential to managing the risks involved. The more complicated the project, the greater the need for experts to advise the State in their consideration of approvals.

### **OSA Involvement**

The State Auditor began to examine the circumstances related to the project in 2003. In August 2003, the Office of the State Auditor (OSA) released a limited review of the Land, Water and Timber Resources Act in which it offered to begin monitoring LWT agricultural development projects including Mississippi Beef Processors. In September, the Board authorized expenditure of funds made available in House Bill 1596, 2003 Regular Session, to reimburse OSA's actual costs.

In the first of a series of bond monitoring on Mississippi Beef Processors issued in May, 2004, OSA noted the financial risks:

*It should be understood that state involvement in funding projects like MBP is not without certain risks. Price volatility in the cattle market means there are no guarantees that a project like this, no matter how well planned and managed, will necessarily result in a viable long-term activity. While perceived public benefits may justify the State subsidizing a large-scale processing facility to protect State beef supplies, these risks are real and must be fully understood and managed.*

*In an industry with a historically low profit margin, attention to issues such as product acquisition cost, market supply and demand, and pricing structure is critical to success. Small fluctuations in any or all of these factors could prove the difference between handsome profits and disastrous losses. Losses could result in loss of taxpayer support grant monies as well as State loan guarantees.*

In the past 12 months, OSA has made six announced and unannounced site visits, reviewed project records, and taken appropriate steps to keep decision makers and public agencies informed regarding the status of project activities. The State Auditor continues to monitor developments to assist in determining how best to protect the taxpayers' economic investments.

### **Project Overview**

A feasibility study, prepared by Mississippi State University in January 2001, estimated combined equipment and construction costs at \$21.7 million to develop a facility capable of processing 1,000 head of cattle per day. A minimum of \$6.8 million in additional operating capital, the study said, would also be required.

In July 2001, the Land, Water, and Timber Board approved a \$5 million grant to Mississippi Beef Processors, LLC. The grant was contingent upon the

grantee's securing the remaining financing. However, in April 2002, after a February legislative meeting at the State Capitol, a memorandum of understanding was signed between Mississippi Beef Processors (MBP); Mississippi Development Authority (MDA); Land, Water and Timber Resources Board (LWT), Community Bank; and Yalobusha County.

The agreement generally outlined the terms and conditions for a 100% state guarantee of a \$21 million loan. With this, the bank has a first lien guarantee of a \$6.5 million operating line of credit. The loan guaranty agreement and guaranty authorization, negotiated by McGlinchey Stafford, PLLC, was signed by Community Bank and MDA in May 2002. The \$6.5 million operating line of credit with Community Bank, including the owner's \$1.5 million cash tied to the loan, was closed in July, while the loan closing for the \$21 million in construction capital was closed in September, 2002.

In addition to costs associated with the development of the project facility, a number of related infrastructure improvements were undertaken with state and federal taxpayer dollars including a \$2.5 million Community Development Block Grant for wastewater treatment; a \$250,000 Small Municipalities Grant Program for a gas pipeline; and other federal infrastructure improvement funds for the industrial park where Mississippi Beef Processors is located.

Budget overruns led to additional requests for state financial assistance in February 2003 when a revised construction budget of \$29 million was submitted on behalf of MBP by owner, Richard Hall, Jr. Upon further study and against a backdrop of outstanding invoices from contractors and other creditors, the LWT Board turned to Facility Group, a consulting company specializing in this area, for a preliminary project audit.

In March, Facility Group indicated that the project could be finished with a budget of \$43 million, including a \$3.5 million project management fee. This led to the Legislature amending the statute to increase the guarantee amount from \$21 million to \$35 million. Facility Group was selected to help implement revised plans over MBP objections.

Project setbacks continued to occur. By December 2003, MDA notified Community Bank of potential material changes adverse to the financial viability of the project and stated that no additional MDA

controlled state funds would be provided until outside financing could be arranged. These funds were to be secured by the owner no later than February 1, 2004.

In February 2004, Community Bank notified MDA of the owner's outside financing and asked MDA if the agency complied with the Bank position on the financing. In order to keep the project on time, MDA agreed to this financing source and agreed to allow additional payments to be made.

Budget overruns continued, leading Hall, in May 2004, to request an additional \$1.5 million loan for operating expenses. This application was denied by the LWT Board. However, in September an agreement was reached to allow for the release of \$1.5 million of collateral held by the bank. The State contends that MBP understood this to be the final assistance available from the State and the owner would be responsible for all other operational costs.

In early November, after a series of meetings regarding change orders and other cost overruns totaling at least \$2 million in unpaid work, the State Auditor received a request from the owners requesting an additional \$5.25 million to be used for operating expense related to cattle purchases.

### **State Funding Commitments for Mississippi Beef Processors' Facility**

Source of State Funds	Amount
Land, Water, & Timber Grant	\$5,000,000
Land, Water, & Timber Project Management Contract	\$3,547,974
State-Guaranteed Bank Loan	\$35,000,000
<b>Total State Commitments for Facility</b>	<b>\$43,547,974</b>

The table shows total state obligations for the construction of the facility. Additional state and federal funds have been utilized for infrastructure improvements to the industrial park where Mississippi Beef Processors, LLC, is located.