

BEFORE THE METRO COUNCIL

FOR THE PURPOSE OF CONSIDERING)
A REQUEST BY SPECIALTY)
TRANSPORTATION SERVICES, INC.)
FOR CONSENT TO A CHANGE OF)
CONTROL AND OWNERSHIP)

RESOLUTION NO. 00-3020
Introduced by Mike Burton,
Executive Officer

WHEREAS, on March 27, 1989, Metro entered into a certain Waste Transport Services Agreement with Jack Gray Transport, Inc. ("Gray") for the transportation of mixed solid waste from the Metro Central and Metro South Transfer Stations to the Oregon Waste Systems, Inc. disposal site in Arlington, Oregon; and

WHEREAS, in 1998 Metro adopted Resolution 98-2590B, thereby approving assignment of that Agreement from Gray to Specialty Transportation Services, Inc. ("STS"), a subsidiary of Asche Transportation Services, Inc. ("Asche"); and

WHEREAS, on June 15, 2000, STS requested Metro's approval of a second change of ownership and control from Asche to Churchill Environmental & Industrial Equity Partners, L.P. ("Churchill"); and

WHEREAS, pursuant to Change Order Nos. 21 and 23 to the Waste Transport Services Agreement, the consent of Metro is required for a change of control or change of ownership; and

WHEREAS, Metro's Regional Environmental Management Department Staff and its consultants have reviewed the stated criteria for approval of the request; have analyzed various correspondence, agreements, and financial reports; and have prepared findings; and

WHEREAS, Metro's Regional Environmental Management Department Staff, based upon such findings, has recommended approval of the change of control and of ownership

of STS to Churchill, subject to certain conditions as set forth in the accompanying Staff Report;
and

WHEREAS, It may be necessary to amend the Waste Transport Services Agreement to provide for the proposed change of control and change of ownership, and to make other necessary modifications; and

WHEREAS, This resolution was submitted to the Executive Officer for consideration and was forwarded to the Metro Council for its approval; now therefore

BE IT RESOLVED, THAT

1. The Metro Council hereby consents to and approves of the change of control and change of ownership of STS to Churchill, *provided* the following conditions are met:

a. That Churchill execute a form of Guarantee, as approved by the Metro General Counsel, which guarantees both the full and prompt performance by STS of all of the obligations of STS under the Waste Transport Services Agreement and also guarantees payment to Metro of actual damages which Metro may incur as the result of any default by STS;
and

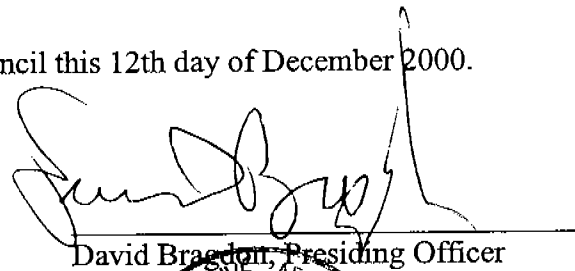
b. That Churchill and STS enter into appropriate financial agreements with any and all financial lenders of STS by which such lenders expressly recognize Metro's right and priority, in the event of any default by STS resulting in termination of the Solid Waste Transport Agreement, to assume control of all equipment used by STS in the performance of its contractual obligations to Metro for a period of one year following any default by STS and subsequent termination; and

c. That Churchill and STS agree to amendments to the Solid Waste Transport Services Agreement clarifying terms in the contract and further requiring STS to strictly comply with specified financial reporting provisions designed to enable Metro to monitor more closely the financial condition of STS; and

d. That Churchill exercises all options which it may possess to acquire stock ownership of STS.

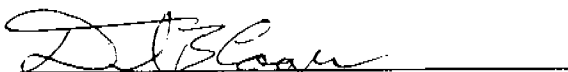
2. The Metro Council authorizes the Executive Officer, within 30 days after the date of this Resolution, to execute on behalf of Metro a form of Waste Transportation Services Agreement Change Order incorporating all conditions set forth herein and such additional terms consistent with this Resolution as may be deemed suitable and appropriate by the Metro General Counsel.

ADOPTED by the Metro Council this 12th day of December 2000.



David Braedon, Presiding Officer

Approved as to Form:


Daniel B. Cooper, General Counsel

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REGIONAL ENVIRONMENTAL MANAGEMENT COMMITTEE REPORT

CONSIDERATION OF RESOLUTION NO. 00-3020, FOR THE PURPOSE OF CONSIDERING A REQUEST BY SPECIALTY TRANSPORTATION SERVICES, INC., FOR CONSENT TO A CHANGE OF CONTROL AND OWNERSHIP

Date: December 11, 2000

Presented by: Councilor McLain

Committee Recommendation: At its December 6 meeting, the Committee considered Resolution No. 00-3020 and voted unanimously to send the resolution to the Council for adoption. Voting in favor: Councilors McLain and Park and Chair Washington.

Background: Specialty Transportation Services, Inc., (STS) currently has a 20-year contract with Metro under which it provides transportation services for solid waste sent from the two Metro transfer stations to the Columbia Ridge landfill near Arlington. The contract expires in 2009. Under the terms of the contract, STS must obtain Metro's consent to any change in majority control or ownership of the company. Failure to gain such consent would place the company in default on the contract. The contract provides that Metro either approve or disapprove the proposed change within 90 days and that any approval shall not be unreasonably withheld.

The proposed change of ownership addressed by Resolution 00-3020 is the second change of ownership request during the past three years. The first ownership change occurred in 1997 when the original contractor (Jack Gray Transport) was purchased by Asche Transportation Services. STS was created as a subsidiary of Asche and was assigned the management of the Metro contract.

Last spring, reports were published that alleged financial irregularities by high ranking corporate officials at Asche. As a result, Metro requested certain financial data and hired an outside consultant to review the financial condition of both Asche and STS and determine if it might have any impact on the company's ability to perform its Metro contract. On June 15, Metro was notified that Churchill Environmental and Industrial Equity Partners (Churchill) had been given the right to assume 85% control of STS for providing a \$7 loan to the company. STS agreed to a 90-day extension to give Metro additional time to review the change of control request. This extension expires on December 14, 2000.

The REM staff report for the proposed resolution has concluded "their (STS) financial condition has not improved" and that "STS still faces significant financial difficulty and may not be able to continue to provide services under the Waste Transport Contract."

Committee Discussion: Terry Petersen, REM Director, originally presented the staff report at a special November 28 REM Committee meeting. He explained that the purpose of the proposed resolution was to approve the request for a change of control and ownership subject to four conditions being met within 30 days after the passage of the resolution. The four conditions are: 1) execution of a corporate guarantee by Churchill that would guarantee full and prompt performance of the contract and payment to Metro for actual damages resulting from any default, 2) increasing Metro's access to all equipment used by STS in performing the contract from the current 180 days to one year following any default, 3) compliance with specified

financial reporting requirement to enable Metro to monitor the financial condition of STS, and 4) that Churchill exercise all options for acquiring stock ownership in STS.

Marv Fjordbeck, Senior Assistant Legal Counsel, explained the timeline for addressing the change of control and ownership request. He noted that, if the resolution were adopted, Churchill and STS would have 30 days (mid-January) to comply with the conditions. If the conditions were not met, the Executive Officer would be authorized to send a notice of default letter, which would give Churchill/STS 30 days (mid-February) to cure the default. If the default were not cured, the Executive Officer would then send a termination letter. The company would then likely exercise its right to binding arbitration, which could take up to 9-12 months to complete.

At both the November 28 and December 6 meetings, Mr. Peterson reviewed the need for each of the conditions proposed in the resolution.

Corporate guarantee. Petersen explained that Metro currently has a corporate guarantee from Asche and a letter of credit from Mellon Bank that will decline to a minimum value of \$1.3 million by September 2001. Metro is requesting a guarantee from Churchill because the current financial condition of Asche may significantly reduce or eliminate the financial value of any guarantee provided by the company. He indicated that, while Churchill has been willing to give verbal assurances that it would guarantee performance of the contract, the company has not been willing to commit these assurances to writing. He said that the major stumbling block was a provision in Churchill's partnership agreement that limits the amount of money that can be invested in a single company. Under this limitation, only \$6.6 million in additional funds can be invested in STS.

Councilor interest focused on the need to insure that the corporate guarantees in place following the change of ownership must be at least equal to those that are currently in place.

At the December 6 meeting, representatives from Churchill and STS testified that they were prepared to meet the conditions set forth in the resolution within the 30-day timeline. With regard to the need for a corporate guarantee, they noted they had been reluctant to make such a guarantee while they were still addressing the future financial relationship between Churchill and Asche and STS. They indicated that most of these issues have now been resolved and that they believe that an acceptable corporate guarantee can be developed within the timeline set in the proposed resolution.

Equipment Access. The need for Metro to access the STS equipment used to fulfill the contract in the event of a default is based on the assumption that Metro would not be able to contract for or procure replacement equipment for a period of time. The current contract provides for access for up to 180 days. Metro is seeking to extend this right of access to one year. Petersen testified that the intent of this provision has been to insure that the garbage would keep moving to the Arlington landfill until Metro could replace STS with a new transportation vendor. He indicated that such a process would likely be completed within the current 180-day timeline but that the requested one-year access requirement would insure that a new vendor could be selected and ready to replace STS before Metro relinquished access to the STS equipment.

Councilors asked Petersen to explain Metro's contingency plan should STS default on the contract with little or no notice. He responded that staff has been negotiating with several vendors that would be capable of responding within 24-48 hours. He indicated that Metro would use one or more of these vendors in the event of default. He assured the committee members that solid waste would not back up at the transfer stations.

Representatives from Churchill/STS indicated that they could accept this proposed extension of the access requirement.

Additional Financial Data and Monitoring. Representatives from Churchill/STS indicated that they had been unable to agree to the proposed requirement for additional financial data and monitoring because they were still sorting out the financial relationship between Churchill, Asche and STS. They testified that these relationships are now better defined and therefore they felt that language on these issues could be worked out in a way that would satisfy Metro's concerns.

Exercise of Stock Options By Churchill. Representative from Churchill/STS indicated that negotiations to exercise these options were already occurring and that they should be completed, and the options exercised in a manner that met the condition outlined in the proposed ordinance.

STAFF REPORT

FOR THE PURPOSE OF CONSIDERING A REQUEST BY SPECIALTY TRANSPORTATION SERVICES, INC., FOR CONSENT TO A CHANGE OF CONTROL AND OWNERSHIP

Date: November 30, 2000

Presented by: Terry Petersen

PROPOSED ACTION

Adoption of Resolution No. 00-3020 granting Metro approval of the change of ownership of Specialty Transportation Services, Inc. (STS), from Asche Transportation Services, Inc. (Asche), to Churchill Environmental & Industrial Equity Partners, L.P. (Churchill), with conditions. The resolution is in response to a request from STS for the approval.

EXISTING LAW

The Contract for Waste Transport Services, as amended by Change Orders No. 21 and No. 23, states that: "The Metro Council shall, within ninety (90) days of receipt of a written request to enter into the transaction, either approve or disapprove the request, provided that any approval shall not be unreasonably withheld."

FACTUAL BACKGROUND

In 1989, Metro entered into a 20-year agreement (Waste Transport Services) with Jack Gray Transport Inc., to transport waste from Metro's transfer stations to the Columbia Ridge Landfill located in Gilliam County, Oregon. Approximately 700,000 tons of waste were transported under the Waste Transport Services agreement in 1999.

In 1997, the firm requested assignment of the contract to STS, a subsidiary of Asche Transportation Services, Inc. Metro approved the requested assignment in January 1998 per Resolution No. 98-2590B. The resolution authorized execution of Change Order No. 23 to contract. In addition to authorizing assignment of the contract, the change order also provided Metro with additional protections. These included doubling the amount of time Metro could operate the contractor's equipment in the event of a default, and improvements in the default provisions of the contract.

In May 1999, Metro approved Change Order No. 24 to the Waste Transport Services agreement. The change order was initiated by STS to assist in remedying financial problems the firm was experiencing. Metro in turn was interested in obtaining long term financial savings and operational changes at its Metro South transfer station.

The negotiated change order made a number of changes to the agreement involving payments, operations and protections to Metro. Payment provisions were modified to prepay fixed costs due STS over the remainder of the contract (\$6.6 million) in exchange for lower per load costs and the elimination of payments for shuttling transfer trailers to the compactors at Metro South. Operations were modified by reducing the area for storage of transfer trailers at Metro South in order to facilitate the construction of a public unloading area desired by Metro. Protection provisions were

modified to release retainage held by Metro in exchange for a letter of credit (\$4.1 million) and a corporate guarantee from the parent company. The value of the letter of credit declines by \$100,000 per month, to a final level of \$1.3 million (as of November 16, it is valued at \$2.3 million). The net savings to Metro due to these changes are approximately \$9 million over the life of the contract.

After approval of Change Order No. 24, STS and their parent, Asche, continued to restructure their finances through a substantial recapitalization of the company. Churchill acquired a significant interest in Asche with an investment of \$12 million in September 1999. This followed an equity investment of about \$3 million by a private investor in the summer of 1999. Unfortunately, even with these additional capital investments STS and Asche continued to have financial difficulties. In the spring of this year, Asche announced that they were terminating the employment of its CEO and other officers due to alleged financial irregularities. Press releases from the company as well as news stories related to the company indicated that Asche was suffering from serious cash flow problems.

Metro staff requested financial information from STS and its parent after seeing these reports. Based on its review of the data, Metro Staff determined that the financial condition of STS was such that it called into question their ability to continue to perform their obligations under Metro's Contract for Waste Transport Services. Metro retained a consultant with experience in dealing with financially troubled companies to provide advice on the impact STS' financial condition may have on their ability to perform under the contract and to advise Metro on actions it should take to ensure continued service.

As part of a plan to alleviate their financial problems, STS obtained a loan of \$7 million from Churchill in July 2000. The terms of this loan give Churchill the right to obtain up to 85% of the stock in STS and 53% of the stock of Asche. On June 15, 2000, Metro received a letter from STS requesting Metro's consent for a change in control of the Waste Transport Services agreement from STS to Churchill Environmental & Industrial Equity Partners, L.P. Such consent is required under the agreement.

STS agreed to give Metro an additional 90 days, until December 14, 2000, to review their request for approval of this change of ownership. Metro has used this time to evaluate the impact of this change of ownership on the financial condition of STS and therefore, STS' ability to adequately perform their contract obligations. Metro obtained additional financial data including Asche's plan for addressing its financial problems as well as those of STS. Financial data provided by STS was reviewed to determine the impact of the Churchill investment on STS' financial performance.

Unfortunately, their financial condition has not improved as was anticipated in the financial plan provided by STS management. Fuel prices have remained at very high levels and have significantly impaired STS' ability to improve their financial condition. Even with the infusion of cash from Churchill, STS still faces significant financial difficulty and may not be able to continue to provide services under the Waste Transport Contract.

Analysis

Change Order No. 21 to Waste Transport Services agreement requires that "any change in control or the transfer of a controlling interest in stock ownership of Contractor shall require the prior written consent of Metro." The Change Order also requires that "Contractor shall give Metro a written request to approve the change in control prior to any change in control taking effect. If a change in

control occurs without prior written notice to Metro, such change shall constitute a material breach of the contract and Metro, in its sole discretion, may terminate this contract for such breach.”

In determining whether to approve or disapprove a request by the Contractor to sell the company, Metro may consider the following criteria, according to Change Order No. 21:

- (1) Whether the proposed purchaser is of sufficient size to perform the obligations required in the agreement.
- (2) Whether the proposed purchaser has sufficient financial resources to fill the operational and financial guarantees specified in the agreement.
- (3) Whether the proposed purchaser has sufficient favorable experience providing services similar to those required in the agreement.
- (4) The nature of any other commitments which the proposed purchaser may have in related solid waste disposal services either nationally or within the Metro service area.

Under the contract, Metro has 90 days to either approve or disapprove of a request for a change of ownership. As noted above, STS agreed to an extension of time so that Metro could more fully review the impact of this change in ownership. Metro had John G. Wiencken, a local business consultant, review information provided by STS and Churchill to determine Churchill’s suitability as an owner under the criteria noted above. The following is a summary of the analysis performed by Mr. Wiencken:

Churchill Environmental & Equity Partners, L.P.

The Churchill Environmental and Equity Partners, L.P. is one of a number of investment partnerships formed by Churchill Capital, Inc. This firm was founded in 1989 by two former bankers for investing funds raised from various institutions, investors and investor groups. In the aggregate, all six of the Churchill funds have raised over \$900 million that has been invested in a variety of businesses. Churchill Environmental & Equity Partners has obtained commitments for various investors totaling \$128 million. Data provided by Churchill indicates that approximately \$71 million of the partnerships commitments have been invested in four different firms, including a total investment of \$19 million in Asche and STS.

- (1) *Is the proposed purchaser of sufficient size to perform the obligations required in the Waste Transport Services Agreement?*

Churchill Environmental & Equity Partners, L.P. (Churchill) is an investment fund and does not have either the employees or the equipment to perform the obligations of the contractor under the Waste Transport Services Agreement. If they acquire STS, they will own the company with the assets that have provided these services for the last 10 years. Therefore, if they complete the purchase of STS they will be the owners of an asset with the capability to perform the obligations.

- (2) *Does the proposed purchaser have sufficient financial resources to fulfill the operational and financial guarantees specified in the agreement?*

Churchill is an investment fund with total resources of \$128 million. It is clear that they have total financial resources sufficient to fill the operational and financial guarantees specified in the contract. However, the terms of the partnership agreement the fund operates under limits the total amount of money that may be invested in any single company. Churchill has indicated that the maximum they can invest in Asche and STS is \$25.6 million. They have already invested \$19 million in these firms. Metro's consultant questions whether the additional \$6.6 million is sufficient to ensure the continued operation of STS unless current operating conditions improve at STS. Churchill has also indicated that they have "established relationships with other private equity firms as well as investment banking firms that may also be used to provide capital" to portfolio companies.

- (3) *Does the proposed purchaser have sufficient favorable experience providing services similar to those required in the agreement?*

Churchill itself has no experience in providing services similar to those required in the agreement. The operational experience needed to provide these services will be provided by the management and staff of STS. Mr. John Quirk and Ms. Melissa White, two principals of Churchill, serve on the board of STS. They have experience in financing of businesses in the waste industry and they strengthen the firm in that area. STS recently hired Mr. Jim Dancy as Chief Operating Officer. Mr. Dancy brings over 30 years of experience in the waste management industry to STS. The current management team at STS has been responsible for the delivery of these services for the last 10 years; therefore, one can conclude that after Churchill acquires STS, they will have sufficient favorable experience.

- (4) *The nature of any other commitments which the proposed purchaser may have in related solid waste disposal services either nationally or within the Metro service area.*

Churchill has a 76.2% ownership interest in Horizon Waste Services, a solid waste company headquartered in Aliso Viejo, California. Horizon has collection and disposal operations in Hawaii, Arizona and Southern California. At its current level of business, Horizon is expected to generate annual revenues of \$60 million.

This analysis is not based on whether the current owner, Asche Transportation Services, Inc., or the proposed owner, Churchill Environmental & Industrial Equity Partners, L.P., is a better owner. Instead, it is based on determining whether or not Churchill brings sufficient resources to STS to improve the likelihood of their continued performance of the Transport Contract. Metro staff has focused its efforts on obtaining assurances related to the following two concerns.

- (1) **STS Financial Problems** – STS has very serious financial problems that could lead to failure of the company and the risk of a sudden work stoppage. While the risk of a sudden failure to provide service is relatively small, the poor financial condition will require Metro to closely monitor their performance to help protect against a break in service.

- (2.) Potential Deterioration in Performance – While Metro has not observed any significant deterioration in either the level of service provided or in equipment maintenance, both could suffer if STS’ financial difficulties continue. Again, additional staff time will be required to monitor these factors.

Metro staff met with representatives of both STS and Churchill to discuss the change in ownership and its impact on the financial condition of STS. Based on these discussions and analyses provided by outside consultants, staff has determined that Churchill will have demonstrated that they meet the requirements for a new owner if the following conditions are met.

- (1.) Agreement by STS to a modification of the contract that:
 - a) Provides improved language with respect to defining “actual damages” under the contract;
 - b) Increases the period for access to the contractor’s equipment, in case of default, from 6 months to 12 months;
 - c) Includes stricter reporting requirements to enable Metro to better monitor the financial condition of the contractor.
- (2.) Agreement by Churchill to:
 - a) Provide a guarantee of STS’ performance under the contract in a form similar to the guarantee provided by Asche;
 - b) Exercise its option to convert the \$7 million loan made to STS into stock ownership.

The contract modifications required in the conditions on STS are designed to reduce the impacts in the event of a contract default, as well as provide better warning of any potential default. The conditions placed on Churchill are intended to provide Metro with a guarantee of STS’ performance by its owner and to improve STS’ financial condition.

After review of the data provided by STS and Churchill, Metro Staff has concluded that if the conditions noted above are met, Churchill meets the criteria outlined in the Waste Transport Contract for a new owner of STS:

- (1.) Churchill does not currently have sufficient size (employees and equipment) to perform the services required by the contract, but will possess these resources after the purchase of STS is complete. (Criterion #1).
- (2.) Churchill has sufficient financial resources to fill the operational and financial guarantees specified in the agreement. Provision of the guarantee noted above clearly demonstrates that they meet this requirement. (Criterion # 2).
- (3.) Churchill has sufficient favorable experience providing similar services (Criterion #3 and #4).

BUDGET IMPACT

Approval of the change in ownership has no budget impact.

EXECUTIVE OFFICER RECOMMENDATION

The Executive Officer recommends that the Metro Council approve the change of ownership of Specialty Transportation Services, Inc. (STS) from Asche Transportation Services, Inc. (Asche) to Churchill Environmental & Industrial Equity Partners, L.P. with the conditions specified in Resolution No. 00-3020.

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