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MINUTES OF THE RECONVENED MEETING OF THE JACKSON COUNTY BOARD OF COMMISSIONERS HELD ON JANUARY 19, 2005

The Jackson County Board of Commissioners met in a Reconvened Session on Wednesday, January 19, 2005, at 4:00 p.m. in Room A201, Justice & Administration Building, 401 Grindstaff Cove Road, Sylva, North Carolina.

Present: K. Stacy Buchanan, Chairman
Roberta Crawford, Vice Chair
Joe Cowan, Commissioner
Eddie Madden, Commissioner
Brian McMahan, Commissioner
Kenneth L. Westmoreland, County Manager
W. Paul Holt, Jr., County Attorney
Evelyn Baker, Clerk to Board

Chairman Buchanan called the meeting to order. Chairman Buchanan moved that the Board go into Closed Session pursuant to G.S. 143-318.11(a)(6) Personnel. Commissioner Crawford seconded the Motion. Motion carried.

Chairman Buchanan called the Open Session back to order and stated no action was taken in closed session. He stated he was pleased to report that the preliminary report from the auditor reflects no wrong doing on the part of any county employee.

Chairman Buchanan moved to suspend the rules and add Preliminary Audit Report by Mitch Crisp, CPA, to the agenda. Commissioner Crawford seconded the Motion. Motion carried.

PRELIMINARY AUDIT REPORT: Mitch Hughes of Dixon Hughes, PLLC, addressed the Board. His firm was requested to review the financial affairs of the Economic Development Commission of Jackson County. The auditors inspected records covering the past five to six years, reviewed transactions in and out of EDC's accounts, reviewed the status of approximately six outstanding revolving loans, and did some specific testing in regards to the county's advances to EDC during that time period. One of the concerns was if there was any kind of malfeasance within the accounts. The procedures he has performed thus far do not provide any evidence that there was. There may be concerns about the nature of the operations, the way the organization is organized and supervised, and the way decisions are reached, and the governance provisions. He did not find any evidence that any individual has personally benefited from any of the activities or transactions. He stated they do intend to proceed with resolving some outstanding questions and obtaining some pending information in a few areas and issuing a written report within the next two to three weeks. The report will reflect the exact procedures his firm performed and the exact findings. He anticipated that at that time his firm would be making recommendations regarding management of revolving loans, the management and activities and governance of the activities of the EDC.

JACKSON DEVELOPMENT CORPORATION: Mr. Crisp stated that in the late 1990's a direction was started by the EDC to actually acquire some industrial sites and properties. Some time before that the revolving loan activity had also begun an effort to attract an industrial developer in the area. As those activities became somewhat interwoven in the late 1990's and early 2000's, the EDC became more active as a financial transaction conductor during that time period as well. It actually purchased some property, activated a non-profit corporation that was formed to enter into leases and financial arrangements that were more difficult than a governmental entity could enter into. That non-profit's governing board was appointed originally by the EDC and there are some interlocking requirements that make them related parties, although it is a separate legal entity and is known as Jackson Development Corporation. Some of the earlier activities of Jackson Development Corporation were the acquisition of the former Buster Brown property on Wilkes-Crescent Dr., Sylva. It received that property from the Town of Sylva and Jackson County who had jointly purchased it from the previous owner. Also using borrowed funds, Jackson Development Corporation acquired the Drexel Plant and several acres surrounding it in Whittier. It also became involved at some point in selling the former Buster-Brown property to an industrial client and received a Note receivable. It also sold some real estate and received the cash proceeds. It made, on its own, a loan to more than one industrial client entities, and conducted business up to the current time managing those loans, borrowing money, buying and selling property and basically trying to facilitate industrial development. Those activities were interrelated with the EDC and while reviewing EDC activities, it led the auditors into that entity's transactions so that has been included in the review thus far and will be included in the final report. The Whittier property is under lease to an industrial client and there are some concerns regarding current payment of the lease arrangement, but it is still an occupied property. It also obtained the former Tuckaseigee Mills property in Sylva at a later date using a loan from EDC that was an accumulation of funds from prior activities, loans made and repaid, and grants funded from the county, towns and other grant sources during prior years. As of today there are several properties outstanding and several mortgages on those properties and most recently it has entered into support for a local industry in terms of providing financing for its accounts receivable. The EDC itself is not the holder of any real property; it has used Jackson Development Corporation to serve in that role. The EDC itself is not directly an obligator on any of the note obligations; it also used Jackson Development Corporation to be the entity signing the transactions in connection with those properties. The EDC has received, until the most recent year, an annual support contribution from the county, the towns, in addition to some grants from various sources on a sporadic basis. It has used those funds to provide some grants to industrial recipients and make enhancements to some of the properties, provided various studies and promotional activities in terms of development. The EDC is governed by a board of appointees who are volunteers. There is some concern on the part of the auditors because funding is from various sources, there is the lack of paid fulltime staff to really look after those affairs and there are better ways to organize and operate EDC. The auditors also have some concerns over the isolation of Jackson Development Corporation from the county and towns in terms of oversight of its activities.

He stated that the county had contributed in excess of $1.3 million to EDC. In addition, there are contributions to other entities who are somewhat related.

REVOLVING LOANS: Mr. Crisp stated they reviewed the files for the active loans and there are six identified outstanding loans which were reviewed and added a seventh to that list which is a loan from EDC itself to Jackson Development Corporation for the most recent real estate purchase. He gave a historical review of the outstanding revolving loans as follows:

(a) $225,000 loan which originated in 1997 to Clearwood, LLC. Paying monthly at a reduced payment amount modification as agreed upon. The current balance is $142,961.00. This loan is not considered in default.

(b) $218,000 loan which originated in 1999 to Southern Lumber Co. Paying monthly installments under negotiated extended repayment terms. The current balance is $177,169.00. This loan is considered current.

(c) $14,000 loan which originated in 2001 to Country Collections which is now out of business. The business principals which over time have been associated with that business all deny responsibility for the loan. The company has changed hands at least once. This loan is in default and is approximately $14,000.00, which was the original amount of the loan.

(d) $200,000 loan which originated in 2002 and modified in 2003 to a higher amount to Fraternal Composite Specialties. That total loan amount ended at $325,000. They are paying with a somewhat inconsistent payment record. The current balance is $314,965.00.

(e) $300,000 loan which originated in 2002 to Q. C. Apparel There have been several periods of non-payment. The current balance is $331,381.00. From the surface, this loan appears to be in default for both non-payment and failure to meet the employment commitment.

(f) $250,000 loan which originated in 2004 to Metrostat Communications and originated in November and they are currently paying as agreed.

(g) A seventh loan which the auditors added to the list is:
$568,000 loan which originated in 2002 from EDC funds to Jackson Development Corporation in connection of the purchase of the Tuckaseigee Mills Building. Additional documentation is needed to be exactly clear what the terms of that loan were and from what was observed it appeared to be for a one year period of time. If it was, then it has either been extended or renegotiated. He stated he has not seen the file on this loan. Mr. Crisp stated it was his impression at this point that EDC holds the first deed of trust, however, he has not seen the documents file.
Mr. Holt stated that he received a call from an attorney for Triple SSS, who has a second or third mortgage on the building indicating foreclosure.
Mr. Crisp stated Jackson Development Corporation's financial statements do record a liability to Triple SSS a partnership in connection with that acquisition, of approximately $250,000 outstanding, which would be in addition to the obligation to EDC.

Mr. Holt stated his preliminary investigation revealed that the property was purchased with basically 100% financing.
Mr. Crisp stated that he was working with sketchy information regarding that transaction at this point because it is one of the files he still needs to review.

Mr. Crisp was asked to describe the purpose of the revolving loan fund program. He responded that revolving loans have historically been to provide financing to entities that are valuable for job creation, economic development within the community, the impact thereon, and for whatever reason have difficulty obtaining investment capital through conventional sources. This leads into an area for naturally taking a higher than a normal risk loan into a business venture. Because of the nature of that, the loans must be managed at a higher than normal risk and typically most of these loans have additional provisions recognizing that, and they have additional collateral and very commonly provide additional personal guarantees. There is also an expectation that the revolving loan will be somewhat flexible because the community wants a business to succeed because the purpose of making the loan was to enhance the local economy. Pushing a business out of business does not accomplish that goal. Typically revolving loan funds are fairly generous in terms of re-negotiating terms, rates and payment amounts, in addition to granting brief periods of relief if necessary. The current activities in the revolving loan fund are not at all unusual in terms of the revolving loan fund involvement.

Mr. Crisp was asked to explain the situation with the accounts receivable line of credit with Q. C. Apparel. He stated that Q. C. Apparel is the most significant default loan. It is unclear as to how this developed, but several months ago Jackson Development Corporation, the non-profit corporation put into place by EDC, was approached or became involved in discussions with Q. C. Apparel and the end result of that discussion was that Jackson Development Corporation became what is referred to as a “factor”. This means that when Q. C. Apparel finishes an order and has an invoice ready to present to a customer, a “factor” steps in and pays Q. C. Apparel for that invoice immediately (usually at a discounted amount) and the “factor” collects the money from the customer who owes it to the manufacturer. This speeds up the whole cash flow process for the manufacturer. “Factoring” is a relatively risky business since it involves trying to collect another’s receivables, thus there are generous discounts on those purchases that reflects the risks. Jackson Development Corporation entered into a factoring agreement with a relatively small discount. It obtained a line of credit at a local bank to underwrite its purchase of those receivables, and for the past six months has been buying those invoices and collecting from Q. C. Apparel’s customers. As invoice payments came in, payments were being made to the bank. From the documents he has seen, there is an approximate $50,000 line of credit which is being used to purchase invoices from Q. C. Apparel. The auditors did not spend a lot of time analyzing the status of the outstanding invoices; there is a register, there has been payment activity, and there are some overdue under normal terms, but that doesn’t necessarily mean it is unusual in that industry. There is approximately $40,000 outstanding on the line of credit as of the most recent statement the auditors observed which was probably two or three weeks old. Jackson Development Corporation’s board made the decision to enter into that agreement with Q. C. Apparel, not the EDC.

Mr. Crisp was asked to explain, when he traced the history of Jackson Development Corporation, if it was formed with assets that came from the county, the municipalities, other governmental agencies, and EDC cash grants. He responded that he thought Jackson

Development Corporation was formed approximately in late 1998 and started with the original property transfers as best he could tell.

Mr. Crisp was asked what was his immediate recommendation would be, taking into consideration continuing with the audit, developing a written report that will be shared with the municipalities and those who are interlocked with the EDC, the Board of Commissioners temporary suspension of the county's participation with EDC or bringing those activities in-house or at least ascertain how county government conducts EDC operations, in addition to the revolving loan situation. Mr. Crisp responded that the auditors have not fully developed where they are going with this, but at this point, it certainly deserves stepping back and looking at the way the various ventures are organized and the way they are governed. The revolving loan fund has two distinct activities that are occurring and are not exactly complimentary and should probably be separated. The generation of the loan is for trying to attract a business that will add to the community. Structuring means providing a part of their capital structure. That is entirely different from when all that is in place and having someone who has the patience, talent and will to work with that business to keep them on track in terms of the repayment; knowing when to be firm or flexible and helping the business succeed. Those are probably two functions that need to be separated in the county's revolving loan fund to the extent it can. EDC is a joint venture among the governments in the county. The day to day management and structure needs to be reviewed and more oversight and fulltime management is needed over what is going on with that activity and tighten up the reins somehow, yet at the same time do it in such a manner that allows for the participation of all the members. It is fairly difficult to structure, but it needs to be reviewed collectively. The fiscal oversight needs to be tightened up. Quite frankly the controls were fairly loose and the oversight at present is less than desirable. Financial reporting did occur from time to time; however, it was not consistent. Things could have really, really gone wrong

Mr. Crisp was asked if what he was describing would not ordinarily fall under the prevue of the county's audit. He responded who's audit EDC should come under needs to be resolved. Mr. Crisp was asked that when the county has an annual audit conducted if the EDC operations are a part of it. He responded, no, not under any kind of general rules. The EDC venture among several different governments is a body on its own. Somewhere in its By-Laws it states that EDC should have an audit or given the opportunity to "piggy-back" onto one of the organizations audits. He doesn't think either was ever done. The EDC is a commission created by several governments and is outside the normal structure under which each is operating. It appears logical that the EDC audit should fall under the financial system of one of the participating governmental bodies and simply be part of a sponsoring government, but is not necessarily the only way to accomplish an audit.

Mr. Crisp was asked if he found any wrong doing on the part of any county employee. Mr. Crisp responded "no", but he did have some concerns about the day to day operations of the EDC, such as the how the system is organized, governed, and the oversight of the activities.

Mr. Crisp was asked to include in the written report his recommendations concerning the revolving loans.

Mr. Crisp was asked that since Jackson Development Corporation was a private non-profit, did the county have the right to audit its books. He responded that at this point that is a little unclear. He stated he looked at materials that were voluntarily given to him. The corporation holds a charter of a 501C6 tax exempt entity and under the tax code it is obligated to make certain records public. Chairman Buchanan stated that the current board of Jackson Development Corporation should understand and take serious what created it in terms of where the assets came from. Those assets came from taxpayers' monies and properties that originally belonged to taxpayers.

Mr. Crisp stated the audit should be complete and a written report should be available within three weeks, hopefully two. This issue will be placed on the February 8, 2005 Board of Commissioners Agenda.

Chairman Buchanan moved that the Board go into Closed Session pursuant to G. S. 143-318.11(a)(3) Legal and G. S. 143-318.11(a)(5) Real Property. Commissioner Madden seconded the Motion. Motion carried.

Chairman Buchanan called the Open Session back to order and report no action or votes were taken in Closed Session.

There being no further business, Commissioner Cowan moved that the meeting be adjourned. Commissioner Madden seconded the Motion. Motion carried by unanimous vote and the meeting adjourned at 6:35 p.m.

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Evelyn B. Baker, Clerk	K. Stacy Buchanan, Chairman