



City of Gainesville

Office of the City Auditor

Memorandum

To: Erik Bredfeldt, Economic Development and Innovation Director

Cc: Phillip Mann, Assistant City Manager
Lee R. Feldman, City Manager
Ginger Bigbie, City Auditor

From: Brecka Anderson, Assistant City Auditor

Date: February 4, 2021

Re: Phalanx Defense Systems, LLC, Documentation Review for Loan Forgiveness

Background

On September 12, 2016, Phalanx Defense Systems, LLC (Phalanx), owned and operated by James Coats, executed a mortgage and a promissory note with the City of Gainesville (City) for \$635,000 to purchase a property located at 1125 NE 8th Avenue in Gainesville. The Promissory Note provided certain terms whereby the City could forgive a portion of the loan up to \$535,000 of the \$635,000 owed to the City. The promissory note included opportunities for possible loan forgiveness provided that Phalanx invest in property improvements and create and retain new jobs satisfying established criteria. In February 2018, the City Commission approved the forgiveness of \$335,000 due to Phalanx's qualified actual expenditures for repair, remediation, and improvements (property improvements) to the subject property, resulting in a loan balance of \$300,000.

Both parties executed an Amended and Restated Promissory Note in April 2019 to reflect the portion of Phalanx's debt that was forgiven by the City for property improvements and reflecting Phalanx's remaining loan balance. The maximum total amount of the remaining \$300,000 loan balance eligible for forgiveness was established as \$200,000, if certain criteria are met.

In November 2020, Phalanx contacted City management to request loan forgiveness for the full \$300,000 loan balance. While the City Commission declined to forgive the entire \$300,000 loan balance on December 3, 2020, \$200,000 was determined to be eligible for loan forgiveness if Phalanx met the criteria in the Amended and Restated Promissory Note. The City Manager's Office is responsible for determining whether Phalanx documentation meets the criteria and requested that the City Auditor's Office independently review documentation submitted by Phalanx.

Objective

The City Auditor's Office agreed to provide an independent review of loan forgiveness documentation submitted by Phalanx and compare the documentation to the criteria for loan forgiveness as stated in the Amended and Restated Promissory Note, and Special Warranty Deed.

We did not perform a review of Phalanx operations or property improvements; therefore, we do not provide an opinion on whether prior debt forgiveness for improvements made to the property in prior years complied with the promissory note terms.

Methodology and Results

We reviewed the City's Amended and Restated Promissory Note and Special Warranty Deed to identify the criteria for loan forgiveness for job creation and retention specifically. The criteria around property improvements for loan forgiveness related to the first round of Phalanx loan forgiveness.

Table 1 provides the specific criteria to qualify for job creation and retention loan forgiveness, description of the criteria, and results of auditor review of documentation submitted by Phalanx.

Table 1

Borrower's Criteria for Loan Forgiveness (Amended and Restated Promissory Note)			
Criteria	Description	Auditor Testing Results	Criteria Met?
1. Submit Documentation to the City at the End of the Fiscal Year	At the end of Borrower's fiscal year each year thereafter, Borrower shall report its net full-time positions to the City.	In November 2020 Phalanx submitted payroll records for years 2016, 2017, 2018, and 2019, rather than annually. Phalanx was unable to provide evidence of 2020 payroll records.	No
2. Job Creation Must be Net New Full-Time Positions	All jobs must be qualified net new full-time positions. The net new full-time positions shall be in addition to the filled, full-time positions that the Borrower has on the date it moves its business operations onto the Property. To obtain loan forgiveness for each position, Borrower shall provide documentation to the City – Proof of meeting the salary level and retention as documented by the Borrower's payroll records.	Nine employees were determined to be net new full-time positions hired after the borrower signed the original promissory Note on September 7, 2016. Phalanx occupied the property on March 1, 2017.	Yes
3. Job Retention Must be At Least One (1) Year	All jobs shall be net new full-time positions created and retained for a period of one (1) year. To obtain loan forgiveness for each position, Borrower shall provide documentation	One of nine net new full-time employees was not retained for a period of at least one year as required in the Amended and Restated Promissory Note.	No

	to the City – Proof of meeting the retention period as documented by the Borrower’s payroll records.	Six of nine net new full-time employees were not retained for a period of two years, as required in the original promissory note.	
4. City Enterprise Zone Residency Required for Certain Tiers	To obtain loan forgiveness for each position, Borrower shall provide documentation to the City – Proof of residency in the City’s Enterprise Zone documented by deed or lease/rental agreement in the name of the employee.	No deeds or leases were submitted for consideration.	No
5. VA or US Military Honorable Discharge Veteran Status Documentation for Certain Tiers	To obtain loan forgiveness for each position, Borrower shall provide documentation to the City – Proof of honorably discharged veteran status documented by a DD-219 or other official VA or US Military documentation.	No qualifying documentation was submitted for consideration.	No
6. Employee Salary Level (Five Tiers)*	Employee Salary Must be at least a Certain Percentage of Average Annual Alachua County Wage. These salary levels are documented as Five Tiers as shown in Table 2.	<p>Two of eight qualifying employee salaries exceeded salary levels based on Enterprise Florida’s publication entitled “State of Florida Incentives Average Wage Requirements,” based on 2019 average annual county wage data.</p> <p>Below is an excerpt from Table 2. See Table 2 for more details.</p> <p>Tier 1 – 1 of 8 salaries qualified Tier 2 – 0 of 8 Tier 3 – 0 of 8 Tier 4 – 1 of 8 salaries qualified Tier 5 – 0 of 8</p>	Yes
7. Occupy Property for Business Operations for 10 Years following Date of Recording Deed	Grantee must occupy the property for Grantee’s business operations for a period of 10 years following the date of recording this deed. The deed was recorded on September 7, 2016. If not met, the property can revert back to the City.	<p>We viewed three patents obtained by Mr. Coats and assigned to Phalanx Defense Systems LLC.</p> <p>Mr. Coats communicated that Phalanx Defense Systems, LLC merged with a South Carolina based company called Tactical Medical Solutions in December 2019 and separated from Tactical Medical Solutions in January 2021.</p> <p>On December 2, 2019, Phalanx changed its Florida business registered name from Phalanx Defense Systems, LLC, to PDS Defense, LLC.</p> <p>On November 12, 2020, Mr. Coats registered a new business at the armory, “Reserve Station”.</p>	Not Determined

		<p>On January 21, 2021, we became aware of a Phalanx Defense Systems website message stating “WE’RE MOVING! We are currently completing the move to our brand new facilities! We hope to start shipping orders by the week of the 11th. Thanks for your patience!”</p> <p>On September 1, 2016, Mr. Coats registered a new business at the property, “Superheroes for Hope, Inc” which is a registered not for profit owned and operated by Mr. Coats.</p>	
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*See Table 2

TABLE 2			
Qualified New Full-time Job Creation and Retention			
	<i>Total new full-time jobs created and retained for at least one year (per amended agreement dated 4/11/2019) :</i>		8
	Tier I -salary at least 115% of Average Annual Alachua County Wage	\$3,000 per position	1 of 8
	Tier 2 - salary at least 150% of Average Annual Alachua County Wage	\$6,000 per position	0 of 8
	Tier 3 - hire is a resident of the City's Enterprise Zone or is an honorably discharged U.S. veteran, and the salary is at least \$25,000	\$6,000 per position	0 of 8
	Tier 4 -salary at least 200% of Average Annual Alachua County Wage	\$9,000 per position	1 of 8
	Tier 5 - hire is a resident of the City's Enterprise Zone and is an honorably discharged U.S. veteran, and the salary is at least \$25,000	\$9,000 per position	0 of 8
	<i>Based on 2019 salary data.</i>		

Conclusion

The City Auditor’s Office performed an independent review of Phalanx job creation and retention documentation submitted by Phalanx to request loan forgiveness as stated in the Amended and Restated Promissory Note, and Special Warranty Deed. Our results are summarized in Tables 1 and 2.