



**THE PORT  
OF LOS ANGELES**  
Executive Director's  
Report to the

Board of Harbor Commissioners

**DATE: MAY 29, 2012**

**FROM: FINANCIAL MANAGEMENT**

**SUBJECT: RESOLUTION NO. \_\_\_\_\_ - APPROVE FISCAL YEAR  
2012/13 ANNUAL BUDGET**

**SUMMARY:**

The proposed Fiscal Year (FY) 2012/13 Annual Budget of \$954,131,832 reflects the City of Los Angeles Harbor Department's (Harbor Department) efforts to align initiatives under its newly established Port of Los Angeles (Port) 2012-2017 Strategic Plan (Strategic Plan) with the associated costs to achieve them, balanced with projected amounts of revenues. It includes the revenues, expenses, and capital improvement plan for the Harbor Department based on key financial metrics in accordance with the Harbor Department's Financial Policies. The proposed budget is consistent with the preliminary information provided to the Board of Harbor Commissioners (Board) during the budget hearing held on March 15, 2012; no significant changes were made subsequent to the hearing.

**RECOMMENDATION:**

It is recommended that the Board of Harbor Commissioners:

1. Adopt the proposed Fiscal Year 2012/13 Annual Budget for the Harbor Department and appropriate funds in accordance therewith;
2. Authorize the Executive Director, or designee, to make any technical adjustments consistent with Board action(s) to the Fiscal Year 2012/13 budget documents, so as to provide for the implementation of this budget; and
3. Adopt Resolution No. \_\_\_\_\_.

**SUBJECT: APPROVE FISCAL YEAR 2012/13 ANNUAL BUDGET****DISCUSSION:**

The total proposed budget of \$954,131,832 for FY 2012/13 (Transmittal 1) represents a \$22.5 million or 2.3% decrease from the \$976,585,403 FY 2011/12 Adopted Budget (Adopted Budget) and a \$35.8 million or 3.6% decrease from the \$989,940,935 estimated expenditures for the current fiscal year. Despite higher capital improvement spending as projects move from design to the construction phase under a \$285.7 million Capital Improvement Program (CIP), the slightly smaller proposed budget includes relatively flat operating revenues given the difficult economy and controlled operating expenses reflecting the state of revenues. Capital and operating grant reimbursements are anticipated to increase by 47% compared to the Adopted Budget, augmenting our sources of cash and non-operating revenue. As a result, over 6,500 jobs are estimated to be created through Harbor Department spending proposed for FY 2012/13.

The key components of the \$954.1 million proposed budget are:

- \$340.7 million or 35.7% of the total budget for Capital;
- \$260.3 million or 27.3% as the Unappropriated Balance carried forward;
- \$213.1 million or 22.3% for Operating Expenses;
- \$180.2 million or 18.9% as Restricted Cash (including future year commitments); and
- \$29.9 million or 3.1% as Non-Operating Expenses and Balance Sheet transactions.

The proposed budget also includes an estimated level of potential commercial paper borrowing of \$70 million for managing cash flow. In addition to overall budget performance, financial market conditions and the timing of expenditures, the level of actual borrowing also takes into consideration maintaining a cash reserve requirement of \$235 million in compliance with the Harbor Department's Financial Policies.

The proposed FY 2012/13 Annual Budget was formulated based on the Strategic Plan, financial metrics based on the Harbor Department's Financial Policies, and input from the Board.

Strategic Plan – The budget process this year ran in parallel and in coordination with the strategic planning process. At the onset of the budget process, proposed priorities were developed based on the Harbor Department's then evolving Strategic Plan. Through strategic planning discussions at the senior management level and input from the divisions, stakeholders, and the Board, the three resulting broad key result areas of Competitive Operations, Strong Relationships, and Financial Strength became the proposed priorities for FY 2012/13. Through the budget process, divisions proposed initiatives and funding requests that aligned with the proposed priorities. The Strategic Plan was

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approved by the Board on April 19, 2012 and outlines the objectives, initiatives to be implemented over the next five years, and associated performance metrics to accomplish the Port's mission. (A complete copy of the approved Strategic Plan may be accessed on the Port's website at <http://www.portoflosangeles.org/>.)

Financial Metrics – In addition to the proposed priorities, the proposed budget was established based on maintaining the following key financial metrics in compliance with the Harbor Department's Financial Policies and Strategic Plan performance metrics:

- A minimum debt service coverage of 2.0X;
- A minimum level of cash reserves of \$235 million; and
- A minimum operating margin of 45%.

Board Review – A special Board meeting was held on March 15, 2012 to review the preliminary proposed budget. During this meeting, the Board discussed the components of the budget with, and provided input and guidance to, the Harbor Department's Executive Director and senior management. The Board requested additional information relating to specific items, which were provided under a separate memo. Such requests included: a Market Share Trend Analysis Report and how market share and TEU (Twenty-foot Equivalent Unit) volumes can fluctuate independent of each other; information regarding the China Shipping Container Terminal Development liquidated damages; details of the Capital Improvement Program contingency budget; statistics relating to Jacobsen pilots; considering doing more now in the way of deferred maintenance; more in-depth benchmark analysis between the Port of Long Beach and Harbor Department; anticipated duration of the security audit; goals for reducing workers' compensation expenses; number of employees participating in the Harbor Department's respective benefits; a final version of the Strategic Plan; and a copy of the March 29, 2012 Waterfront presentation.

Two changes were made subsequent to the meeting, resulting in a \$389.5 thousand net reduction to the overall operating expense budget:

- Salaries and Benefits were reduced by \$538.3 thousand for technical corrections to positions due to changes in classifications, step levels, etc.
- Materials and Supplies were increased by \$148.8 thousand to fund damage to the Cabrillo Marina Ship-in-a-Bottle exhibit.

Operating and Non-Operating Budget: Year-to-Year Results – The major drivers to the variance between FY 2011/12 estimates and FY 2012/13 proposed budget are Clean Truck Program revenues, Salaries and Benefits, City Services, Litigation, and Non-Operating revenues. Comparisons of the proposed budget with FY 2011/12 estimates and Adopted Budget are as follows:

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**FY 2012/13 Proposed Operating/Non-Operating Budget  
Comparisons with FY 2011/12 Estimates and Adopted Budget**

	(000s) Adopted Budget		Estimates	Proposed Budget	Δ \$	Δ %	Δ %
	FY 2011/12	FY 2011/12	FY 2011/12	FY 2012/13	Estimate to Proposed Budget	Estimate to Proposed Budget	Adopted to Proposed Budget
<b>Operating Revenues</b>							
Shipping Services	\$348,122	\$346,163		\$347,498	\$1,335	0.39%	-0.18%
Rentals	49,533	45,011		45,174	163	0.36%	-8.80%
Royalties and Fees	2,693	2,896		2,925	29	1.00%	8.61%
Clean Truck Fees	2,040	2,955		500	-2,455	-83.08%	-75.49%
Other Operating	2,984	2,471		2,495	24	0.97%	-16.39%
<b>Total Operating Revenues</b>	<b>405,372</b>	<b>399,496</b>		<b>398,592</b>	<b>-904</b>	<b>-0.23%</b>	<b>-1.67%</b>
<b>Operating Expenses</b>							
Salaries & Benefits	110,631	105,385		108,221	2,836	2.69%	-2.18%
Marketing and Public Relations	3,955	3,762		3,614	-148	-3.93%	-8.62%
Travel	873	798		925	127	15.91%	5.96%
Outside Services	36,598	34,817		35,217	400	1.15%	-3.77%
Materials & Supplies	7,311	6,859		7,635	776	11.31%	4.43%
City Services	40,325	37,965		36,150	-1,815	-4.78%	-10.35%
Allocations to Capital	-6,210	-9,000		-9,000	0	0.00%	44.93%
Other Operating Expenses	32,136	24,203		30,290	6,087	25.15%	-5.74%
<b>Total Operating Expenses</b>	<b>225,619</b>	<b>204,789</b>		<b>213,052</b>	<b>8,263</b>	<b>4.03%</b>	<b>-5.57%</b>
<b>Income from Operations before Depreciation</b>	<b>179,753</b>	<b>194,707</b>		<b>185,540</b>	<b>-9,167</b>	<b>-4.71%</b>	<b>3.22%</b>
Depreciation	-91,814	-97,696		-98,601	-905	0.93%	7.39%
<b>Income from Operations</b>	<b>87,939</b>	<b>97,011</b>		<b>86,939</b>	<b>-10,072</b>	<b>-10.38%</b>	<b>-1.14%</b>
Non-Operating Revenues	30,031	20,509		30,938	10,429	50.85%	3.02%
Non-Operating Expenses	-32,958	-28,805		-28,605	200	-0.69%	-13.21%
<b>Net Income</b>	<b>\$85,012</b>	<b>\$88,715</b>		<b>\$89,272</b>	<b>\$557</b>	<b>0.63%</b>	<b>5.01%</b>

Note: Figures in this chart may differ from the Comparative Statement of Operations (Transmittal 1) due to rounding.

Operating Revenue Budget – Proposed Operating Revenues are budgeted to be \$398.6 million and are generally flat compared to the current fiscal year estimate of \$399.5 million. Proposed Shipping Services revenue continues to be driven by TEU volumes. The budgeted TEU volume level of 8.03 million represents both full and empty inbound and outbound TEUs for next fiscal year, which is a 1.1% increase from current year estimates based on data from our tenants and market estimates. The projected volume levels are those that we have not seen since FY 2007/08, but continue to show a positive yet gradual upward trend. As a result, associated Shipping Services are budgeted to increase slightly by \$1.3 million or 0.4%. This increase is, for the most part, offset by a budgeted decrease of \$2.5 million or 83.1% in Clean Truck Program revenue due to fewer trucks that are subject to a fee, resulting in overall proposed Operating Revenues remaining generally flat to the current fiscal year.

When compared to the FY 2011/12 Adopted Budget, proposed Operating Revenues are \$6.8 million or 1.7% lower primarily due to lower Rentals by \$4.4 million and Clean Truck Program income by \$1.5 million. For Rentals, the

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Adopted Budget included approximately \$5 million in new fixed land rental income that did not materialize in the current fiscal year. This is now projected to occur in FY 2013/14.

Operating Expense Budget –The Operating Expense budget of \$213.1 million represents an \$8.3 million or 4% increase from the current fiscal year estimate and a \$12.6 million or 5.6% decrease from the FY 2011/12 Adopted Budget. Earlier this fiscal year, when it became evident that the budgeted growth in cargo volumes would not materialize, the Harbor Department took steps to realign its current fiscal year spending to that of FY 2010/11 or \$209 million. This served as the base upon which the proposed budget was formulated.

Salaries and Benefits continue to be the largest contributors to expenses, comprising 51% of the Operating Expense budget and a primary driver in the increase in Operating Expenses from the current fiscal year estimate. Higher Litigation expenses for Community Mitigation also contributed towards the increase from the current fiscal year estimate, while lower City Services partially offset the increases. Compared to the Adopted Budget, lower Salaries and Benefits, Outside Services, City Services, and Litigation expenses were the primary drivers for the decrease in the proposed budget.

**1. *Proposed Salaries and Benefits*** increased by 2.7% or \$2.8 million from the current fiscal year estimate and decreased by 2.2% or \$2.4 million from the FY 2011/12 Adopted Budget. The primary reasons for the year-to-year increase are attributed to:

- **Added Positions** – A net increase of five positions were added, totaling approximately \$500 thousand, bringing the authorized level to 994 from 989. The increase was primarily for the Construction and Maintenance Division to provide resources to maintain new Port facilities, such as the Wilmington Waterfront Park, the Los Angeles Port Police Headquarters, and the Maritime Law Enforcement Training Center.
- **Salary Adjustments** – Approximately \$1.9 million is budgeted for step increases, other Memorandum of Understanding (MOU) adjustments, promotions, and higher health care costs.
- **Student Worker Programs** – Approximately \$400 thousand is funding a new international student work program and an expanded summer intern program.

Compared to the Adopted Budget, Salaries and Benefits are lower due to increased capitalization as a result of increased capital spending and lower pension contribution rates.

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- 2. *Proposed Marketing and Public Relations*** expenses include department-wide marketing activities such as customer and community outreach and sponsorships. Expenses in this category are lower compared to both the current fiscal year estimates and Adopted Budget as a result of reduction efforts by the Communications group in realigning spending with strategic initiatives.
- 3. *Proposed Travel*** expenses are proposed to be higher than both current year estimates and the Adopted Budget. Consistent with the Strategic Plan, additional travel funds are allocated towards marketing efforts to retain and grow market share.
- 4. *Proposed Outside Services*** are remaining generally flat to current fiscal year estimates and \$1.4 million or 3.8% lower than the Adopted Budget. During this budget process, efforts continue to be made to align the budgeted amount with spending. The proposed Outside Services budget of \$35.2 million is within the Harbor Department's average range of spending over the past 6 years. Major spending in this expense category is budgeted for environmental assessments, maintenance improvement, and information technology.
- 5. *Proposed Materials and Supplies*** spending are budgeted to increase by \$776 thousand or 11.3% compared to FY 2011/12 estimates and \$324 thousand or 4.4% primarily due to increased expenses for new facilities.
- 6. *Proposed City Services*** budgeted expenses are lower compared to both FY 2011/12 estimates and Adopted Budget by \$1.8 million or 4.8% and \$4.2 million or 10.4% respectively. Compared to estimates, the decrease is attributed to lower Cost Allocation Plan (CAP) rates and lower fireboat maintenance costs than budgeted in the current fiscal year. Compared to the Adopted Budget, the decrease was also attributed to lower fire costs and CAP rates, as well as reduced staffing in the Mayor's Liaison Office.
- 7. *Proposed Other Operating Expenses*** are higher compared to FY 2011/12 estimates by \$6.1 million or 25.1% and \$1.8 million or 5.7% lower compared to the Adopted Budget. Both are due to Community Mitigation contributions for projects budgeted in the current fiscal year but not launched and therefore not paid; the project is now planned and associated Community Mitigation contributions are budgeted for next fiscal year.
- 8. *Overhead Allocations to Capital*** are flat compared to current year estimates. Compared to Adopted Budget, the budget is higher by \$2.8 million or 44.9% primarily due to the growth in administrative support to match the increase in the level of capital spending in the Construction and Maintenance Division. Generally, allocations to capital overhead have primarily applied to

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the Development Bureau Divisions such as Engineering, Construction, and Environmental Management that engage in capital improvement projects. Beginning this fiscal year, the Information Technology and Finance Divisions are also expected to have allocations to capital overhead for the implementation of the Enterprise Resource Planning (ERP) system.

Non-Operating Budget – Non-Operating Revenues are budgeted to increase by \$10.4 million or 50.9% from current fiscal year estimates and by \$0.9 million or 3% compared to the Adopted Budget due primarily to an increase in Federal pass-through grant receipts. Non-Operating Expenses are budgeted to slightly decrease by \$0.2 million or 0.7% compared to current year estimates, due primarily to the \$8.3 million loss on the sale of Port of Los Angeles High School this fiscal year, a lower Alameda Corridor Transportation Authority (ACTA) shortfall by \$3 million, \$3 million in lower capital projects closed to expense, \$0.5 million in lower interest and other expenses, partially offset by \$12.8 million in higher Federal pass-through grant receipts disbursements, and \$1.7 million in higher commercial paper cost of issuance expenses. Compared to the Adopted Budget, Non-Operating Expenses are lower by \$4.4 million or 13.2% primarily due to \$9.7 million in reserves that were budgeted for the ACTA shortfall, \$3 million in lower capital projects closed to expense, \$1.3 million in lower interest and other expenses, partially offset by \$7.2 million in higher Federal pass-through grant receipts and \$2.7 million in higher commercial paper interest and cost of issuance.

Capital Budget – To meet the future needs of the Harbor Department and to enhance job creation and economic development, a Capital Budget of \$340.7 million is proposed, which includes expenditures for projects that have been approved, those that are pending approval and proposed equipment purchases. The components of the Capital Budget include:

- \$285.7 million Capital Improvement Program;
- \$46.4 million in Allocations to Capital (for overhead and other expenses); and
- \$8.6 million for Capital Equipment.

The Capital Improvement Program component of the Capital Budget proposed at \$285.7 million represents a \$95.3 million or 50% increase from the estimated current year expenditure of \$190.4 million. Compared with the current year Adopted Budget of \$229.7 million, this is a \$56 million or 24.4% increase. The amount of the CIP was established by taking into consideration the priority and timing of the projects and their construction and how these factors align to the debt capacity of the Harbor Department as it maintains a minimum debt service coverage ratio of 2.0X. Transmittal 1 contains a complete listing of projects. At this time, the Harbor Department anticipates about \$70 million in additional commercial paper borrowings to meet the cash flow needs of Port-wide projects and operations. However, depending on financial market conditions and the

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timing of spending, borrowings, if any, may vary and are subject to Board approval.

Grants – The proposed budget includes a total of \$81 million in both operating and capital grant reimbursements. This represents an increase of \$26 million or 47.3% from the current fiscal year estimates and includes:

By Funding Source: \$81M	By Project Category: \$81M	By Function: \$81M
Federal Grants: \$59 million	Capital: \$58 million	Security: \$43 million
State Grants: \$22 million	Operating: \$ 2 million	Transportation: \$36 million
	Pass-Through: \$21 million	Environmental: \$ 2 million

The Harbor Department’s grants management program is currently managing approximately \$437 million in active grants. Approximately \$92 million potential awards are currently under consideration or in the application process.

Proposed Budget Priorities Funding Highlights – Based on budget submittals and input received from divisions, the following chart depicts an approximation of the proposed Operating Budget aligned by the Port’s Strategic Plan Key Result Areas.

**Proposed Operating Budget  
\$213.1 Million  
Aligned By Strategic Key Result Areas  
(\$'s in Millions)**



Among the many initiatives in the Strategic Plan to be accomplished next fiscal year, five are highlighted as the key priorities for FY 2012/13, as follows:



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- Deliver critical terminal and infrastructure projects on time and within budget through the execution of the Capital Improvement Program
  - Of the \$285.7 million CIP budget, \$266 million is for terminal and infrastructure projects (Transmittal 1).
- Adapt the Business Development Plan to changing dynamics of the industry and leverage relationships with ocean carriers, marine terminal operators, beneficial cargo owners and other key supply chain stakeholders
  - \$1.7 million has been earmarked to expand Trade Connect Programs, evaluate and recommend new markets, establish a Customer Service Account Manager Program, among others.
- Implement the recommendations of the Competitive Cargo Strategy Committee and/or Port-initiated incentive programs
  - \$1.1 million has been estimated to implement the recommendations of the Competitive Cargo Strategy Committee, including staffing costs.
- Update the Port Master Plan, including the Terminal Island Plan
  - \$2.5 million has been budgeted for environmental consultants to prepare the Environmental Impact Report, for engineering consultants to prepare capacity, rail and traffic studies, as well as staffing costs.
- Develop and implement a comprehensive Stakeholder Outreach Plan by second quarter 2013. Use the Strategic Plan as the first topic for a message matrix system that maintains consistent “one voice” messaging across the entire organization
  - \$155 thousand has been budgeted for consulting services for both internal and external communication outreach plans, media engagement plan, and other ancillary needs (e.g., writing, printing, etc.).

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The proposed action is approval of the FY 2012/13 Annual Budget. All projects potentially financed through the Resolution would require separate Board approval. As an administrative activity, the Director of Environmental Management has determined that the proposed action is exempt from the requirements of the California Environmental Quality Act (CEQA) in accordance with Article II, Section 2(f) of the Los Angeles City CEQA Guidelines.

**ECONOMIC BENEFITS:**

The proposed FY 2012/13 Annual Budget supports the creation of over 6,500 jobs within the region as follows:

	Actual FY 2011	Estimates FY 2012	Proposed Budget FY 2013
Direct Jobs at the Port	958	954	994
Jobs Created by the Port – Capital Spending	3,943	3,372	4,643
Jobs Created by Other Port Spending	<u>755</u>	<u>839</u>	<u>874</u>
Total Jobs Created	5,656	5,165	6,511

**FINANCIAL IMPACT:**

Approval of the proposed FY 2012/13 Annual Budget will establish the Harbor Department's Operating and Capital Improvement Budgets and appropriate the necessary funds for the Harbor Department's operations in the next fiscal year. Any requirements that exceed amounts authorized in the Annual Budget will require separate Board authorization.

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CITY ATTORNEY:

There are no legal issues to address at this time.

TRANSMITTAL:

1. Fiscal Year 2012/13 Annual Proposed Budget

FIS Approval: KIP (initials)  
CA Approval: TAC (initials)

  
KARL K.Y. PAN  
Chief Financial Officer

  
MOLLY CAMPBELL  
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APPROVED:

  
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