



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

Board of Harbor Commissioners

DATE: APRIL 6, 2016

FROM: FINANCIAL MANAGEMENT

SUBJECT: RESOLUTION NO. _____ - REQUEST FOR
BUDGETARY TRANSFER FROM FY 2015/16 ADOPTED CAPITAL
IMPROVEMENT PROGRAM BUDGET TO ADOPTED OPERATING
EXPENSE BUDGET

SUMMARY:

The City of Los Angeles Harbor Department (Harbor Department) staff proposes total budgetary transfers of \$6,816,419, summarized as follows:

1. Transfer \$2,413,267 from the Fiscal Year (FY) 2015/16 Adopted Capital Improvement Program Budget (Adopted Capital Budget) to meet a shortfall in the FY 2015/16 Adopted Operating Expense Budget (Adopted Operating Expense Budget) "Other Operating Expenses" category;
2. Transfer \$4,273,152 from the Adopted Capital Budget to the Adopted Operating Expense Budget's "City Services" category; and
3. Transfer \$130,000 from the Adopted Capital Budget to the Adopted Operating Expense Budget's "Materials & Supplies" category.

The first anticipated shortfall within the Other Operating Expenses category results from an accounting requirement to reserve an allowance for potentially uncollectible revenue resulting from ongoing litigation, while the second results from an increase in pollution remediation expenses as determined by the annual reconciliation of estimated pollution remediation costs for 21 active projects. The anticipated shortfall within the City Services category results from higher than anticipated maintenance expenses for recreational facilities within the Harbor area as well as additional payments which reconcile the difference between estimated and actual overhead costs incurred by the City of Los Angeles. The anticipated shortfall within the Materials & Supplies category results from greater amounts of materials required for the Construction & Maintenance (C&M) Division to perform its growing level of maintenance responsibilities. Sufficient funds are available within the Adopted Capital Budget for this budgetary transfer as staff anticipates a surplus will exist by fiscal year end. Payment of the expected Other Operating, City Services and Materials & Supplies expenses is the financial responsibility of the Harbor Department.

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RECOMMENDATION:

It is recommended that the Board of Harbor Commissioners (Board):

1. Find that the Proposed action is exempt from the requirements of the California Environmental Quality Act (CEQA) under Article II Section 2(f) of the Los Angeles City CEQA Guidelines as determined by the Director of Environmental Management;
2. Approve the following budgetary transfers to resolve a projected shortfall in the respective operating expense accounts:
 - a. Transfer \$2,413,267 from the Adopted Capital Budget, Account 13807, Center 1000, Program 000 to Other Operating Expenses (Program 000) as follows:
 - i. \$1,816,792 to Center 0900, Account 59810; and
 - ii. \$596,475 to Center 0330, Account 59960;
 - b. Transfer \$4,273,152 from the Adopted Capital Budget, Account 13807, Center 1000, Program 000 to City Services (Program 000) as follows:
 - i. \$2,072,844 to Center 0900, Account 57070;
 - ii. \$768,345 to Center 0120, Account 57010;
 - iii. \$398,967 to Center 0900, Account 57065; and
 - iv. \$1,032,996 to Center 0900, Account 57075; and
 - c. Transfer \$130,000 from the Adopted Capital Budget, Account 13807, Center 1000, Program 000 to Materials & Supplies (Program 000), Center 0510, Account 55010;
3. Direct the Board Secretary to transmit the Resolution to the Mayor for approval pursuant to Section 343(b) of the City Charter;
4. Direct the Board Secretary to notify the City Clerk of such transfer pursuant to Section 343(d) of the City Charter at the time such transfer is made; and
5. Adopt Resolution No. _____.

DISCUSSION:

Background/Context

Transfer for BNSF License Fee Allowance – Per Order No. 13-7125, the Board of Harbor Commissioners (Board) approved a Site Preparation and Access Agreement (SPAA) that would allow the BNSF Railway Company (BNSF) to perform necessary site preparation work, and to construct a proposed intermodal near-dock rail facility to be known as the Southern California International Gateway (SCIG). During the first year of the SPAA, the proposed compensation (License Fee) to the Harbor Department was to be \$6,266,106 annually with annual adjustments based upon the Consumer Price Index. Up to \$12.6 million in abatement costs incurred by BNSF to demolish existing improvements as well as any unanticipated BNSF expenditures on any environmental

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remediation would also be credited against the annual License Fees payable by BNSF to the Harbor Department.

Per section 11.1 (Section 11.1) of the SPAA, for any period of time where there is litigation, license fees due from BNSF to the Port of Los Angeles will be tolled and paid over the life of the agreement once the litigation has been settled. Following the execution of Order No. 13-7125, License Fees began to accrue as per the terms of the SPAA. During FY 2014/15, License Fees in the amount of \$10,886,841 were invoiced by the Harbor Department to BNSF.

However, following the execution of Order No. 13-7125 and Los Angeles City Council ratification, the City of Long Beach, the Long Beach Unified School District and other parties pursued litigation against the City of Los Angeles over the project. As of February 29, 2016, any resolution of this litigation is still pending.

Due to this litigation, as per Section 11.1 of the SPAA, BNSF did not pay the License Fees invoiced by the Harbor Department in FY 2014/15, and has continued to not pay these License Fees during FY 2015/16. In order to better account for the manner in which the Harbor Department invoices BNSF for License Fees that then go unpaid by BNSF while litigation is ongoing, staff has determined it appropriate to create a reserve against the amount of License Fees invoiced during any given fiscal year in which the BNSF SCIG facility is being litigated. Given that litigation may continue for years until an initial decision is delivered and all subsequent appeals are resolved, creating an annual reserve equal to the amount of invoiced License Fees will avoid a large future one-time expense in the event that BNSF is not able to prepare the site and construct the SCIG facility.

During FY 2015/16, the Harbor Department anticipates invoicing BNSF for License Fees totaling \$6,439,537. As discussed above, BNSF will not pay these License Fees until the litigation is concluded and BNSF is able to begin preparing the site ahead of its construction of the SCIG facility. Therefore, a reserve in an amount equal to the \$6,439,537 of invoiced License Fees is required in order to appropriately reflect the risk that the License Fees could potentially become uncollectible if the ultimate litigation resolution prevents BNSF from preparing the site and constructing the SCIG facility.

Reserves against potentially uncollectible accounts were budgeted to be \$200,000 within the FY 2015/16 Adopted Budget. As summarized below, savings are expected to be realized within other 59-series accounts such that a budget transfer for the full amount of invoiced SCIG License Fees will not be necessary at this time:

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TABLE 1: BUDGET SHORTFALL SUMMARY (PROVISION FOR BAD DEBTS)

A59810: Provision for Bad Debts		
FY 2015/16 Adopted Budget – A59810		\$ 200,000
Adjustments:		
BNSF-SCIG License Fee Reserve	6,439,537	
Less: Other Operating Expense Savings from Other 59 Accounts	(4,622,745)	
Total Adjustments (Budget Transfer Request)		1,816,792
FY 2015/16 Adopted Budget – A59810, Adjusted		\$ 2,016,792

A budget transfer in the amount of \$1,816,792 is being requested at this time because a reserve against the annual amount of invoiced BNSF-SCIG License Fees was not considered when the FY 2015/16 Budget was originally adopted.

Transfer to Record Remediation Obligations – In November 2006, the Government Accounting Standards Board (GASB) issued Statement No. 49 (GASB 49) establishing standards for accounting and financial reporting of pollution remediation obligations by state and local governments. GASB 49 requires a government to estimate the components of expected pollution remediation outlays and determine whether outlays of those components should be accrued as a liability or, if appropriate, capitalized, if any one of the following obligating events occur:

- i) The government is compelled to take pollution remediation action because of imminent endangerment;
- ii) The government violated a pollution prevention-related permit or license;
- iii) The government is named, or evidence indicates that it will be named, by a regulator as a responsible party or potentially responsible party for remediation, or as a government responsible for sharing costs;
- iv) The government is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation; or
- v) The government commences or legally obligates itself to commence pollution remediation.

In compliance with GASB 49, the total cost of remediation for GASB projects shall be reflected as an expense and the future spending obligations will be reflected as a liability in the Harbor Department's balance sheet. The GASB FY 15/16 Annual Report included an annual reconciliation for all 21 active projects, and requires an increase of \$596,475 to account for increased remediation estimates to four projects: Former Warehouse 12 (\$932,680), New Dock Pump Station (\$600,000), San Pedro Boat Works (\$411,000), and Southwest Marine (\$3,250,000). The \$5,193,680 increase associated with these four projects was offset by reductions in estimated expenditures for other projects during the reconciliation process.

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The Harbor Department has determined that the remediation outlays for the Former Warehouse 12, New Dock Pump Station, San Pedro Boat Works, and Southwest Marine meet the standards under GASB 49. The remediation costs will therefore be expensed and recorded as a liability in the financial statements. Since these adjustments were not previously budgeted, a transfer is necessary.

The increase in the GASB Remediation Obligation is due to increases in remediation estimates for the four projects described above and is summarized as follows:

TABLE 2: BUDGET SHORTFALL SUMMARY (POLLUTION REMEDIATION)

A59960: Pollution Remediation Expense		
FY 2015/16 Adopted Budget – A59960		\$ -
Adjustments:		
Ending Pollution Remediation Obligation Balance	73,998,576	
Less: Beginning Pollution Remediation Obligation Balance	73,402,101	
Total Adjustments (Budget Transfer Request)		596,475
FY 2015/16 Adopted Budget – A59960, Adjusted		\$ 596,475

As noted within the table above, the FY 2015/16 GASB Annual Report ending balance of \$73,998,576 exceeds the GASB FY 2014/15 beginning balance of \$73,402,101. Therefore, a budget transfer in the amount of \$596,475 is being requested at this time.

Transfer for Fire Services – The Los Angeles Fire Department (LAFD) provides firefighting, emergency medical and technical response services to the Harbor Department, and these Fire Services include the use of fireboats, fire engines, urban search and rescue equipment as well as hazardous materials teams both within the immediate Harbor area and the surrounding local communities. In addition to paying the salaries of local LAFD personnel, the Harbor Department pays for overtime, LAFD medical, pension and other fringe benefits as well as overhead charges that are intended to capture central services and administrative expenses. These overhead charges are memorialized and updated in the city's Cost Allocation Plan (CAP). In FY 2015/16, the LAFD invoices have included \$1.63 in overtime, benefits and overhead expenses for every \$1 in salaries incurred by local LAFD personnel.

The City's CAP for a given fiscal year is typically published after that fiscal year has ended on June 30. For instance, CAP #37 was the relevant CAP for FY 2014/15; however, it was not published until September 2015. Because applicable CAP rates are unavailable throughout a given fiscal year, the most recently available CAP rates are applied to personnel salaries, overhead charges are estimated within LAFD invoices to the Harbor Department, and any differences between estimated overhead charges and applicable overhead charges are reconciled through a true-up which is paid in a subsequent fiscal year. Furthermore, due to this timing difference in which a given fiscal year's CAP rates are not made available until after that fiscal year has ended, the CAP rates utilized for Harbor Department budgeting purposes are typically subject to at

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least a two-year lag, and differences between budgeted overhead expenses and billed overhead expenses do arise.

During FY 2015/16, the LAFD invoiced the Harbor Department for a true-up of \$1,018,186 in overhead costs related to the FY 2013/14 billing cycle ("FY 2013/14 True-Up") because applicable overhead rates exceeded the overhead rates estimated and applied over the course of FY 2013/14. The FY 2013/14 True-Up was not budgeted in FY 2015/16 because the applicable FY 2013/14 CAP rate was not published until September 3, 2015, approximately 3 months after the FY 2015/16 budget was adopted in June 2015.

Lastly, as previously indicated, the FY 2015/16 budget was developed using the most recently available, in this case FY 2012/13, CAP rates at the time when the FY 2015/16 budget was adopted. Based upon the current run rate of expenses, overhead charges which include extraordinary maintenance costs are expected to be \$1,054,658 greater than budgeted.

In aggregate, \$2,072,844 in additional overhead payments and extraordinary maintenance costs were not originally budgeted within the FY 2015/16 Adopted Budget, summarized as follows:

TABLE 3: BUDGET SHORTFALL SUMMARY (FIRE SERVICES)

A57070: City Services – Fire	
FY 2015/16 Adopted Budget – A57070	\$ 21,032,280
Adjustments:	
FY 2013/14 True-Up	1,018,186
Budget – Estimate Difference	1,054,658
Total Adjustments (Budget Transfer Request)	2,072,844
FY 2015/16 Adopted Budget – A57070, Adjusted	\$ 23,105,124

A budget transfer in the amount of the \$2,072,844 is being requested at this time because the aforementioned CAP rate increases and extraordinary maintenance costs were not contemplated when the FY 2015/16 Budget was adopted.

Transfer for City Attorney – The City of Los Angeles Office of the City Attorney (City Attorney) provides legal services to the Harbor Department. In exchange for these Legal Services, the Harbor Department reimburses the City Attorney for the related salaries, benefits and overhead incurred by City Attorney staff.

Similar to how a true-up is required to offset the difference between estimated overhead expenses and actual overhead expenses incurred for Fire Services (described previously), a true-up is required to offset the difference between estimated overhead and actual overhead expenses incurred for Legal Services.

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TABLE 4: BUDGET SHORTFALL SUMMARY (CITY ATTORNEY)

A57010: City Services – City Attorney	
FY 2015/16 Adopted Budget – A57010	\$ 4,899,154
Adjustments:	
FY 2013/14 True-Up	517,066
Budget – Estimate Difference	251,279
Total Adjustments (Budget Transfer Request)	768,345
FY 2015/16 Adopted Budget – A57010, Adjusted	\$ 5,667,499

Specifically, a budget transfer in the amount of \$768,345 is being requested at this time because the aforementioned CAP rate increases were not contemplated when the FY 2015/16 Budget was adopted.

Transfer for Personnel Services – The City of Los Angeles Personnel Department provides workforce management as well as employee support and development services to the Harbor Department. In exchange for these services, the Harbor Department reimburses the Personnel Department for the related salaries, benefits and overhead incurred by Personnel Department staff.

Similar to how a true-up is required to offset the difference between estimated overhead expenses and actual overhead expenses incurred for Fire Services (described previously), a true-up is required to offset the difference between estimated overhead and actual overhead expenses incurred for Personnel Services. Furthermore, an additional \$352,357 in funds are being requested due to a higher than budgeted run-rate in Personnel Services expenses.

TABLE 5: BUDGET SHORTFALL SUMMARY (PERSONNEL SERVICES)

A57065: City Services – Personnel Services	
FY 2015/16 Adopted Budget – A57065	\$ 502,727
Adjustments:	
FY 2013/14 True-Up	46,610
Budget – Estimate Difference	352,357
Total Adjustments (Budget Transfer Request)	398,967
FY 2015/16 Adopted Budget – A57065, Adjusted	\$ 901,694

Specifically, a budget transfer in the amount of \$398,967 is being requested at this time because the aforementioned CAP rate increases were not contemplated when the FY 2015/16 Budget was adopted and estimated Personnel Services expenses exceed the FY 2015/16 Budget.

Transfer for Recreation and Parks – The Department of Recreation and Parks (RAP) provides operational and maintenance services (RAP Services) at various locations throughout the Harbor-area. In exchange for these RAP Services, the Harbor

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Department reimburses the RAP for the salaries, benefits and overhead related to providing RAP Services at the following Harbor-area locations:

- Cabrillo Marine Aquarium
- Cabrillo Beach Lifeguard
- Cabrillo Beach Maintenance
- Cabrillo Parking Operations
- Maritime Museum
- Point Fermin Lighthouse
- Gaffey Street Greenbelt

In addition, the Harbor Department reimburses the RAP for a proportionate share of city-wide construction costs as well as a proportionate share of Pacific Region Ranger expenses.

The RAP Services FY 2015/16 Adopted Budget of \$8,169,249 was derived by applying a 3% growth rate to FY 2013/14 Actual costs. In FY 2014/15, actual expenses of \$8,395,958 were incurred for RAP Services, and this level of expenses exceeded the budget that had been adopted for the subsequent fiscal year. Based upon RAP invoices received through December 2015, the Harbor Department anticipates that expenses of \$9,202,245 will be incurred during FY 2015/16. The increase relative to FY 2014/15 has been primarily driven by higher salaries, benefits and overhead expenses being incurred at the Cabrillo Marine Aquarium, Maritime Museum and other facilities as well as lower Parking Receipts, summarized as follows:

TABLE 6: BUDGET SHORTFALL SUMMARY (RECREATION AND PARKS)

A57075: City Services – Recreation and Parks	
FY 2015/16 Estimate – A57075	\$ 9,202,245
Less: FY 2015/16 Adopted Budget	(8,169,249)
RAP Budgetary Transfer Request	\$ 1,032,996

As noted within the table above, the FY 2015/16 Estimate of \$9,202,245 exceeds the FY 2015/16 Adopted Budget of \$8,169,249. Therefore, a budget transfer in the amount of \$1,032,996 is being requested at this time.

Transfer for Materials & Supplies – In order to address maintenance needs, the C&M Division requires additional materials and supplies that were not originally budgeted. As of February 29, 2016, the Harbor Department anticipates a \$130,000 deficit within the C&M Division’s Adopted Budget for *A55010: Parts & Materials* (A55010). This deficit has arisen primarily due to higher work requests coming into C&M than originally budgeted. Historically, spending within C&M’s A55010 has averaged approximately 100% of budget, and, as of February 29, 2016, fiscal year-to-date (FYTD) spending within C&M’s A55010 has exceeded its FYTD budget by 8%. Without the requested funding, some requests will be deferred until sufficient funding is made available.

Capital Budget Surplus – Adopted as part of Resolution No. 15-7810, the Adopted Capital Budget included funding of \$198.8 million for approved capital improvement program expenditures incurred during FY 2015/16. As of February 29, 2016, staff estimates that actual annual capital expenditures will be approximately \$178.1 million during FY 2015/16, resulting in a surplus of approximately \$20.7 million. As discussed

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previously, this surplus has been identified to offset projected deficits in other operating accounts.

ENVIRONMENTAL ASSESSMENT

The proposed actions are to transfer funds from the Adopted Capital Budget to the Adopted Operating Expense Budget to resolve a projected shortfall in the Other Operating Expenses, City Services and Materials & Supplies categories. As an administrative action, the Director of Environmental Management has determined that the proposed action is exempt from the requirements of CEQA under Article II Section 2(f) of the Los Angeles City CEQA Guidelines.

FINANCIAL IMPACT

The transfer of funds from the Adopted Capital Budget, Account 13807, Center 1000, Program 000 to the Adopted Operating Expense Budget will increase the FY 15/16 Adopted Operating Expense Budget by \$6,816,419, and will reduce the Adopted Capital Budget by the same dollar amount. This transfer of funds will impact the Harbor Department's FY 2015/16 Estimated Operating Margin; however, the impact on the FY 2015/16 Estimated Operating Margin must also take into account: (i) an anticipated \$6,725,430 increase in FY 2015/16 Operating Revenues, and (ii) anticipated savings of \$7,000,000 in FY 2015/16 salaries and benefits expenses, as depicted within the table below:

TABLE 7: OPERATING MARGIN AND DEBT SERVICE COVERAGE RATIO

	FY 2015/16 Adopted Budget	Estimated Revenue Increase	Estimated S&B Decrease	Budget Transfers	FY 2015/16 "As- Adjusted"
Operating Revenues	428,588,311	6,725,430			435,313,741
Less: Operating Exp.	233,484,156		(7,000,000)	6,816,419	233,300,575
Operating Income	195,104,155				202,013,166
Operating Margin %	45.5%				46.4%

As noted above, the combined effect of the proposed budgetary transfer and the above-referenced other items would be an increase in FY 2015/16 Estimated Operating Margins from 45.5% to 46.4% which continues to exceed the Harbor Department's self-mandated minimum Operating Margin of 45%. In accordance with City Charter Section 343, this intradepartmental budgetary transfer requires the approval of the Board of Harbor Commissioners and the Mayor.

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CITY ATTORNEY

The Office of the City Attorney has reviewed this report, and the proposed action raises no legal issues at this time.

FIS Approval: MB (initials)
CA Approval: [Signature] (initials)



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