THE PORT OF LOS ANGELES
Executive Director's Report to the Board of Harbor Commissioners

DATE: APRIL 29, 2021

FROM: CARGO MARKETING

SUBJECT: RESOLUTION NO. ______________ - APPROVE PERMANENT ORDER TO AMEND PORT OF LOS ANGELES TARIFF NO. 4, SECTION TWENTY-THREE, "INCENTIVES - GENERAL RULES AND REGULATIONS", ITEM NO 2325, "OCEAN COMMON CARRIER INCENTIVE PROGRAM" UPDATING THE QUALIFYING YEAR PROVISION

SUMMARY:

Staff requests approval of an amendment (Amendment) to Port of Los Angeles (Port) Tariff No. 4 (Tariff) Section Twenty-Three, "Incentives - General Rules and Regulations", Item No. 2325 "Ocean Common Carrier Incentive Program." The proposed amendment would remove the "but not zero" container volume referenced in the Qualifying Year period of the Ocean Common Carrier (OCC) Incentive program (Program), retroactive to September 1, 2018, and remove the qualifying year as an eligibility requirement effective April 1, 2021. The COVID-19 global pandemic has caused unexpected and erratic trading patterns impacting container volumes beyond the control of OCCs. Removing the qualifying year requirement would adjust the program in response to the unforeseen COVID-related decrease in container volume during Fiscal Year (FY) 2020 and incentivize OCCs to drive future container volumes through the Port. The "but not zero" container volume reference in the Qualifying Year did not consider OCCs that had not brought any container volume to the Port in the two years preceding their arrival, nor did it recognize OCCs that had very limited market participation and then dramatically increased container volumes through the Port, effectively "New Market Entrants".

The program will continue to provide eligible OCCs with a financial incentive that could amount to $10.00 per incremental Twenty-foot Equivalent Units (TEU) and a maximum payout of $2,000,000 per OCC per Incentive Period as stated in Tariff No. 4 Item No. 2325.

Payouts to OCCs earned under the terms of the proposed OCC Incentive Program are the financial responsibility of the Harbor Department.

RECOMMENDATIONS:

It is recommended that the Board of Harbor Commissioners:

1. Find that the Director of Environmental Management has determined that the proposed action is administratively exempt from the requirements of the California Environmental Quality Act (CEQA) under Article II Section 2(f) of the Los Angeles City CEQA Guidelines;

2. Approve the amendment to Port of Los Angeles Tariff No. 4 revising Section Twenty-Three, "Incentives - General Rules and Regulations", Item No. 2325 "Ocean Common Carrier Incentive Program", subject to the California Association of Port Authorities' review and approval, and authorize the Executive Director to work with the California Association of Port Authorities to secure this approval or proceed to take independent action in accordance with the California Association of Port Authorities' procedure;

3. Adopt Permanent Order No.__________ to amend Port of Los Angeles Tariff No. 4, Section Twenty-Three, "Incentives - General Rules and Regulations", Item No. 2325 "Ocean Common Carrier Incentive Program";

4. Direct the Board Secretary to transmit to the City Council for approval the Permanent Order and the Ordinance approving and authorizing the Amendments to Port of Los Angeles Tariff No. 4 pursuant to City Charter 653(a);

5. The Board Secretary shall certify to the adoption of this Order by the Board of Harbor Commissioners and shall cause the same to be published in a daily newspaper printed and published in the City of Los Angeles;

6. After the effective date of the Ordinance, transmit the Permanent Order and Ordinance to the Executive Director or his nominee for implementation and posting to the Port of Los Angeles website as regulated by the Federal Maritime Commission; and

7. Adopt Resolution No. _______.

DISCUSSION:

Background and Context

On August 23, 2018, the Board approved the OCC Incentive Program, effective September 1, 2018, allowing eligible OCCs to receive a $10.00 per TEU financial incentive on incremental loaded and empty TEUs, which exceeds Transpacific growth. When the OCC Incentive Program was first introduced, in order for an OCC to be eligible to receive a payout under the OCC Incentive Program, that OCC had to meet certain administrative and data transmission requirements. After these administrative and data transmission requirements were met, an OCC had to also meet certain performance criteria. As part of this performance criteria, an OCC's Incentive Year (current year) performance was evaluated relative to its Baseline Year (1 year prior) and Qualifying Year (2 years prior) thresholds to determine payout eligibility. Lastly, Qualifying Year container volumes must be greater than zero.

For instance, for an OCC to be eligible to earn an incentive, that OCC's FY 2021 container volume performance must, at a minimum, exceed its FY 2020 Baseline Year performance **AND**, the OCC's FY 2020 Baseline Year performance must exceed or be equal to its FY 2019 Qualifying Year performance, which must be greater than zero. The inclusion of the Qualifying Year provision was intended to provide a financial incentive to OCCs that continuously grew their business through the Port.

Following the significant year-over-year decline in global trade observed from January through June 2020 due to the onset of the COVID-19 pandemic, FY 2020 container volumes handled by OCCs, through no fault of their own, declined relative to FY 2019. OCCs have recovered a significant portion of the business lost in the first half of calendar year 2020. From July through December 2020, ten OCC's have grown their business at the Port in excess of Transpacific growth. None of these ten OCC's would be eligible for an incentive payout in FY 2021 because their FY 2020 Baseline Year performance did not exceed their respective FY 2019 Qualifying Year performance.

On April 1, 2021, the Board approved the amendment to the OCC Incentive Program removing the Qualifying Year performance provision adjusting the program in response to the unforeseen COVID related decrease in container volume during FY2020. Effective April 1, 2021 OCCs Incentive Year (current year) performance will now be compared to the Baseline Year (1 year prior) container volume, less Transpacific growth percentage volume, to determine payout eligibility.

From the onset, the intent of this Program was aimed at attracting additional cargo volumes to the Port above the Transpacific trade growth percentage. Staff is constantly reviewing the effectiveness of the program and looking at ways that are beneficial to strengthening the Port's competitive position in Transpacific trade.

Following the approval of the recent amendment to the OCC incentive program which removed the Qualifying Year requirement effective April 1, 2021, it was discovered that "New Market Entrants" that started moving container volumes through the Port after the effective date of the OCC incentive program were not able to receive the same benefits existing OCCs were receiving at the Port. The reference to "but not zero" container volume in Tariff No. 4 (Tariff) Section Twenty-Three, Item No. 2325 "Ocean Common Carrier Incentive Program and Eligibility Requirements, means that an OCC has to have moved a minimum of **"one"** container through the Port during the qualifying year. "New Market Entrants" are effectively ineligible to receive an incentive, which is contrary to the intent of the program.

In fairness, “New Market Entrants” should be able to receive the same benefits existing OCCs received when the program was first introduced; the Qualifying Year requirement did not apply for all OCC’s during the initial Incentive Period of the Program. This can be achieved with the removal of the “but not zero” container volume reference in the Qualifying Year period effective retroactively to September 1, 2018.

Two “New Market Entrants” are particularly impacted as a result of this “but not zero” container volume reference. Both OCCs had anticipated receiving the benefit of this OCC Incentive program and made considerable efforts to ensure data was provided into the Port Optimizer to ensure they would be eligible for this incentive. Moreover, one OCC in particular relied on the OCC Incentive Program as part of the terminal selection evaluation.

The removal of the “but not zero” reference would be retroactively effective to September 1, 2018.

Staff estimates that the April 1, 2021 approved Tariff amendment eliminating the Qualifying Year provision would result in shipping line earned payouts between $3.5 and $4.0 million from April 1, 2021 to June 30, 2021. In addition, the removal of the “but not zero” container volume provision of this Program would allow one OCC to earn $182,225.00 for their performance ending in Fiscal Year 2020, and another OCC would receive the maximum incentive amount of $2 million upon completion of Fiscal Year end 2021.

All other terms and conditions of the current OCC Incentive Program would remain in effect.

<u>Need for Approval</u>

A separate action recommends Board adoption of a Temporary Order within its Los Angeles City Charter authority to approve changes to Tariff No. 4, to be effective for a period not to exceed 90 days. This action for Board and City Council adoption of a Permanent Order (Transmittal 1) and Ordinance (Transmittal 2) are required under the Charter to make changes to Tariff No. 4 (Transmittal 3) beyond the Temporary Order’s 90-day effective period.

ENVIRONMENTAL ASSESSMENT:

The proposed action is approval of a Permanent Order to amend Port of Los Angeles Tariff No. 4 OCC Incentive Program, to remove the “but not zero” container volume reference and the Qualifying Year provision, which is an administrative activity. Therefore, the Director of Environmental Management has determined that the proposed action is administratively exempt from the requirements of CEQA in accordance with Article II, Section 2 (f) of the Los Angeles City CEQA Guidelines.

FINANCIAL IMPACT:

As was stated in the April 1, 2021 Board report on this Program, approval of the proposed Amendment would eliminate the Qualifying Year performance provision associated with the current OCC Incentive Program, effective April 1, 2021. Based upon a proposed effective date of April 1, staff estimates that FY 2021 funding of $4,000,000 will be required in order to meet anticipated payouts under the amended OCC Incentive Program.

Payouts related to incentivized OCC performance observed from April 1, 2021 through June 30, 2021, will not be recorded until FY 2022 once all container counts are finalized and incentive payout calculations can be completed. Therefore, staff will request that $4,000,000 be included in the FY 2022 Budget within Account 59961 (Container Incentives), Center 0422, Program 000, subject to Board approval. Funding for future years will be requested as part of the annual budget adoption process, subject to Board approval.

In the event that removal of the Qualifying Year performance provision results in a one percent increase in the Port's TTM Market Share, staff estimates that revenues could increase by $6,290,000 per year.

Approval of the additional amendment would remove the "but not zero" reference and enable New Market entrants to receive the same benefit of its volume not subject to the qualifying year provision of the program as it originally existed. Staff estimates that removing the "but not zero" reference would result in two shipping lines earning a payout of $2,182,225.00.

SUBJECT: PERMANENT ORDER TO AMEND TARIFF NO. 4, SECTION TWENTY-THREE, ITEM NO. 2325

CITY ATTORNEY:

The Office of the City Attorney has reviewed and approved the proposed Order and Ordinance as to form and legality.

TRANSMITTALS:

1. Permanent Order
2. Ordinance
3. Tariff No. 4 Section Twenty-Three, Item No. 2325

FIS Approval: MB
CA Approval: JS

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