

DATE: MAY 18, 2011

FROM: FINANCE DIVISION

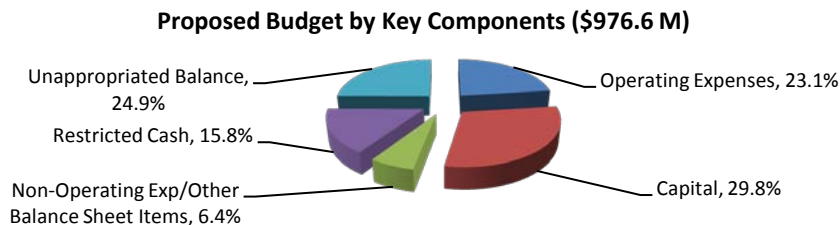
**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

SUMMARY:

Transmitted herewith is the proposed Fiscal Year (FY) 2011/12 Annual Budget for revenues, expenses, and capital for the City of Los Angeles Harbor Department (Harbor Department or Port) - see Transmittal No. 1. This proposed budget reflects the Harbor Department's effort to balance its Strategic Priorities with the costs associated with implementing them, along with the anticipated amounts of revenues. The proposed budget is generally consistent with the preliminary information provided to the Board of Harbor Commissioners (Board) during the budget hearing held on March 17, 2011; significant changes subsequent to the hearing are delineated herein.

The total proposed budget of \$976,585,403 for Fiscal Year 2011/12 represents a \$67 million or 7.4% increase from the \$909,585,784 Fiscal Year 2010/11 Adopted Budget (Adopted Budget) and a \$23.3 million or 2.3% decrease from the \$999,789,126 estimated expenditures for the current fiscal year, primarily reflecting the realignment of funding capital projects with construction needs.

Of the total budget, the key components are (and as depicted in the following chart):



- \$291.0 million or 29.8% of the total budget for Capital;
- \$243.4 million or 24.9% as the Unappropriated Balance carried forward;
- \$225.6 million or 23.1% for Operating Expenses;
- \$154.2 million or 15.8% as Restricted Cash (including future commitments); and
- \$62.4 million or 6.4% as the Non-Operating Expenses and other balance sheet items (i.e., bond issuance costs).

SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET

RECOMMENDATION:

It is recommended that the Board of Harbor Commissioners:

1. Adopt the proposed Fiscal Year 2011/12 Annual Budget for the Harbor Department and appropriate funds in accordance therewith (see Transmittal No. 1);
2. Authorize the Executive Director, or designee, to make any technical adjustments consistent with Board action(s) to the Fiscal Year 2011/12 budget documents, so as to provide for the implementation of this budget; and
3. Adopt Resolution No. _____.

DISCUSSION:

The proposed FY 2011/12 Annual Budget was formulated based on the Harbor Department's Strategic Plan and proposed Strategic and Budget Priorities, financial metrics based on the Harbor Department's Financial Policies, and input from the Board.

Proposed Strategic and Budget Priorities – At the onset of the budget process, proposed Budget Priorities were developed based on the Harbor Department's current Strategic Plan. Through ongoing strategic planning discussions at the senior management level, this plan also includes input from the divisions and the Board, resulting in three broad Strategic Priorities: Competitive Operations, Strong Relationships, and Financial Strength. The strategic planning process continues to evolve, which subject to Board approval will ultimately yield a new five-year strategic plan with performance metrics.

The proposed Budget Priorities for FY 2011/12 are centered on long-term planning – both operationally and fiscally, internal and external communication and staff development, and are categorized by Strategic Priority as follows:

- Competitive Operations
 - Consolidate and Institutionalize the Port's Overall Master Plan – With changing technology, cargo trends, and world-wide developments in the maritime industry, the Port master plan will be updated to ensure that development plans continue to address Port user needs and public concerns, as well as respond to competition from other U.S. seaports.

SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET

- Strong Relationships
 - Improve Communication – Efforts will continue to improve department-wide communication with an emphasis on understanding workforce strengths and values, which will help foster effective internal communication and, at the same time, align the Port's internal identity with its external "brand" identity wherever possible.
 - Develop an Overall Port Staff Development Training Curriculum – An overall training curriculum will be developed as part of the Harbor Department's ongoing efforts to utilize and develop resources in the most efficient and effective manner possible.
- Financial Strength
 - Update Property Leases – Emphasis will be placed on updating Port property leases while ensuring tenant conformance with existing terms.
 - Seek Diversification of Funding Sources and Improve Financial Efficiency and Cost Control – In order to maintain financial strength, continued focus will be placed on seeking additional grants and other funding sources, as well as financial efficiencies and cost controlling measures.

Financial Metrics – In addition to the proposed Budget Priorities, the proposed budget was established based on maintaining the following financial metrics:

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

Board Input – A special Board meeting was held on March 17, 2011 to review the preliminary proposed budget. During this meeting, the Board discussed the proposed budget with and provided input and guidance to the Harbor Department's Executive Director and senior management.

Subsequent to the March 17, 2011 meeting, certain events occurred resulting in the following significant changes: the Operating Revenue budget was decreased by \$5.7 million due to the discontinuance of a shipping line calling at a Port terminal; the Operating Expense budget was increased by \$532 thousand as a result of the City of Los Angeles' labor union negotiations; the Non-Operating Expense budget was decreased by a net \$19.2 million to primarily reflect

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

capitalization of \$29 million in imputed interest expense (and at the same time, this added to capitalized expenditures) and a reserve for the Alameda Corridor Transportation Authority; and the Capital Improvement Program budget was increased by \$20.5 million due to timing adjustments of projects. These changes in part resulted in a \$41.8 million increase in Net Income when compared to the FY 2010/11 Adopted Budget and a \$16.4 million decrease when compared to current fiscal year estimates.

Year-to-Year Results – The major drivers to the variance between FY 2010/11 estimates and FY 2011/12 proposed budget are Rentals revenue, Clean Truck Program revenues and expenses, Salaries and Benefits, Outside Services, City Services, and Non-Operating revenues and expenses. Comparisons of the proposed budget with FY 2010/11 estimates and Adopted Budget are as follows:

**FY 2011/12 Proposed Operating/Non-Operating Budget
Comparisons with FY 2010/11 Estimates and Adopted Budget**

(000s)	Adopted Budget	Estimates	Proposed Budget	Δ \$	Δ %	Δ %
	FY 2010/11	FY 2010/11	FY 2011/12	Estimate to Proposed Budget	Estimate to Proposed Budget	Adopted to Proposed Budget
Operating Revenues						
Shipping Services	\$320,459	\$348,170	\$348,122	(\$47)	0.0%	8.6%
Rentals	45,847	43,908	49,533	\$5,625	12.8%	8.0%
Royalties and Fees	2,360	2,685	2,693	\$8	0.3%	14.1%
Clean Truck Fees	2,655	6,488	2,040	(\$4,448)	-68.6%	-23.2%
Other Operating	2,034	2,975	2,984	\$9	0.3%	46.7%
Total Operating Revenues	373,354	404,226	405,373	\$1,147	0.3%	8.6%
Operating Expenses						
Salaries & Benefits	108,210	101,125	110,631	\$9,506	9.4%	2.2%
Marketing and Public Relations	3,913	3,741	3,955	\$214	5.7%	1.1%
Travel	886	702	873	\$170	24.3%	-1.5%
Outside Services	37,277	30,714	36,598	\$5,883	19.2%	-1.8%
Materials & Supplies	7,410	7,128	7,311	\$183	2.6%	-1.3%
City Services	38,928	38,736	40,325	\$1,589	4.1%	3.6%
Allocations to Capital	-7,000	-6,762	-6,210	\$552	-8.2%	-11.3%
Other Operating Expenses	31,652	31,978	32,136	\$158	0.0%	1.5%
Total Operating Expenses	221,276	207,362	225,619	\$18,257	8.8%	2.0%
Income from Operations before Depreciation	152,078	196,864	179,754	(\$17,110)	-8.7%	18.2%
Depreciation	-89,045	-89,365	-91,814	(\$2,449)	2.7%	3.1%
Income from Operations	63,032	107,499	87,940	(\$19,559)	-18.2%	39.5%
Non-Operating Revenues	17,578	17,230	30,031	\$12,801	74.3%	70.8%
Non-Operating Expenses	-37,362	-23,219	-32,958	\$9,739	-41.9%	-11.8%
Net Income	\$43,248	\$101,510	\$85,013	(\$16,497)	-16.3%	96.6%

Note: Figures in this chart may differ from the Comparative Statement of Operations (Transmittal No. 1) due to rounding.

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

Operating Revenue Budget – Proposed Operating Revenues are budgeted to be \$405.4 million and are generally flat compared to the current fiscal year estimate of \$404.2 million. Proposed Shipping Services revenue are primarily driven by continued year-on-year TEU (Twenty-foot Equivalent Unit) growth, but tempered by tenant incentives and the discontinuance of The Containership Company (TCC) trans-Pacific line. Budgeted TEU volume levels of 8.07 million for next fiscal year is an 1.7% increase from current year estimates based on input received from the Business Development Bureau and their communication with our tenants. The projected volume levels are those that we have not seen since Fiscal Year 2007/08 but show a positive upward trend compared to the years since the economic downturn. Rentals income is budgeted to increase by \$5.6 million compared to current fiscal year estimates as fixed land rentals are projected to increase as a result of new business. This increase is, for the most part, offset by a budgeted decrease of \$4.4 million 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 Fiscal Year 2010/11 Adopted Budget, proposed Operating Revenues are \$32 million or 8.6% higher primarily due to the increase in cargo volumes and Rentals income.

Operating Expense Budget –The Operating Expense budget of \$225.6 million represents an \$18.3 million or 8.8% increase from the current fiscal year estimate and a \$4.3 million or 2.0% increase from the FY 2010/11 Adopted Budget. Salaries and Benefits continue to be the largest contributors to expenses, comprising 49% of the Operating Expense budget and the main cause of the increase in Operating Expenses from the current fiscal year estimate and Adopted Budget. Outside Services also contributed towards the increase in Operating Expenses from the current fiscal year estimate, while it remained relatively flat to the Adopted Budget. Other expense categories remained relatively flat or slightly increased from both the current fiscal year estimates and Adopted Budget.

Proposed Salaries and Benefits increased by 9.4% or \$9.5 million from the current fiscal year estimate and 2.2% or \$2.4 million from the FY 2010/11 Adopted Budget. The primary reasons for the year-to-year increase are attributed to:

- Slowed Hiring – While the level of proposed authorized positions (989) remains flat to the Adopted Budget, the projected headcount in the current fiscal year has been lower than anticipated as the pace of hiring to fill vacancies has slowed resulting in a \$1.1 million increase in proposed Salaries from current fiscal year estimates. The department had projected a full headcount of 989 in the current fiscal year and assumed no attrition.

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

However, at April 1, 2011, headcount was 955 and it is projected that the department will end the fiscal year with an average headcount of 945. A 3% attrition rate has been included in the proposed budget, which is equivalent to a projected average headcount of approximately 960 employees.

- **Salary Adjustments** – Based upon the recent ratification by most labor groups of the agreement between the City of Los Angeles and the Coalition of Los Angeles City Unions (Coalition), member employees at the Harbor Department will receive a Cost of Living Allowance (COLA), with future step increases frozen. Non-ratifying Coalition members will receive both the COLA and step increases. This results in an increase to Salaries and Benefits of \$3.2 million from the current fiscal year estimate.
- **Pension and Health Contribution Increases** – The Harbor Department's contribution rates to the Los Angeles City Employees' Retirement System (LACERS) and the Los Angeles Fire and Police Pensions (LAFPP) have increased by 3.26 and 5.03 in percentage points respectively, resulting in an approximate \$4.1 million increase in employee benefits costs compared to current fiscal year estimates. Health benefits for Civilian personnel have increased by \$744 per employee and \$872 per sworn employee, resulting in a \$600 thousand increase compared to current fiscal year estimates. The proposed budget reflects the impact of the contribution rate increases on a projected average headcount of approximately 960 employees, after taking into consideration a 3% attrition rate.

Proposed Marketing and Public Relations expenses include department-wide marketing activities such as customer outreach and sponsorships. Compared to the current fiscal year estimates, the increase is \$214 thousand or 5.7% as promotional expenses were increased primarily for the International Association of Ports & Harbor (IAPH) conference planning costs. It is budgeted to remain relatively flat compared to Adopted Budget.

Proposed Travel increased by \$170 thousand or 24.3% compared to FY 2010/11 estimates as increased travel is anticipated for marketing; less spending occurred this fiscal year as the Director of Business and Trade Development for whom the travel was intended was not hired until approximately mid-year. Compared to the current year Adopted Budget, the proposed budget represents a decline of \$13 thousand or 1.5% as non-essential travel was reduced.

Proposed Outside Services are remaining generally flat to the Adopted Budget. During this budget process, efforts were made to align the budgeted amount with spending. The proposed Outside Services budget of \$36.6 million is within the

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

Harbor Department's average range of spending over the past 6 years. Spending in this expense category is budgeted to increase by \$5.9 million or 19.2% compared to FY 2010/11 estimates primarily due to an increase in costs for environmental services (\$1.8 million), cruise terminal facility operator (\$1.2 million), Enterprise Resource Planning backfill consultants (\$800 thousand), new facilities maintenance (\$600 thousand), Port master plan update (\$200 thousand), and POLA (Port of Los Angeles) University curriculum development (\$150 thousand). Additionally, approximately \$1.5 million in new environmental remediation and baseline assessment expenses are included in the FY 2011/12 proposed Operating Budget. Prior to last fiscal year, remediation and baseline assessment expenses for capital projects were capitalized and funded in the Capital Improvement Program budget. Due to a ruling under GASB (Governmental Accounting Standards Board) 49, expenses for environmental remediation purposes (including baseline assessments) are considered operational costs.

Proposed Materials and Supplies spending are budgeted to increase by \$183 thousand or 2.6% compared to FY 2010/11 estimates due to increased expenses for new facilities. Compared to Adopted Budget, expenses are budgeted to decrease by \$99 thousand or 1.3% due to better control on spending for administrative and operating supplies.

Proposed City Services budgeted expenses are higher compared to both FY 2010/11 estimates and Adopted Budget by \$1.6 million or 4.1% and \$1.4 million or 3.6% respectively. The increase is attributed to increases in Fiscal Year 2010/11 "true-up" costs for Fire Services payable next fiscal year, indirect charges for the City Treasurer that were not budgeted in the current fiscal year, and additional staffing for the City Attorney.

Proposed Other Operating Expenses are relatively flat when compared to FY 2010/11 estimates. Compared to the current Adopted Budget, expenses in this category are \$484 thousand or 1.5% higher primarily due to increases in utilities for new facilities (\$986 thousand), litigation (\$2.9 million) and Clean Air Action Plan incentives (\$1.5 million), partially offset by a decrease in Clean Truck Program expenses (\$5 million).

Allocations to Capital, when compared to current year estimates, is budgeted to decrease by \$552 thousand or 8.2% as the level of proposed Capital Improvement Program expenses are lower than current fiscal year estimated spending.

Non-Operating Budget – Non-Operating Revenues are budgeted to increase by \$12.8 million or 74.3% from current fiscal year estimates due primarily to an increase in Federal grants by \$3.8 million and pass-through receipts by \$8.9

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

million. Non-Operating Expenses are budgeted to increase by \$9.7 million or 41.9% compared to current year estimates, due primarily to an increase in Federal pass-through grant receipts disbursements by \$8.9 million, a \$9.7 million reserve set aside in anticipation of a shortfall for the Alameda Corridor Transportation Authority (ACTA), and one-time transactions reflected in the current fiscal year estimates. These include higher capitalization of imputed interest expense as well as an \$8.3 million Loss on Disposal of Fixed Assets for the loss on the sale of POLA High School.

Capital Budget – To meet the future needs of the Harbor Department and to enhance job creation and economic development, a Capital Budget of \$291 million has been 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:

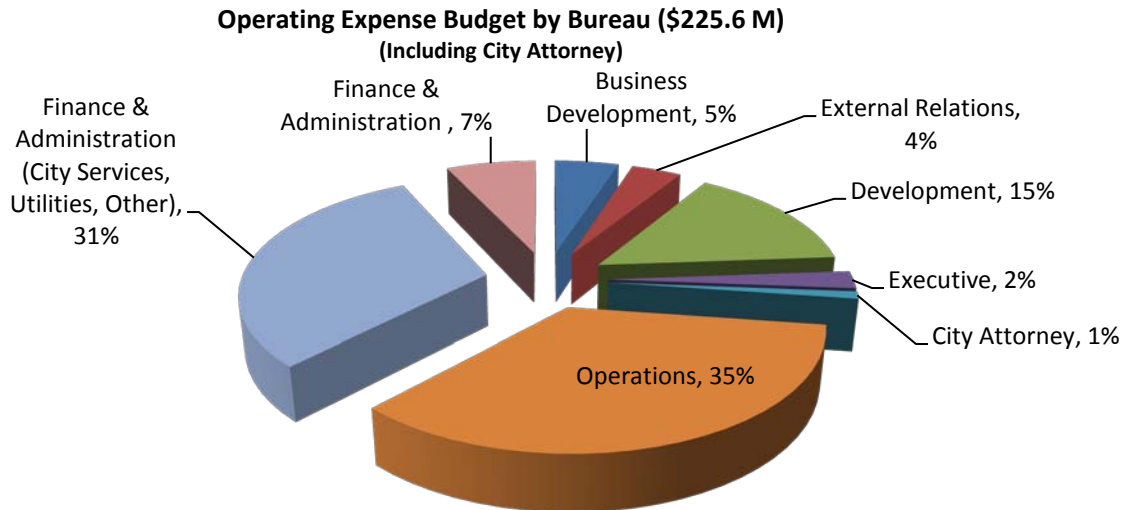
- \$229.7 million Capital Improvement Program;
- \$48.1 million in Allocations to Capital (for overhead and other expenses); and
- \$13.3 million for Capital Equipment.

The Capital Improvement Program (CIP) component of the Capital Budget proposed at \$229.7 million represents a \$16.7 million or 6.8% decrease from the estimated current year expenditure of \$246.4 million. Compared with the current year Adopted Budget (Adjusted) of \$269.5 million, this is a \$39.8 million or 14.8% decrease. 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 seeks to maintain a minimum debt service coverage ratio of 2.0X (see Transmittal No. 1 for a complete listing of projects). At this time, the Department does not anticipate any additional borrowings. However, depending on financial market conditions and the timing of spending, borrowings, if any, may vary and are subject to Board approval.

Key Components of the Operating Expense Budget by Bureau – The Harbor Department is comprised of 6 Bureaus and 18 Divisions. The highest percentage of the Operating Expense Budget of 35% is allocated to the Operations Bureau, with the next highest of 15% appropriated to the Development Bureau. It should be noted that the Finance and Administration Bureau also administers the budget of slightly over \$40 million in payments made through the City Services bill to the City of Los Angeles and Inter-Departmental Orders for payments for services rendered, such as fire services and maintenance of grounds by the Department of Recreation and Parks; it also administers budget for basic utilities and other department-wide administrative expenses. The following chart provides a percentage breakdown of the

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

Operating Expense Budget by Bureau. (Details relating to all Bureau and Division budgets were previously provided at the March 17, 2011 Board meeting.)



Proposed Budget Priorities Funding Highlights – Funding highlights of proposed Budget Priorities initiatives are as follows:

- Consolidate and Institutionalize the Port's Overall Master Plan – Initiatives to comprehensively consolidate planning processes and institutionalize land use priorities include:
 - Terminal Island land use study (\$110 thousand); and
 - Commencement of an Environmental Impact Report (EIR) (\$500 thousand).
- Improve Communication – Efforts to improve Department-wide communication include:
 - Internal communications initiatives and survey (\$185 thousand); and
 - Development of a Government Relations Strategy (utilizing in-house staffing).
- Develop an Overall Port Staff Development Training Curriculum – A POLA University curriculum will be developed (\$150 thousand).
- Update Property Leases – Property leases will be brought up to date (utilizing in-house staff).

**SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET**

- Seek Diversification of Funding Sources and Improve Financial Efficiency and Cost Control - Initiatives include:
 - Grant receipts budgeted at \$55.1 million:

By Funding Source:	By Project Category:	By Function:
Federal Grants: \$46.9 million	Capital: \$37.0 million	Security: \$40.7 million
State Grants: \$ 8.2 million	Operating: \$18.1 million	Transportation: \$11.3 million
		Environmental: \$ 3.1 million

- A more rigorous grants management program (\$100 thousand);
- Strengthening our government relations and advocacy services (\$540 thousand);
- Launching Phase I of the Enterprise Resource Planning (ERP) implementation, which will replace the Harbor Department's mainframe financial system (\$6.4 million); and
- Seeking Federal Railway Administration (RRIF) and other funding sources (utilizing in-house staff).

ENVIRONMENTAL ASSESSMENT:

The proposed action is approval of the Fiscal Year 2011/12 Los Angeles Harbor Department budget. The Resolution is administrative in nature; all projects potentially financed through the Resolution would require separate Board approval. As such, the Director of Environmental Management has determined 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.)

ECONOMIC BENEFITS:

The proposed FY 2011/12 Annual Budget supports the creation of over 5,000 jobs within the region as follows:

SUBJECT: RESOLUTION NO. _____ - FISCAL YEAR 2011/12
PROPOSED ANNUAL BUDGET

	Actual FY 2010	Estimates FY 2011	Proposed Budget FY 2012
Direct Jobs at the Port	962	945	989
Jobs Created by the Port – Capital Spending	2,827	5,781	3,352
Jobs Created by Other Port Spending	<u>839</u>	<u>809</u>	<u>727</u>
Total Jobs Created	4,628	7,535	5,068

FINANCIAL IMPACT:

Approval of the proposed FY 2011/12 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.

CITY ATTORNEY:

There are no legal issues to address at this time.

TRANSMITTALS:

1. Fiscal Year 2011/12 Annual Proposed Budget

FIS: KP
CA: TR


KARL K.Y. PAN
Chief Financial Officer


MOLLY CAMPBELL
Deputy Executive Director

APPROVED:


for GERALDINE KNATZ, Ph.D.
Executive Director

KP:EY:ey
Author: E. Yoshimura