

DATE: NOVEMBER 15, 2013

FROM: EXECUTIVE OFFICE

SUBJECT: RESOLUTION NO. _____ - (1) 2014 OPERATING BUDGET FOR HCBF; (2) J.P. MORGAN PRIVATE BANK AS INDEPENDENT FINANCIAL MANAGER OF PCMTF; AND (3) HARBOR DEPARTMENT SIGNATORIES FOR PCMTF DISBURSEMENTS

SUMMARY:

The Port Community Mitigation Trust Fund (PCMTF) was established by the City of Los Angeles Harbor Department (Harbor Department) for the purpose of funding projects that will protect, improve and assess public health by off-setting past, present, and future off-port impacts from port operations for the communities of Wilmington and San Pedro. The Harbor Community Benefit Foundation (HCBF), a nonprofit organization established to operate the PCMTF, is required to submit a detailed budget and report to the Board of Harbor Commissioners (Board) regarding its administrative needs and grant allocations. On October 18, 2013, the proposed HCBF Calendar Year (CY) 2014 Operating Budget was approved by HCBF's Board of Directors. Staff recommends the Board approve HCBF's proposed budget with the condition that HCBF provides the Board prior notice of any reallocation within the HCBF budget that exceeds 10% of the total annual budget.

For calendar year 2014, HCBF requests approval of an operating budget of \$511,700, and release of \$475,000 from the PCMTF, which combined with HCBF's projected 2013 surplus of \$36,700, will provide funds for the requested operating budget for 2014. Additionally, to improve fiscal management of the PCMTF, staff also recommends the Board concur with the HCBF Board's selection of J.P. Morgan Private Bank (JPMorgan) as the new independent financial manager to receive, manage, and disburse funds from the PCMTF, and approve Harbor Department signatories for disbursements from PCMTF at JPMorgan.

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RECOMMENDATION:

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

1. Approve the Harbor Community Benefit Foundation Calendar Year 2014 Operating Budget of a not-to-exceed amount of \$511,700 with the condition that Harbor Community Benefit Foundation provide the Board of Harbor Commissioners prior notice of any reallocation within the Harbor Community Benefit Foundation budget that exceeds 10% of the total annual budget;
2. Authorize the Executive Director or designee to execute a joint letter with Harbor Community Benefit Foundation to approve the distribution of funds in one lump sum payment of \$475,000 from the California Community Foundation to the Harbor Community Benefit Foundation subject to the same condition;
3. Adopt Resolution No. _____ approving JPMorgan as the authorized independent financial manager of the Port Community Mitigation Trust Fund in accordance with Operating Agreement Section 5D; and designating the Harbor Department Executive Director and Deputy Executive Directors as signatories for disbursements from the newly created Port Community Mitigation Trust Fund account at JPMorgan Private Bank;
4. Authorize the Executive Director or designee to execute a joint letter with Harbor Community Benefit Foundation to approve the transfer of all remaining funds held in the trust fund, net of fees, in one lump sum payment from the California Community Foundation to JPMorgan Private Bank; and
5. Adopt Resolution No. _____.

DISCUSSION:

Background/Context - On December 6, 2007, the Board certified the Final Environmental Impact Report (EIR)/Environmental Impact Statement (EIS) for the Berth 136-147 (TraPac) Container Terminal and approved the TraPac project. Subsequent to project approval, certain entities, individuals, and organizations (TraPac Appellants) appealed the certification/project approval to the City Council under the provisions of the California Environmental Quality Act (CEQA). On April 2, 2008, the Board approved a Memorandum of Understanding (TraPac MOU) between the City of Los Angeles Harbor Department and the TraPac Appellants, which provides for the settlement of the appeal and the creation and funding of a Port Community Mitigation Trust Fund to be

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administered by a nonprofit entity (Transmittal 1). HCBF is the nonprofit organization established to provide oversight and administration of the PCMTF.

On October 20, 2012, the Board approved the Operating Agreement to the TraPac MOU (Operating Agreement), between the Harbor Department, TraPac Appellants, and HCBF, which provided specific details regarding the PCMTF and the role and responsibilities of HCBF (Transmittal 2). While the TraPac MOU has expired, the terms of the Operating Agreement remain in effect until May 2016, when the projects listed in Exhibit B of the TraPac MOU are projected to be completed.

Through the Operating Agreement, the Harbor Department provided funds to establish the PCMTF with California Community Foundation (CCF) for the purpose of funding appropriate mitigation projects and grants for the communities of Wilmington and San Pedro. As of September 30, 2013, the Harbor Department has made a total contribution of \$9,840,313, of which \$7,780,671 has not been allocated.

Harbor Community Benefit Foundation Operating Budget – HCBF’s mission is to assess, protect, and improve the health, quality of life, aesthetics, and physical environment of the harbor communities of San Pedro and Wilmington. In accordance with Section 5F of the Operating Agreement, HCBF must submit a detailed budget and report to the Board on an annual basis regarding its administrative needs and requirements. The Board shall exercise its independent judgment as to the requested budget, may not arbitrarily or unreasonably decline a budget request, and shall provide written findings relating to reasons for any rejection. Upon Board approval, funds may be transferred from the PCMTF to HCBF for the purposes outlined in the approved annual budget.

Calendar Year 2012 Operations – In the foundation’s 2012 fiscal year, which follows the calendar year, total operating expenses were \$839,312 of which \$658,000 went to program expenses and \$181,312 related to management and general expenses (Transmittal 3). In percentage terms of program services expenses to total expenses, in its first year of operations, the ratio stood at 78.4%, which is better than the standard ratio of 66.7% calculated by non-profit monitoring agency Charity Navigator. .

The approved operating budget for 2013 was \$499,200, of which \$462,800 is projected to be spent (Transmittal 4). Budget savings in 2013 can be attributed to cost controls regarding legal, audit, strategic planning, and advisory consultant fees. Additionally, HCBF hired staff gradually over the year, based on the progress of the organization, creating a surplus of \$36,700.

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Although there was a budget surplus in 2013, HCBF foresees the need of a 2.5% budget increase to accommodate a fully staffed organization and the services required to operate well established grant and study programs. The proposed HCBF CY 2014 Operating Budget total is \$511,700. Upon Board approval \$475,000 will be released from the PCMTF and transferred to HCBF. This amount, combined with HCBF's 2013 projected surplus of \$36,700, will constitute the funds for the total requested HCBF CY 2014 Operating Budget (Transmittal 5).

HCBF has awarded \$1,300,000 in grant funding to date. An additional \$550,000 in grants is pending Board approval and will be presented at a future Board meeting. If approved, a total of \$1,850,000 in Health Care and Community Benefit Grants will have been awarded by HCBF.

Staff recommends approval of the HCBF CY 2014 Operating Budget in the amount of \$511,700, with the condition that HCBF provide the Board prior notice of any reallocation within the HCBF operating budget that exceeds 10% of the total annual operating budget. This same condition was imposed by the Board's approval of HCBF CY 2013 Operating Budget on February 7, 2013; however, to date, no such request from HCBF has come to the Board.

Update on Accounting for Non-Tidelands Activities of HCBF - In March 2012, the Board imposed the condition that the Office of the City Attorney and HCBF work together to determine a method for accounting for any non-Tidelands activities of HCBF. This accounting is needed to ensure that the Tidelands-restricted funds released to HCBF for its operating budget are not used for non-Tidelands purposes, while still allowing HCBF to engage in non-Tidelands activities using separate non-Tidelands funds.

HCBF has since hired law firm Jenkins & Hogin, LLP as its legal counsel. Harbor Department staff and the Office of the City Attorney have discussed the accounting of non-Tidelands activities with HCBF and its counsel multiple times and have also included staff from the State Lands Commission (SLC) in some discussions. The calculation of non-Tidelands activities and the factors, on which it will be based, have yet to be formalized. Prior to bringing a formal resolution for Board consideration, the following describes the concepts under consideration. This version of concepts under consideration was shared with SLC.

Non-Tidelands Accounting Concepts to be Considered:

- 1) HCBF's annual estimated future projections of non-Tidelands administrative activities, delivered prior to commencement of the fiscal year. When HCBF makes its annual operating budget request to the Board, it shall provide an

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estimated projection of the percentage of its non-Tidelands administrative activities for the upcoming year. HCBF may only request release of funds from the PCMTF equal to its total proposed operating budget reduced by the projected percentage of non-Tidelands activities. If non-Tidelands activities are estimated to total 5% or less of the budget total request, these activities will be deemed de minimis and will not reduce the allowable budget request.

- 2) Annual reconciliation based on actual non-Tidelands administrative activities, delivered following the conclusion of each fiscal year audit. In conjunction with preparation of its annual audit by its outside auditing firm, HCBF will report its actual percentage of non-Tidelands administrative activities from the current year, and reconcile it with the previous projection. The amount of this reconciliation shall be taken into account as a debit or credit, as the case may be, calculated into the amount of annual operating budget funds released from the PCMTF to HCBF for the following year.

In accordance with the proposed methods of accounting non-Tidelands activities, HCBF performed an internal audit of their CY 2013 administrative activities and determined that there were no non-Tidelands expenditures. This information was shared with the SLC, who completed review of the HCBF audit report and concurred there were zero non-Tidelands related expenditures in 2013. HCBF has also provided SLC with a forecast of zero non-Tidelands related expenditures for CY 2014.

PCMTF Independent Financial Manager – The Operating Agreement provides that CCF or other appropriate independent financial manager manage the PCMTF funds. CCF is a public nonprofit organization focused on philanthropy and civic engagement efforts within the County of Los Angeles. As such, the CCF manages the CCF Community Initiatives Fund (CIF) in which the PCMTF was originally established. Under a Restricted Fund Services and Management Agreement among the Harbor Department, HCBF and the CCF (Management Agreement), the CCF has acted as the escrow agent responsible for reporting account activity and for the receipt, investment and disbursement of PCMTF funds, as “independent financial management” under Section 5D of the Operating Agreement.

Under the terms of the Management Agreement, CCF was able to charge a combination of fees for management of the PCMTF and has resulted in an approximate loss of \$85K in principle to date. The CCF charges both an administrative and an investment manager fee. Since inception these charges total \$14,984 date. The funds of the PCMTF were invested in a “Short-Term Pool” where the annual yield was not enough to absorb the fees charged (Transmittal 6). For year-to-date June 30, 2013, the PCMTF funds at the CCF generated income totaling \$22,179 while paying fees of

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\$25,400, incurring a loss of \$3,221. In addition, there was a loss in net asset value of another \$15,277 over the same period given the rise in interest rates generating an overall net loss of \$18,498 over the period.

HCBF felt the PCMTF would be better served with a more aggressive investment strategy. HCBF made efforts to move the PCMTF to a higher risk investment pool and renegotiate the administrative fees and language regarding other allowable service fees stipulated in the Management Agreement. CCF was unable to change the investment pool due to HCBF's billing structure and unwilling to reduce any fees or change the terms of the Management Agreement. As such, HCBF was compelled to seek an alternate independent financial manager.

Section 5D of the Operating Agreement requires that CCF "or other appropriate financial manager" must manage the PCMTF funds, but does not specify a process for selection of an alternate to CCF, other than that "the City and Appellants shall work cooperatively" to transfer funds to the independent financial manager.

On August 13, 2013, the Harbor Department and HCBF jointly sent a 60-day notice to CCF to terminate the Management Agreement. HCBF formed an ad hoc committee consisting of their Executive Director and Board of Directors' Chairman and Treasurer to research alternate "independent financial management" providers. The ad hoc committee evaluated several options and recommended two final candidates: 1) Liberty Hill Foundation and Morgan Stanley; and 2) J.P. Morgan Private Bank, for final consideration by their Board of Directors.

The HCBF selected JPMorgan given its responsiveness and ability to provide a higher risk investment portfolio. Based on historical yields the JPMorgan estimates an annual yield of \$174,000, exclusive of fees (Transmittal 7), which are a blended 0.70%. Net of fees then, if the yields hold, annual net revenues would be \$121,500. The proposal from JPMorgan creates an investment portfolio comprised of six different JPMorgan managed mutual funds. PCMTF money would be allocated among the different funds. The funds range from conservative short duration U.S. government instruments, HLLVX, to a much higher risk fund that invests in foreign exchange, EXGSX. The largest holdings of EXGSX are in Indonesian and Mexican currencies. Generally, when undertaking higher risk, the opportunity for greater return as well as greater losses exists. As an example, in the fund JPHSX, which invests in floating rate bonds, the year-to-date return through the end of October is 4.74% while the return for EXGSX for the same period is a loss of 2.24%. In comparing the proposed investment to the investment at CCF, the most appropriate fund comparison at JPMorgan would be HLLVX, which has a similar profile to the CCF short-term portfolio. The return on both on a year to date basis are almost identical at about 0.08%. Note further that the fee

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structure at the CCF is approximately 0.51% on the funds invested while the fee for HLLVX is 0.55%.

On October 18, 2013, the HCBF Board of Directors approved JPMorgan to act as the escrow agent for the PCMTF (Transmittal 8). Harbor Department staff recommends that the Board concur with HCBF's selection of JPMorgan to become the new independent financial manager for the PCMTF.

PCMTF Transfers - As required in the Operating Agreement, all PCMTF transfer requests by HCBF must be accompanied by signed approval of said disbursement by the Harbor Department Executive Director or authorized Deputy Executive Director, or by copy of official minutes indicating Board approval without veto action by the Los Angeles City Council, attested by the Board Secretary. Upon Board approval of JPMorgan as the PCMTF's new independent financial manager, all the funds being held by CCF would need to be transferred to a newly created JPMorgan account. The Executive Director or his designee will execute a joint letter with HCBF to approve the transfer of all remaining funds held in the trust fund, approximately \$7,780,671, in one lump sum payment from the CCF to JPMorgan.

In accordance with the Operating Agreement and the required documents to establish the new Port Community Mitigation Trust Fund account at JPMorgan, staff recommends the Board approve the Harbor Department Executive Director and Deputy Executive Directors as signatories for disbursements from the PCMTF (Transmittal 9).

ENVIRONMENTAL ASSESSMENT:

The proposed action is approval of the HCBF CY 2014 Operating Budget and independent financial manager of the PCMTF. 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:

Approval of the proposed budget will support approximately 4 full-time direct jobs in the five-county region.

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FINANCIAL IMPACT:

On September 30, 2013, the balance of the PCMTF was \$7,780,671 (Transmittal 5). The approved HCBF operating budget for CY 2013 is \$499,200. Transmittals 2a and 2b summarizes the transfer of funds from the PCMTF to HCBF and details the projects and amounts spent in its attached internal financial reports. The proposed HCBF CY 2014 Operating Budget (Transmittal 2c) anticipates an increase from the HCBF CY 2013 Operating Budget amount by 2.5%, or \$12,500, for a total amount of \$511,700. This total amount consists of a transfer from the PCMTF, currently held at the CCF, in the amount of \$475,000 coupled with the projected \$36,700 surplus from the HCBF CY 2013 Operating Budget. There will be no financial impact to the Harbor Department as all PCMTF funds are held by the independent financial manager.

Separately, the proposed move to JPMorgan will have a greater impact on the balances of the PCMTF given the proposed increased level of risk associated with the majority of the funds that have been selected to be used as investment vehicles. While there will be no financial impact to the Harbor Department as all PCMTF funds are held by the independent financial manager, the investment returns of the funds at the PCMTF will vary either more positively or negatively.

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CITY ATTORNEY:

The Office of the City Attorney has reviewed and approved the requested transfer with the one condition as to form and legality including conformance with the TraPac MOU and Operating Agreement.

TRANSMITTALS:

1. TraPac Memorandum of Understanding
2. Operating Agreement of the TraPac Memorandum of Understanding
3. HCBF Audited 2012 Financial Statements
4. HCBF 2013 & 2014 Operating Budget Comparison
5. Request from the Harbor Community Benefit Foundation Operating Budget, YE December 31, 2014 and PCMTF Transfer
6. CCF Quarterly Report September 30, 2013
7. J.P. Morgan Bank Portfolio Recommendation
8. HCBF Board Approval of J.P. Morgan Bank
9. Resolution Appointing Harbor Department Signatories to Harbor Community Benefits Foundation Account with J.P. Morgan

FIS Approval: _____ (initials)
CA Approval: _____ (initials)

APPROVED:

CYNTHIA M. RUIZ
Deputy Executive Director, External Relations

GARY LEE MOORE, P.E.
Interim Executive Director