



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

**DATE: DECEMBER 3, 2009**

**FROM: MARKETING DIVISION**

**SUBJECT: RESOLUTION NO. \_\_\_\_\_ LOS ANGELES HARBOR  
DEPARTMENT CALENDAR YEAR 2010 CONTAINER CUSTOMER  
INITIATIVES**

**SUMMARY:**

In 2009, the Board of Harbor Commissioners (Board) approved various incentive programs to maintain the Los Angeles Harbor Department's (Harbor Department's) competitive position in the marketplace, to assist our container terminal customers (customers) during the economic crisis, and to help them maintain their current market share. Customers consist of APM Terminals, China Shipping Holding, Eagle Marine Services, Evergreen America, TraPac, Yang Ming Line, and Yusen Terminals, Inc. Although there are signs of economic recovery, customers continue to suffer from low cargo volumes and reduced revenues. At the same time, there is concern that container cargo may be diverted to other ports as competition to retain volume continues. For Calendar Year (CY) 2010 the Harbor Department staff has identified (i), an economic relief program that will provide each customer with a one-time credit in the amount of 6 percent of revenue paid in Fiscal Year (FY) 2007/2008, and (ii) two additional programs aimed at addressing commercial and competitive concerns. These programs can be implemented without compromising the operational and capital improvement budgets. Harbor Department staff recommends a one-time container terminal rent credit, an empty container discount, and a reduction in the trans-shipment rate.

Total Harbor Department operating revenues impacted, if all of the programs recommended are approved, are approximately \$25,773,029 with \$22,748,029 affecting the revenues for FY 2009/2010 and the remaining \$3,025,000 potentially reducing projected revenues in FY 2010/2011.

**RECOMMENDATION:**

It is recommended that the Board of Harbor Commissioners:

1. Approve the one-time container terminal rent credit, empty container discount, and trans-shipment reduction as described in this Board report and instruct staff to prepare individual permits as required to implement; and
2. Adopt Resolution No. \_\_\_\_\_.

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**DISCUSSION:**

Background – In late 2008 and throughout 2009, customers were faced with an unexpected change in economic conditions where Asia-United States container trade volumes plummeted, negatively impacting the Harbor Department's volumes. In addition to lower cargo volumes, worldwide vessel capacity increased, forcing ocean freight rates to decline. As a result, vessels are sitting unused. Many shipping lines have required financial assistance from their parent companies or their respective governments. The Harbor Department has experienced a port-wide 15.4 percent decline in container volumes year-to-date 2009 versus the same period in 2008.

In early 2009, the Board approved a series of financial incentive programs to benefit our customers. On February 19, 2009, the Board approved the Intermodal Container Discount Program, which provided a 10 percent discount to customers on every intermodal container moving through their container terminal between January 1, 2009, and December 31, 2009. On March 19, 2009, the Board approved the Inland Points Intermodal Incentive Program, which created an incentive for eligible Ocean Common Carriers (carriers) that increased the amount of intermodal containers moved through the Port of Los Angeles (Port). Any incremental container volume moved through the Port between May 1, 2009, and April 30, 2010, over and above container volumes moved through the Port between May 1, 2008, and April 30, 2009, would have been eligible to receive a \$20 per twenty-foot equivalent unit (TEU) incentive. Finally, during 2009, the Board approved various lease amendments for the customers that provided for a 50 percent rate reduction on up to 6 acres of space assignments. The amendments will expire on December 31, 2009.

To date, each of the aforementioned incentive programs provided customers with operating cost relief during the economic crisis. The following amounts represent the estimated financial impact of these programs on the operating revenues of the Harbor Department:

- Intermodal Container Discount Program: \$13,000,000 reduction.
- Inland Points Intermodal Incentive Program: If volume attained, the program would be additive to revenues but the magnitude is unknown.
- Fifty percent Rate Reduction on up to 6 acres of space assignment (all Customers): \$1,800,000 reduction.

The total estimated operating cost relief provided to Customers by the end of CY 2009 is estimated to be \$14,800,000.

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Need for Resolution –

- Economic Relief:
  - The Harbor Department received numerous requests by its customers to provide temporary rental relief during this economic downturn, which is predicted to continue into 2010. Therefore, Harbor Department staff recommends a one-time 6 percent rent credit based on our customers' total operating revenues paid to the Harbor Department during FY 2007/2008. The credit is proposed to be issued between January 1, 2010, and June 30, 2010. It is estimated that the operating revenue reduction to the Harbor Department and simultaneous cost relief to the customers is expected to be \$19,273,029. To effectuate this credit, the Harbor Department is recommending amendments to each customer's permit.
  
- Commercial Issues:
  - Currently, Port of Los Angeles Tariff No. 4 (Tariff), Section Five, Item 550-031 contains an empty container rate of \$9.33 per 20 foot container, \$18.74 per 40 foot container and \$24.13 per 45 foot container or larger. However, when permits were initially negotiated with customers, a blended TEU rate was established factoring in the number of loaded and empty containers. The number of empty containers considered in these blended TEU rates was approximately 20 percent. Over time, with import volumes increasing at rapid rates and the imbalance of trade, empty container volumes may exceed 20 percent of our customer's total volumes. During CY 2008 and CY 2009, Port-wide empty containers accounted for 25 percent and 23 percent, respectively, of total (loaded and empty) container volumes.

To remain competitive in the marketplace, as other ports in the United States differentiate their wharfage rates for loaded and empty containers, Harbor Department staff recommends an empty container discount. If a customer's empty TEU volume exceeds 20 percent of its overall TEU volume (loaded containers and empty containers), the incremental empty TEU volume is subject to be charged at the current tariff rate. Some customers have enjoyed an empty container rate in their current or past permits. By approving the proposed amendments to those remaining customers, all customers would be enjoying the same cost relief. Should the tariff rates change in the future, including empty rates, the customers at all times will be subject to these adjustments. The estimated yearly operating revenue loss to the Harbor Department and cost relief to the

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customers will be approximately \$5,500,000. To address this empty discount program, the Harbor Department is recommending amendments to each customer's permit commencing January 1, 2010, and ending December 31, 2010, unless extended.

Trans-shipment merchandise is merchandise that remains in an ocean carriers' possession and is transferred from one vessel to another within the Port. Currently in Tariff No. 4, Section Five, Item 515, the rule for trans-shipment merchandise states that a "single wharfage charge only will be assessed on the inbound movement." Recently the Port of Long Beach took action and modified their tariff by deducting 50 percent off the single wharfage rate for trans-shipped merchandise. In order to remain competitive in the marketplace, Harbor Department staff recommends harmonizing with the Port of Long Beach and reducing our rate by 50 percent off the single wharfage rate for trans-shipped merchandise. The estimated yearly operating revenue loss to the Harbor Department and concomitant cost relief to the customers is expected to be approximately \$550,000. To implement this incentive, the Harbor Department is recommending amendments to each customer's permit commencing January 1, 2010, and ending December 31, 2010, unless extended.

Need for Approval – These programs will allow the Harbor Department to assist its customers by providing operating cost relief during this difficult economic period and serve to support the Harbor Department's efforts towards continued equity with other U.S. ports in order to remain competitive in the marketplace.

Harbor Department Fiscal Requirements – The total estimated cost of these programs is a reduction of approximately \$25,773,029 to operating revenues.

**ENVIRONMENTAL ASSESSMENT:**

The proposed action is a financial program aimed at preventing cargo diversion to other ports. The proposed action will not allow customers to exceed the current terminal capacity and operations will remain consistent with existing lease provisions. As such, the action is exempt from the requirements of the California Environmental Quality Act (CEQA) in accordance with Article II, Section 1 of the Los Angeles City CEQA Guidelines.

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**ECONOMIC BENEFITS:**

The movement of containerized cargo through the Port supports over 30,000 direct jobs and 50,000 indirect jobs in the five-county region. The economic benefit of this program will be the preservation of these existing jobs, some of which would be lost if cargo is diverted to competing ports.

**FINANCIAL IMPACT:**

Costs and/or Revenue Impact – The total cost of these programs is projected to be approximately \$22,748,029 for the current FY 2009/2010. This is comprised of approximately \$19,723,029 for the container terminal rent credit, \$2,750,000 for the Empty Container Discount Program, and \$275,000 for the trans-shipment container wharfage discounts. These amounts will be charged against the ongoing revenues generated from the customers with the net effect of reducing the overall revenues to the Harbor Department when netted against the budgeted operating revenue amount for FY 2009/2010.

For FY 2010/2011, it is projected as the empty and the trans-shipment discounts continue for the first six months of that fiscal year, revenues will be reduced by another \$3,025,000, \$2,750,000 for the empty discount and \$275,000 for the trans-shipment program. At the current level of operating revenues and at the current projected pace of operating revenue generation and operating expense spending, it is estimated that with these discount programs, the Harbor Department will continue to be able to exceed its debt service coverage policy of 2.0X for the current and next fiscal year. It may be required that as the FY 2010/2011 budget is constructed, the \$3,025,000 reduction in operating revenues will need to be offset by an increase in projected operating revenues or decrease in operating expenses.

In providing the rent credit program, the discount is not expected to reduce the level of payments from any of the operators such that the total revenues received will sink below the minimum annual guarantee (MAG) amounts set for each customer. If in the event the rent credit program creates an amount that would appear to violate the MAG amount for the year, provision may be made to defer the amount of the credit to a subsequent FY or years until such credit is fully given in order to meet the MAG of the current year.

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Alternatives Considered – A variety of customer discounts and incentives have been considered. In addition to those outlined above, single operator discounts, incremental volume incentives, intermodal discounts, and the continuance of using the existing rate structure that provides reduced TEU charges when volumes exceed certain thresholds have also been considered. The proposed programs are being presented for consideration given their relative fairness to the terminal operators and the ease of administration.

Benefits of Funding – With all others things being equal, any reduction to revenues reduces the cash flow to the Harbor Department. By undertaking the above programs, the Harbor Department provides financial assistance to its major customers in a difficult economic environment. Central to the discount programs is being cognizant of the economic challenges faced by the largest contributors to the Harbor Department's revenues. The seven major terminal operators that will primarily benefit from this program generate approximately 75 percent of the total operating revenues the Harbor Department receives in any given FY. Recognizing that level of revenue contribution, the Harbor Department demonstrates tangibly its recognition of its main customers' difficulties. In the long term these actions seek to retain and perhaps increase economic benefit to the Harbor Department and the community.

Financial Impact if Not Approved – With shipping revenues budgeted to be approximately \$311,000,000 for this FY, not approving these actions will likely allow the Harbor Department to be on track to maintain that level of revenues. This would also likely be true for the FY 2010/2011 operating budget as the empty and trans-shipment programs are for CY 2010 and would affect the first six months of revenue for the next fiscal year. There is no guarantee that volumes of TEUs will be maintained with these actions.

Sources of Funding – No funds are being requested as the discounts will be applied as a credit against revenues.

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**CITY ATTORNEY:**

Any amendments presented to the Board to implement the programs referenced herein will be approved as to form by the Office of the City Attorney.

FIS Approval: KP (initials)

  
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FOR KATHRYN McDERMOTT  
Deputy Executive Director

APPROVED:

  
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