



BPC Policy No. 117

SUBJECT: OPERATING RESERVE POLICY

PURPOSE: The purpose of this policy is to establish general guidelines for the establishment, maintenance, and use of an operating reserve.

POLICY STATEMENT:

Operating reserves (i.e., cash reserves) are a measurement of sound fiscal management. Operating reserves generate investment income, provide a margin of safety and stability to protect the Port from exposure to catastrophic events and economic impacts, and provide flexibility to pursue emergent opportunities. To ensure long-term financial sustainability, the San Diego Unified Port District shall establish and endeavor to maintain an operating reserve balance that is available at the end of each fiscal year in an amount equal to six months of budgeted operating and maintenance expenditures.

PROCEDURE:

1. Establishing the operating reserve balance
 - a. The operating reserve balance shall be established annually upon the adoption of the fiscal year budget.
 - b. The dollar amount of the operating reserve balance shall be one-half the sum of budgeted operating and maintenance expenses minus budgeted expenses for the SDCRAA Harbor Police Service Level Agreement and any other operating expense for which a separate reserve exists.
 - c. The operating reserve balance includes a \$20 million minimum required operating reserve balance, which is established for the purpose of self-insurance against possible losses that could occur as the result of a catastrophic event (i.e., a natural or man-made disaster).
2. Maintaining the operating reserve balance
 - a. At least annually, Financial Services staff will forecast cash inflows and outflows over a five-year period to evaluate the sufficiency of the target operating reserve balance over the forecast horizon.

- b. Financial Services staff will present the results of the cash flow forecast to the Senior Management Team and discuss the target operating reserve balance over the forecast horizon.
- c. In the event that forecast cash inflows are insufficient to maintain the target operating reserve balance, staff will propose strategies to replenish the operating reserve balance, which include using one-time revenues, reducing expenses, suspending programs not linked to strategic goals, increasing revenues, or any combination of those strategies.
- d. At no time, except due to the occurrence of a catastrophic event, shall the operating reserve balance be allowed to fall below the \$20 million minimum required operating reserve balance without approval by the Board of Port Commissioners.

3. Uses of the operating reserve balance

- a. Operating reserves above the \$20 million minimum required operating reserve balance are authorized for use for the following purposes and in accordance with the following criteria.
 - i. A project is needed to comply with a current regulatory requirement or legal mandate.
 - ii. Cash flow requirements

Temporarily needed as a result of unfavorable financial performance due to the impact of an unfavorable economic environment.
 - iii. Major maintenance
 - 1. Project is necessary for the preservation of prior capital investment or an existing revenue stream; or
 - 2. Project costs exceed initial estimates due to higher than expected construction or material costs or an unforeseen problem during construction; or
 - 3. Project is scheduled to commence in a future fiscal year but is critical to complete earlier than planned.

iv. Capital development

Project is directly linked to and strongly supports one of the Port's strategic goals and is needed to start, resume, accelerate, or augment a currently approved Capital Development Program project.

v. Emergent opportunities

1. Directly benefits the Port by:
 - a. Creating a new revenue stream; or
 - b. Significantly enhancing an existing revenue stream; or
 - c. Preserving an existing revenue stream; or
 - d. Strengthening the Port's financial performance; and
2. Project payback is five years or less.
- b. Except in the case of a catastrophic event and in accordance with the San Diego Unified Port District Act § 58 "Suspension of Rules and Regulations in Emergencies; Emergency Regulations," any use of the \$20 million minimum required operating reserve balance requires approval by the Board of Port Commissioners.
4. The balance in the operating reserve shall be reported quarterly as necessary. Use of the operating reserve balance in no way contradicts, nullifies or usurps any other Board Policy, including but not limited to, BPC 110, "Procedure for the Administration of Contracts, Agreements, and the Purchasing of Supplies, Materials, and Equipment."

RESOLUTION NUMBER AND DATE: 2009-128, dated July 7, 2009

(1)

Re Adoption of BPC Policy 117,]
Operating Reserve Policy]
_____]

REFERENCE
COPY
55299

RESOLUTION 2009-128

BE IT RESOLVED by the Board of Port Commissioners of the San Diego Unified Port District, as follows:

That Board of Port Commissioners Policy No. 117, Operating Reserve Policy, a copy of which shall be placed on file in the office of the District Clerk, is hereby adopted.

ADOPTED this 7th day of July, 2009.

sw
7/7/09

(6)

AGENDA ITEM 27**SAN DIEGO UNIFIED PORT DISTRICT****DATE:** July 7, 2009

REFERENCE

COPY

55299

**SUBJECT: RESOLUTION ADOPTING BOARD OF PORT COMMISSIONERS (BPC)
POLICY REGARDING AN OPERATING RESERVE****EXECUTIVE SUMMARY:**

The Board of Port Commissioners (Board) requested that it adopt a written policy regarding the establishment, maintenance, and use of an operating reserve.

RECOMMENDATION:

Resolution adopting Board of Port Commissioners Policy regarding an operating reserve.

FISCAL IMPACT:

This proposed Board action has no direct fiscal impact. The application of this policy will have fiscal impacts on a case by case basis.

COMPASS STRATEGIC GOALS:

This agenda item supports the following strategic goal through its linkage to the objective of maintaining the Port's financial stability.

- ☐ Promote the Port's maritime industries to stimulate regional economic vitality.
- ☐ Enhance and sustain a dynamic and diverse waterfront.
- ☐ Protect and improve the environmental conditions of San Diego Bay and the Tidelands.
- ☐ Ensure a safe and secure environment for people, property and cargo.
- ☐ Develop and maintain a high level of public understanding that builds confidence and trust in the Port.
- ☐ Develop a high-performing organization through alignment of people, process and systems.
- ☒ Strengthen the Port's financial performance.
- ☐ Not applicable.

DISCUSSION:**Background**

On April 26, 1994, the then existing Capital Improvements Program Ad Hoc Committee (Committee) presented to the Board seven recommendations regarding non-airport

ACTION TAKEN: 07-07-2009 - Resolution 2009-128

AGENDA ITEM 27**Page 2 of 3**

projects and financing options. One of the Committee's recommendations was that the Board "...adopt a reserve policy which establishes and maintains, as a minimum, a reserve equal to six month's non-airport operating and maintenance expense requirements." Another recommendation was direction to "...staff to prepare for Committee review and recommendation to the Board, a reserve utilization strategy that would enable the Port to increase funds available for CIP requirements without jeopardizing the Port's financial integrity."

While the minutes show that the Board approved both recommendations, there is no record that either a written reserve policy or a reserve utilization strategy was ever presented to or adopted by the Board. Despite the lack of an adopted reserve policy, it has been the Board's practice since that time to maintain a reserve equal to six month's "non-airport" operating and maintenance expense requirements.

At the February 12, 2008 Capital Development Program (CDP) Workshop, the question as to the appropriate level of operating reserves was posed and, as a follow-on to this question, the Board directed staff to provide additional information concerning the appropriateness of the Port's six-month operating reserve practice. Staff submitted a memorandum to the Board on March 21, 2008 that responded to these two questions.

At the January 5, 2009 Board retreat, the Board requested that staff recommend criteria for using the operating reserve.

Proposed Operating Reserve Policy

Staff has developed, and submits for the Board's review and approval, a policy establishing general guidelines for the establishment, maintenance, and use of operating reserves.

Consistent with the Board's fiscal prudence, the proposed policy:

- Establishes an operating reserve in an amount equal to six months budgeted operating and maintenance expenses.

The operating reserve amount reflects a responsible approach to managing the Port's exposure to natural or man-made disasters, supporting forecasted cash flow requirements over the next five years, and responding to adverse fiscal conditions.

- Establishes, within the operating reserve, a minimum balance of \$20 million that may only be used in the event of a catastrophic emergency or with Board approval.

The \$20 million operating reserve "floor" represents expected cash requirements needed in the event of an earthquake or other catastrophic emergency. With respect to earthquake damage, the Port previously carried insurance that would cover \$15 million of an estimated maximum probable loss of \$70 million. The Port

AGENDA ITEM 27**Page 3 of 3**

is now self-insured for damage resulting from an earthquake and requires at least this level of cash reserves to begin rebuilding revenue producing assets. To ensure the Port maintains this minimum reserve level, any use of the \$20 million operating reserve "floor" requires Board approval.

- Defines how the reserve balance will be maintained:

Maintaining cash reserves is of paramount importance. On an annual basis, the Senior Management Team will review forecasted cash inflows and outflows over a five-year period and evaluate the sufficiency of the target operating reserve balance. The Senior Management Team will propose strategies to replenish operating reserves if net cash flows at the end of the forecast horizon are lower than the target operating reserve balance.

- Identifies approved uses of the operating reserve:

The operating reserves may be used for a variety of purposes, including temporary cash flow needs, major maintenance expenses, capital projects that are approved, but are either unfunded or under funded, or capital projects needed to comply with regulatory requirements. Operating reserves above the \$20 million "floor" may also be used for emergent opportunities, with priority given to projects that either create, enhance, or preserve a revenue stream, or strengthen the Port's financial performance.

Port Attorney's Comments:

The Port Attorney has reviewed and approved the requested document for form and legality.

Environmental Review:

This proposed Board action is not subject to CEQA, as amended.

Equal Opportunity Program:

Not applicable.

PREPARED BY: Janice Erickson
Director, Financial Services



BPC Policy No. XXX

SUBJECT: OPERATING RESERVE POLICY

PURPOSE: The purpose of this policy is to establish general guidelines for the establishment, maintenance, and use of an operating reserve.

POLICY STATEMENT:

Operating reserves (i.e., cash reserves) are a measurement of sound fiscal management. Operating reserves generate investment income, provide a margin of safety and stability to protect the Port from exposure to catastrophic events and economic impacts, and provide flexibility to pursue emergent opportunities. To ensure long-term financial sustainability, the San Diego Unified Port District shall establish and endeavor to maintain an operating reserve balance that is available at the end of each fiscal year in an amount equal to six months of budgeted operating and maintenance expenditures.

PROCEDURE:

1. Establishing the operating reserve balance
 - a. The operating reserve balance shall be established annually upon the adoption of the fiscal year budget.
 - b. The dollar amount of the operating reserve balance shall be one-half the sum of budgeted operating and maintenance expenses minus budgeted expenses for the SDCRAA Harbor Police Service Level Agreement and any other operating expense for which a separate reserve exists.
 - c. The operating reserve balance includes a \$20 million minimum required operating reserve balance, which is established for the purpose of self-insurance against possible losses that could occur as the result of a catastrophic event (i.e., a natural or man-made disaster).
2. Maintaining the operating reserve balance
 - a. At least annually, Financial Services staff will forecast cash inflows and outflows over a five-year period to evaluate the sufficiency of the target operating reserve balance over the forecast horizon.

- b. Financial Services staff will present the results of the cash flow forecast to the Senior Management Team and discuss the target operating reserve balance over the forecast horizon.
 - c. In the event that forecast cash inflows are insufficient to maintain the target operating reserve balance, staff will propose strategies to replenish the operating reserve balance, which include using one-time revenues, reducing expenses, suspending programs not linked to strategic goals, increasing revenues, or any combination of those strategies.
 - d. At no time, except due to the occurrence of a catastrophic event, shall the operating reserve balance be allowed to fall below the \$20 million minimum required operating reserve balance without approval by the Board of Port Commissioners.
3. Uses of the operating reserve balance
- a. Operating reserves above the \$20 million minimum required operating reserve balance are authorized for use for the following purposes and in accordance with the following criteria.
 - i. A project is needed to comply with a current regulatory requirement or legal mandate.
 - ii. Cash flow requirements
 - Temporarily needed as a result of unfavorable financial performance due to the impact of an unfavorable economic environment.
 - iii. Major maintenance
 - 1. Project is necessary for the preservation of prior capital investment or an existing revenue stream; or
 - 2. Project costs exceed initial estimates due to higher than expected construction or material costs or an unforeseen problem during construction; or
 - 3. Project is scheduled to commence in a future fiscal year but is critical to complete earlier than planned.

iv. Capital development

Project is directly linked to and strongly supports one of the Port's strategic goals and is needed to start, resume, accelerate, or augment a currently approved Capital Development Program project.

v. Emergent opportunities

1. Directly benefits the Port by:

- a. Creating a new revenue stream; or
- b. Significantly enhancing an existing revenue stream; or
- c. Preserving an existing revenue stream; or
- d. Strengthening the Port's financial performance; and

2. Project payback is five years or less.

- b. Except in the case of a catastrophic event and in accordance with the San Diego Unified Port District Act § 58 "Suspension of Rules and Regulations in Emergencies; Emergency Regulations," any use of the \$20 million minimum required operating reserve balance requires approval by the Board of Port Commissioners.
4. The balance in the operating reserve shall be reported quarterly as necessary. Use of the operating reserve balance in no way contradicts, nullifies or usurps any other Board Policy, including but not limited to, BPC 110, "Procedure for the Administration of Contracts, Agreements, and the Purchasing of Supplies, Materials, and Equipment."

RESOLUTION NUMBER AND DATE: 2009-XX dated July 7, 2009