Port of Port Angeles

Port Angeles, Washington

Commissioners' Resolution No. 10-999

A RESOLUTION OF THE PORT OF PORT ANGELES ESTABLISHING GUIDELINES FOR CAPITAL IMPROVEMENT POLICIES

WHEREAS, the Port of Port Angeles' (Port) mission is to be the primary leader in economic development in Clallam County by marketing and developing properties for the long-term benefit of Port District stakeholders while fulfilling the Port's environmental stewardship role; and

WHEREAS, the Port Commission is committed to pursuing those capital investments which:

A. Create Family Wage Jobs;
B. Promote sustainable environmental practices;
C. Generate adequate Return on Investment in the long-term.

WHEREAS, the Port Commission is charged with providing capital investment guidance sufficient to facilitate sound financial choices and to meet the objectives outlined in the Port's Strategic Plan; and

WHEREAS, the capital investment guidance will address the formulation of (a) the Port's long-term Five Year Capital Improvement Plan, (b) the yearly Capital Improvement Plan within the annual budget, and (c) Project Financing and Evaluation programs,

NOW THERFORE, BE IT RESOLVED, by the Port Commission of the Port of Port Angeles, as follows:

The Capital Improvement Policies of the Port of Port Angeles as set forth in Exhibit A attached to this resolution and by this reference incorporated herein, is adopted for the purpose of establishing the Capital Improvement Policies of the Port of Port Angeles.

Port of Port Angeles

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Commissioners' Resolution No. **10-999** cont'd

ADOPTED by the Port Commission of the Port of Port Angeles this 12th day of July, 2010 and duly authenticated in open session by the signatures of the Commissioners voting in favor thereof and the Seal of the Commission duly affixed.

PORT OF PORT ANGELES
PORT COMMISSION

George H. Schoenfeldt, President

Jim McEntire, Vice President

John M. Calhoun, Secretary

Exhibit "A"

Capital Improvement Policies

A. Five Year Capital Improvement Plan

This is a five-year projection of the port's capital investment needs. Capital improvements are defined as expenditures with a value in excess of $1,000 and an expected life of more than five years.

1. Types of Capital Improvements

    a. New Revenue Generating Improvements are developed for a specific purpose or customer(s) that will result in a new revenue stream.

    b. Replacements of Revenue Generating Improvements are developed to renovate or replace obsolete or aging revenue-producing assets. These projects serve to extend existing revenue streams and may offer additional revenue if replacements enhance the efficiencies of operations or offer additional capabilities or value.

    c. Infrastructure Improvements generally do not directly generate revenue, although they may indirectly benefit a revenue-generating project. These projects are developed to support multiple or future customers or to enhance public infrastructure. Examples are public access areas, roads, bridges, public parking.

    The Port may decide to limit its investment in Infrastructure Projects due to funding sources. Infrastructure Projects have a cumulative effect on future growth without generating adequate returns.

2. Priorities of Capital Improvements

    a. Planned projects are ready to proceed. These projects have customer commitment, permits and are likely to progress this budget year. The Port has reviewed these projects and they meet or exceed its "triple bottom line" requirements, as defined below. These projects will form the bulk of the Port's annual Capital Improvement Plan.

    b. Projected projects identify a business need or opportunity; however, these projects have not been fully developed in scope, cost or permits. These projects are part of the long-term Capital Improvement Plan.

    c. Potential projects are in the conceptual stage with very rough cost estimates. These projects lack customer commitment, permits and design. These projects are part of the long-term Capital Improvement Plan.

B. <u>Annual Capital Improvement Plan (Annual Budget)</u>

1. Alignment of Capital and Operating Budgets

   The Annual Capital Improvement Plan is an important outcome of the long-term Capital Improvement Plan. It also aligns capital needs with resources generated by operating divisions; more specifically, the annual Capital improvement Plan considers the cash flows generated by capital projects with their costs and related ongoing financing requirements.

   The annual Capital Improvement Plan implements the current year spending plan for capital projects. While individual capital projects expenditures will require Commission authorization before they proceed, projects in this Plan are budgeted to be undertaken.

2. Capital Improvement Objectives

   a. "Triple Bottom Line" measures the Capital Budget and individual capital projects delivery on the Port's Mission Statement.

      i. <u>Job Creation</u>

         1. Family Wage Jobs – a job that generates enough income to support a spouse and dependents in Clallam County
         2. Community Enhancement
         3. Alignment with local government goals

      ii. <u>Environmental Stewardship</u> – Port projects will promote sustainable environmental practices. These projects endeavor to do no harm and curtail environmental impact. The Port will build projects that minimize consumption of energy and non-renewable items.

      iii. <u>Return on Investment</u>

         1. <u>Minimum Return on Investment objectives</u> were discussed at the August 9, 1996 Commission meeting. At that meeting, the following minimum ROI objectives were presented:

            - Return on vacant land should range from 8 % to 10% or higher
            - Return on improvements and buildings should be 12 % or higher

         2. <u>Economic Profit</u> is a financial performance method that calculates the true economic profit of an entity. Economic Profit can be calculated as net operating profit minus a charge for the opportunity cost of the capital investment. Economic Profit is an estimate of the amount by

which earnings exceed or fall short of the required minimum rate of return. Economic Profit measures the difference, in monetary terms, between the return on the Port's capital and the cost of that capital.

3. Revenue Bond Debt Service Coverage is the number of times revenue bond debt service (principal plus interest) could be paid with net revenues available for debt service (revenue minus operating, maintenance and administration expense excluding depreciation). A revenue bond issue has a mandatory coverage covenant ranging from 1.00 to 1.35 times coverage depending on its lien level.

4. Financial Capacity – defined as ability to borrow to build customer facilities based on the financial strength of the Port.

C. Capital Improvement Financing Criteria

1. Alignment with funding sources – there are several sources of financing capital improvements; the most common sources include:

   a. Cash from Operations
   b. Reductions in Reserves
   c. Cash from Tax Levy
   d. Issuance of Revenue Bonds
   e. Issuance of General Obligation Bonds
   f. Grants

   In general, the Port will attempt to match the outflows of cash on projects with the cash inflows from funding sources.

   The Commission intends to restrict tax levy proceeds to the following uses:
   (1) Payment of debt service incurred in funding of capital investments; or
   (2) Funding of current or future years' capital improvements.

   The Commission does not permit the use of tax levy proceeds for operational purposes.

2. Tracking multi-year projects - many Port projects require more than one calendar year to complete. When the Commission has approved a multi-year project in a prior year and the project still is in process, the budget and spending to date roll forward into the current year Capital Budget.

3. Capital Budget Financing – The financing costs of all projects (current year as well as projects approved in prior years) will be presented to the Commission on a Port-wide basis for the current budget year.

   a. Debt Policy – to be discussed in a future resolution and policy
   b. All projects will be examined to determine the appropriate type of financing, record debt issued, construction fund

spending, and term of the debt. In all situations, term of debt will be less than estimated project life.

D. <u>Capital Improvement Evaluation Process</u>

1. Capital Project Evaluation – provides a basis for approving a project for inclusion in the Capital Improvement Budget as well as reviewing status of projects over a longer term.

   a. Timing

      i. Capital Improvements should be evaluated in terms of cash flow before being approved in the annual capital budget
      ii. Potential Projects should be reassessed during customer lease negotiations
      iii. Potential Projects should be again reassessed before Commission approval of lease
      iv. Projects should be evaluated annually after being put into service for accountability and learning for seven years. These Projects should be in excess of the threshold (currently $50,000) established in Port Resolution # 10-993 and any future resolution modifying such limit.

   b. Methodology

      i. Estimate relevant cash outflows and inflows for project.
      ii. Calculate the investment's economic worth and/or NPV.
      iii. Compare the investment's economic worth to your acceptance criteria or "hurdle rate". See Exhibit B

   c. Measurement Criteria

      i. Return on Investment Alternatives:

         <u>Net Present Value</u> discounts future cash flows by the Port's "hurdle rate" and compares that amount to the cost of the investment.

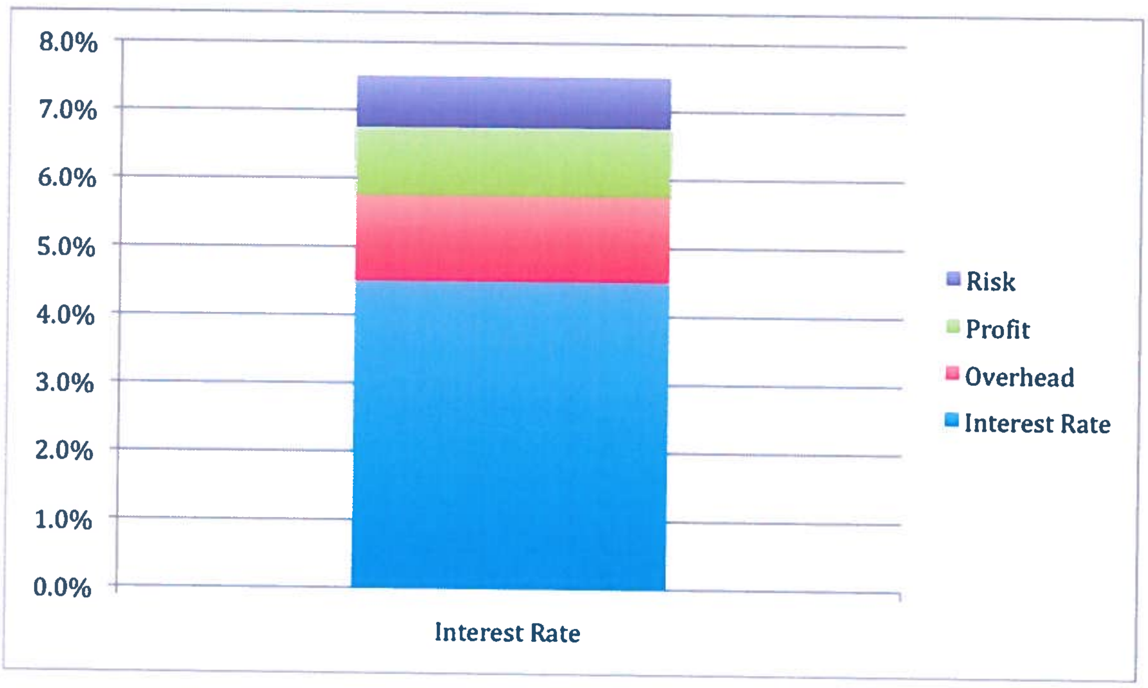
         <u>Internal Rate of Return</u> is the interest rate at which the present value of the cash flows equals the cost of the investment. A project's internal rate of return should be higher than the Port's "hurdle rate" to be accepted.

      ii. Jobs created, net.

      iii. Environmental Impact.

   d. Acceptance Criteria is a calculated interest rate based on the Port's cost of capital plus a factor for:

i. Profit
ii. Overhead
iii. Business risk



Example: Development of an Acceptance Criteria Interest Rate